



Department  
for Education

# **Cost of delivering the early education entitlement**

**Research report**

**November 2015**

**NLH Partnership**

## Research team

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# Executive Summary

## Introduction

This report presents the findings of a mixed method research study commissioned by the Department for Education to explore the costs to providers of delivering the free early education entitlement for 2, 3 and 4 year olds. The study focused on Private, Voluntary and Independent sector (PVI) childcare providers' experiences of delivering the free entitlement and the costs and unit costs of that delivery.

The study aimed to:

- Provide an analysis of the unit costs of delivering the free early education entitlement for 2, 3 and 4-year-olds.
- Explore the extent to which current funding rates are sufficient to enable the effective delivery of the free early education entitlement.
- Explore the capacity of PVI providers to expand their provision in response to any expansion of the entitlement, and any barriers to expansion.
- Explore the degree of any cross-subsidisation of the free entitlement, and the implications of this for any expansion of the free entitlement.
- Explore providers' ability to effectively deliver the free early education entitlement, barriers to effective delivery of the free entitlement, and how any barriers might be overcome.

## Methodology

The study used a mixed method approach to data collection and utilised the following data collection methods:

- In-depth, face-to-face qualitative interviews with representatives from PVI settings.
- Telephone interviews with representatives from PVI settings.
- Collection of a range of quantitative information from PVI settings' through the use of a pro forma completed by each participant PVI setting.

The study included data from 57 separate PVI settings, from 22 different local authority areas.

## Findings

Key findings from this study include:

## **Settings' finances**

- The largest single factor contributing to settings' total costs was 'staffing costs', which accounted for 73% of total costs.
- The majority of settings drew attention to their setting's sensitivity to changes in the cost of childcare staffing, and the implications of this for their setting's viability and sustainability.

## **Costs of delivering the free entitlement**

- Unit cost analysis indicated that the unit cost of delivering an hour of childcare for two-year-olds was £5.39, and for three- and four-year-olds was £3.51.
- 
- Unit costs of delivering childcare for both age groups were significantly greater for Voluntary and Community and Sector (VCS) settings than for privately-run settings.
- Analysis highlighted an average surplus in funding of £0.22 when settings' unit costs for delivering childcare for three- and four-year-olds were compared with local authority funding rates.
- Analysis highlighted an average shortfall in local authority funding rates for two-year-olds of £0.43.
- In terms of delivering childcare for three- and four-year-olds, 34% of settings experienced a shortfall in funding and 66% a surplus.

## **Subsidisation and cross subsidisation**

- The ability to sell additional childcare hours above the free entitlement was important to many settings, who felt that any reduction in their ability to cross-subsidise in this way would be detrimental to their setting's viability.
- A number of settings stated that they were subsidising the free entitlement through other services that they delivered as an organisation.

## **The ability to expand provision**

- Approximately one-third of settings stated that they would be both interested in, and able to, expand the amount of childcare that they offered either by expanding on-site or by taking on additional venues, settings or spaces.
- A key barrier to expansion highlighted by settings was the difficulty that they had found in recruiting suitably qualified or experienced staff.

- Findings suggest that there may be a significant amount of spare childcare capacity available within PVI settings, which could be utilised for the expansion of the free early education entitlement.

### **Barriers to effective delivery of the free entitlement**

- By far, the most frequently cited barrier to effective delivery of the free entitlement was settings' abilities to effectively support children with additional support needs within their settings. A number of settings stated that they faced significant challenges in effectively supporting children with additional support needs, and typically bore the cost of this support without adequate additional funding.
- This study highlighted the risk that some settings may limit the amount of two-year-old funded early education they provide because of additional costs incurred through providing unfunded additional support for children and families.
- This study highlighted a lack of flexibility in the way in which some settings offered the free early education entitlement to local parents.

### **The expansion to 30 hours**

- Findings suggest that the implications of expansion to 30 hour for settings will depend on a complex range of factors, including: occupancy rates; settings' current fee rates and how these compare with the local authority funding rate; number of hours typically sold by settings over and above the current free entitlement; and the mix of age ranges typically cared for within the setting.
- A key concern for settings regarding the expansion to 30 hours was the effect that it would have on their ability to generate revenue by selling additional hours of childcare.
- Many settings were concerned that an increase in the free entitlement to 30 hours would mean they would be able to offer childcare to fewer three- and four-year-olds, and fewer children overall.
- A number of preschool settings that offered fewer than 30 hours of childcare per week expressed concern about their ability to remain sustainable when the free entitlement is increased to 30 hours.

# 1 Introduction

This report presents the findings of a mixed method research study commissioned by the Department for Education to explore the costs to providers of delivering the free early education entitlement for 2, 3 and 4 year olds. The study focused on Private, Voluntary and Independent sector (PVI) childcare providers' experiences of delivering the free entitlement and the costs and unit costs of that delivery.

## 1.1 Background

In 1998 the Government introduced an entitlement to a free funded early education place (for 12.5 hours per week for 33 weeks per year) for all four-year-olds. This entitlement has been expanded significantly in subsequent years. In 2004 the entitlement was extended to include all three-year-olds, and in 2010, the number of free entitlement hours was expanded to 15 hours per week over 38 weeks per year (a total of 570 hours).

In September 2013, the free early education entitlement was extended to include the 20 per cent most 'disadvantaged' two-years-olds, who also became eligible for 15 hours of funded early education per week. This provision was extended to the 40 per cent most 'disadvantaged' two-year-olds in September 2014.

Two-year-olds are eligible to receive free early education if their family meets one of a number of criteria related to income level or receipt of benefits, or are receiving support through Part 6 of the Immigration and Asylum Act (1999). They are also eligible if they are a child looked after by the local authority, have a current statement of Special Educational Needs or an Education, Health and Care (EHC) plan, are entitled to Disability Living Allowance, or are no longer looked after by the local authority as a result of an adoption, special guardianship or child arrangements order.<sup>1</sup>

In addition, many local authorities provide free early education for two-year-olds who meet a number of additional, locally-defined criteria, for instance where children are subject to a Child Protection or Child in Need plan, where a Common Assessment Framework (CAF) is in place for a child, or where the child has otherwise been identified as being from a 'disadvantaged' background or living with circumstances that mean that s/he would potentially benefit from free early education from the age of two.

Local authorities have a statutory duty to secure free early years provision, and the free entitlement can be accessed through a range of providers, including local authority nurseries, nurseries within maintained schools, private, voluntary or independent (PVI) childcare providers, and childminders.

The revenue funding for the free entitlement is distributed to local authorities through the Dedicated Schools Grant (DSG) which authorities receive from the Department for Education. They are required to maximise the proportion of free education

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<sup>1</sup> DfE (2014) Early education and childcare: Statutory guidance for local authorities, Department for Education, September 2014

entitlement funding that they pass to providers, and to set local funding rates via an Early Years Single Funding Formula (EYSFF). Local authorities are able to decide how they fund early education providers locally, and have the flexibility to set different funding rates for different types of provision.

The funding rates received by childcare providers delivering the free entitlement vary from local authority to local authority. PVI childcare providers therefore receive different rates per hour of childcare provided, depending on the local authority in which their setting is located. In addition to a 'base rate' of funding, some local authorities also pay additional supplements or premiums to providers based on factors such as 'quality' (for example, to settings with an 'Outstanding' Ofsted grade) and 'deprivation' (for example, to settings located within particularly 'deprived' localities, or based on the circumstances of individual children receiving the free entitlement).

In May 2015, the Government announced an expansion in the number of free entitlement hours available for some three and four year olds. This expansion will mean that from September 2017 all 3 and 4 year olds of eligible working parents will receive 30 hours of free early education rather than the current 15 hours.

The expansion of the free entitlement to 30 hours takes place within the context of a wider debate about the sufficiency of local authority funding rates for the current 15-hour free entitlement, and the extent to which current rates delegated to settings by local authorities meet the costs that childcare providers incur in delivering free early education. This debate has been intensified by the announcement of the expansion to 30 hours of free funded early education.

## **1.2 Aims of the research**

In April 2015, the Department for Education commissioned NLH Partnership to conduct a small research study involving PVI childcare settings delivering the free early education entitlement. The study aimed to:

- Provide an analysis of the unit costs of delivering the free early education entitlement for 2, 3 and 4-year-olds.
- Explore the extent to which current funding rates are sufficient to enable the effective delivery of the free early education entitlement.
- Explore the capacity of PVI providers to expand their provision in response to any expansion of the entitlement, and any barriers to expansion.
- Explore the degree of any cross-subsidisation of the free entitlement, and the implications of this for any expansion of the free entitlement.
- Explore providers' ability to effectively deliver the free early education entitlement, barriers to effective delivery of the free entitlement, and how any barriers might be overcome.

## 2 Methodology

This chapter outlines the methodological approach used in this study.

### 2.1 Overview

The study used a mixed method approach to data collection and utilised the following data collection methods:

- In-depth, face-to-face qualitative interviews with representatives from PVI settings.
- Telephone interviews with representatives from PVI settings.
- Collection of a range of quantitative information from PVI settings' through the use of a pro forma completed by each participant PVI setting.

### 2.2 Sample

#### 2.2.1 Sampling

Due to the short timescales available for completion of the study, an opportunity sample of PVI settings was utilised. The NLH Partnership team has extensive networks and links within the early years sector, and these were used to select and make contact with a wide range of PVI providers who were then invited to participate in the study.

A list of potential participant settings was compiled, and representatives from these settings were then contacted by NLH Partnership to explore their interest in participating. Willingness to participate in the project was high, with more than eighty per cent of those selected and contacted to participate agreeing to take part.

Representatives from PVI settings were invited to take part in either an in-depth, face-to-face, qualitative interview, or a telephone interview. Further details about these methods can be found in section 2.3. Prior to participating in an interview, prospective interviewees were asked to complete a specially designed project pro forma which asked for a range of setting-related information, including descriptive information such as ownership, type of care delivered and size of setting, as well as information about settings' income, costs, and the number of hours of childcare delivered.<sup>2</sup> A copy of the pro forma can be found in Appendix 2.

In total, pro forma data from 57 separate PVI settings was collected for this project. This sample included PVI settings from 22 different local authority areas, which is particularly important given the range of funding rates in operation across authorities. A list of the 22 local authorities can be found in Appendix 1. Table 1 provides further details about the characteristics of settings for whom quantitative, pro forma data was collected. It shows that the sample included a broad mix of settings in terms of a range of variables, including geographical location, type of care provided, 'deprivation' level, size of setting, and ownership 'type' of setting.

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<sup>2</sup> Where a PVI provider operated more than one setting, the provider was asked to complete a single pro forma and provide quantitative information for only one of their settings.

The 57 settings that participated in this study were responsible for providing more than 3,000 childcare places, and delivering in excess of 1.2 million hours of free early education per annum.

**Table 1: Characteristics of participant PVI settings**

1 Region			6 Number of settings operated	
London	12		1 setting	34
East <sup>3</sup>	21		2-5 settings	18
South East	2		More than 6 settings	5
South West	5			
North West	2		7 Area deprivation level: IDACI <sup>5</sup>	
Yorkshire and Humber	11		30% most 'deprived'	23
East Midlands	4		70% least 'deprived'	34
2 Type of care provided			8 Ofsted grade	
Sessional only	15		Outstanding	17
Full day care	42		Good	35
			Requires improvement	1
3 Ownership type			Awaiting first inspection	2
Private	33		Not applicable <sup>6</sup>	2
Voluntary and Community Sector	21			
Independent School	3		9 Size of setting <sup>7</sup>	
			24 places or fewer	4
4 Age ranges cared for			25-48 places	24
All under 5 age ranges	30		49-72 places	15
Over 2s only	25		More than 72 places	14
3 and 4 year olds only	2			
			10 Urban/rural	
5 LAs within each quartile of LA average <sup>4</sup>			Urban	47
	2 year olds	3/4 year olds	Rural	10
1 <sup>st</sup> quartile	3	6		
2 <sup>nd</sup> quartile	4	5		
3 <sup>rd</sup> quartile	9	4		
4 <sup>th</sup> quartile	6	7		

Since an opportunity sample was utilised for this study, with the aim of including a broad mix of settings, the sample gained was not completely representative of PVI settings across England, in terms of all of the characteristics of settings listed in table 1.

For instance, in terms of 'Region', the sample included an over-representation of some regions (for example, London) and an under-representation of others (for example, the South East). It also included an over-representation of settings in the

<sup>3</sup> The sample included PVI settings from 7 different local authorities within the East region.

<sup>4</sup> The distribution of local authorities within the sample, in terms of quartiles of the average, England-wide, local authority funding rates to providers (Based on Department for Education 2014-15 s251 data).

<sup>5</sup> Based on Income Deprivation Affecting Children Index (IDACI), 2010

<sup>6</sup> Independent school settings without separate Ofsted gradings for childcare on non-domestic premises.

<sup>7</sup> Based on settings' maximum space capacity.

30% most 'deprived' areas, and a slight under-representation of privately-owned settings. A lack of sample representativeness in terms of these key setting characteristics had the potential to lead to biases that would adversely affect the validity of some of the study's findings.

With this in mind, for the unit cost calculations presented in section 3.3, the sample has been weighted so that it is representative of the England-wide distribution of PVI settings in terms of 'Region', 'Ownership type', and 'Area deprivation level'.

## **2.3 Methods**

Data collection was conducted during June and July 2015. The following sections provide further details about the data collection methods used.

### **2.3.1 In-depth, qualitative, face-to face interviews**

A total of 44 in-depth, qualitative, face-to-face interviews were conducted with representatives from PVI settings. Since the interviews were concerned with gaining a wide range of information, including information about the delivery of the free entitlement and the finances of settings, NLH partnership worked with settings to decide on the most appropriate representative/s to participate in interviews. A range of setting representatives participated in interviews, including owners and directors of privately-owned settings, nursery managers, business managers, administrative staff, book-keepers and finance managers, nursery practitioners, and senior managers from voluntary and community organisations.

Interviews were conducted with the aid of an interview topic guide developed to ensure that the key aims of the research project were addressed. Interviews lasted for between 45 and 100 minutes, with a typical interview lasting for approximately 70 minutes.

As stated earlier, representatives from settings who participated in this study were asked to complete a specially designed project pro forma prior to participating in an interview. Interviews involved an in-depth discussion of the pro forma information, and also allowed for the collection of in-depth information about settings' experiences of delivering the free entitlement.

In-depth interviews focused on a range of topics, including:

- The practical implementation and delivery of free early education within participants' settings.
- The costs for settings of delivering the free early education entitlement.
- The extent to which the funding rate received by the setting from their local authority is sufficient to enable the effective delivery of the free early education entitlement.
- The capacity of settings to expand their provision and any barriers to expansion.

- The potential impact for settings of the expansion of the free entitlement to 30 hours for working parents of 3 and 4 year olds.

All in-depth interviews were voice-recorded, and consent for this was gained from project participants prior to interviews commencing.

### **2.3.2 Telephone interviews**

In addition to in-depth, face-to-face interviews, 10 telephone interviews were conducted with PVI settings in order to gather quantitative, pro forma information from a larger number of settings than face-to-face interviews alone would allow, given the timescales for completion of the study.

These interviews focused on collecting project pro forma data rather than on gathering qualitative information from settings. However, interviews typically involved some discussions with setting representatives about their overall experience of delivering the free entitlement and any barriers that existed to effective delivery.

## **2.4 Ethical considerations**

Verbal informed consent was gained from all research participants prior to conducting any interviews. All participants were made aware of the nature and purpose of the study, how information they provided would be used, and assured that their anonymity would be protected.

Where audio recordings were made, specific consent for this was gained from participants, and participants were made aware of how long recordings would be kept before being destroyed. Participants were made aware of the voluntary nature of their participation and of their right to withdraw their participation at any time.

## **2.5 Completion of project pro formas**

In total, 57 different PVI settings provided pro forma data for use in this research study. Of these, pro formas from a number of settings were excluded from the unit cost analysis presented in section 3.3.3.3 This was because these settings were either unable to provide the full range of data required, or were unable to provide accurate data for costs, income or the number of childcare hours delivered. For instance, some providers that operated multiple settings were unable to extract cost or income data for a single setting, and some settings that were part of organisations that delivered a range of services apart from early years childcare were unable to calculate income or costs for the early years portion of their business. Other settings were simply unable to provide accurate data on the number of hours of childcare they had delivered.

In total, 47 settings met the quality criteria for inclusion in the unit cost analysis in section 3.3.3.3.

## **2.6 Data analysis**

A thematic analysis was conducted of all qualitative data collected for this research study. The aims of the study provided a clear framework around which to analyse the data, and so the analysis draws out the key themes that emerged in relation to these aims. Data from all 44 in-depth, qualitative interviews was included in the analysis presented in the sections that follow, in addition to data from telephone interview discussions.

Quantitative information was analysed with the aid of SPSS statistical analysis software.

This report aims to provide an integrated analysis of the qualitative and quantitative data collected for this study.

## 3 Findings

### 3.1 Settings' finances<sup>8</sup>

#### KEY FINDINGS

- The largest single factor contributing to settings' total costs was 'staffing costs', which accounted for 73% of total costs.
- 'Rent/mortgage costs' was the second largest element contributing to total costs, with 'materials and equipment' costs third, 'meals and catering' costs fourth, and 'utilities' fifth.
- The proportion of total costs accounted for by staffing costs was consistent across settings with childcare staff with a childcare related degree, a qualified teacher, or Early Years Professional or Teacher status, and those settings without such staff.
- The majority of settings drew attention to their setting's sensitivity to changes in the cost of childcare staffing, and the implications of this for their setting's viability and sustainability.

#### 3.1.1 Settings' profitability

Analysis of settings' financial information indicated that of the 51 settings who provided data on total income and total costs, 34 had made a surplus/profit during the last financial year, with 5 'breaking even'<sup>9</sup> and 12 making a loss. Analysis of data from the 34 settings that made a surplus/profit shows that the average gross surplus/profit margin of these settings (calculated by dividing gross surplus/profit by total income) was 13.7%.

Further analysis suggests a difference between the profitability of privately owned settings and those in the voluntary and community sector, with 81% of privately owned settings making a surplus/profit. The corresponding figure for Voluntary and Community Sector (VCS) settings was 48%.

Comparisons of the profitability of settings providing only sessional care with those who also provided full day care indicated similar levels of profitability between both types of settings (69% and 66% of settings made a surplus/profit, respectively).

#### 3.1.2 Settings' total costs

The following section provides findings on settings' total costs. The vast majority (74%) of settings who provided information on income and costs were able to provide information from their annual accounts, with the remainder providing an accurate estimate of their income and costs (for example, based on profit and loss statements).

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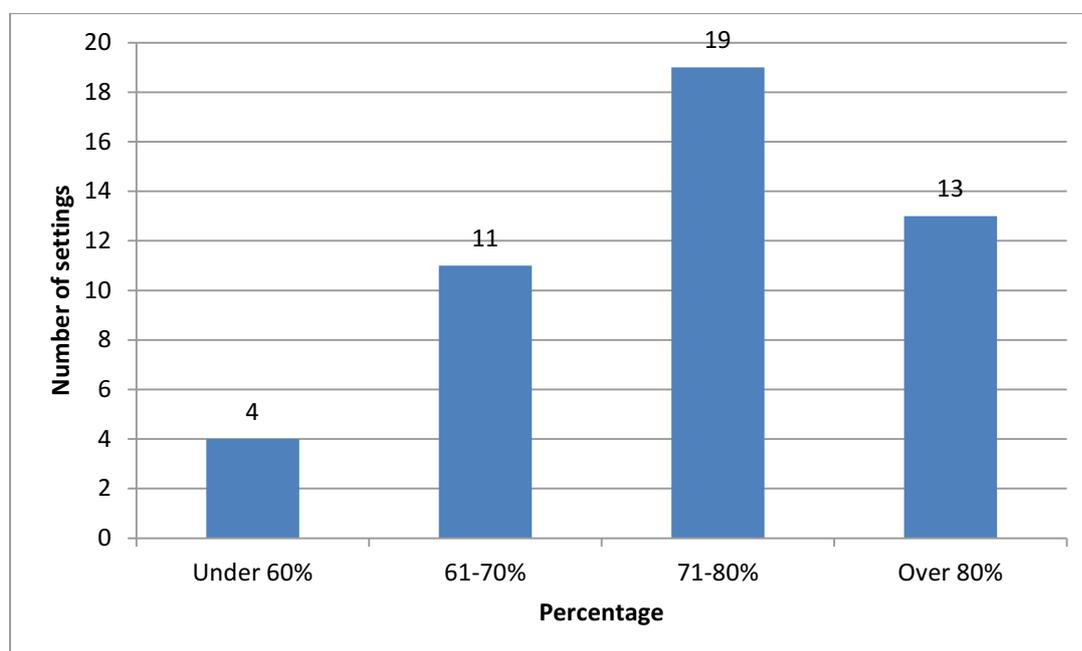
<sup>8</sup> Only one of the three 3 Independent School settings that participated in this study was able to provide financial information related to the early years childcare element of their business.

<sup>9</sup> A setting was defined as breaking even if its profit/surplus or loss was less than 0.5 per cent of its total income.

In line with previous analyses of childcare providers' costs (for example, DfE 2012)<sup>10</sup>, this study found that the largest single factor contributing to settings' total costs was their staffing costs<sup>11</sup>. The average (mean) proportion of total costs accounted for by staffing costs, for the 47 settings whose quantitative data met the quality criteria for inclusion in the cost analysis, was 73% (n=47). As Figure 1 shows, for the majority of settings (32 out of 47), staffing costs accounted for more than 70% of total costs.

The pattern of a high proportion of total costs being accounted for by staffing costs was broadly consistent across provider types, with an average (mean) of 70.6% of total costs accounted for by staffing costs for privately-owned settings (n=27) and the corresponding figure being 75.9% for VCS settings (n=20).<sup>12</sup>

**Figure 1: The proportion of total costs accounted for by settings' staffing costs (n=47)**



All settings whose quantitative data met the quality criteria for inclusion in the cost analysis provided data on staffing costs. However, other costs were not so consistently reported due to variations in the cost categories that different settings use, the way that individual settings collate data on costs and report and categorise costs within their accounts, and the fact that settings combine some of the various business cost elements in different ways.

Some settings therefore had some difficulty in providing a clear breakdown of their costs, and had difficulty in reporting costs against all of the cost categories presented on the project pro forma.

Analysis of available cost data from those settings that provided figures for rent/mortgage costs (n=37) indicated that rent/mortgage costs tended to be the second largest element contributing to total costs, contributing 8.7% of total costs on

<sup>10</sup> DfE (2012) Childcare Providers Finances Survey 2012, Department for Education, May 2012  
<sup>11</sup> Includes wages and National Insurance payments, but excludes training costs.  
<sup>12</sup> The corresponding figure for the single independent school that provided financial information was 65%.

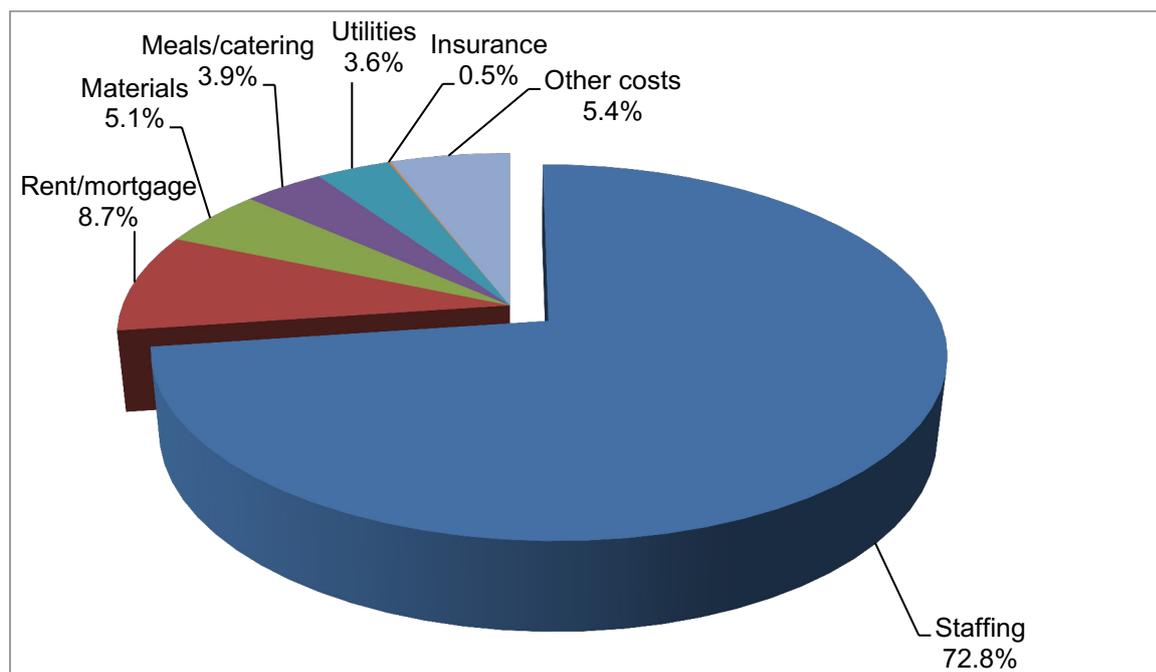
average. Materials and equipment used during sessions was the third largest contributor to total costs (5.1%, n=31).

Cost data from the 33 settings who provided data on the costs of meals and catering indicate that this component was the fourth most significant cost for settings, contributing an average of 3.9% to total costs. Utilities accounted for an average of 3.6% of total costs according to the 27 settings who provided data on this cost element, with insurance (the final cost category listed on the pro forma) contributing 0.1% on average (n=19).

The costs listed above account for the vast majority of settings' total costs. During interviews, representatives from settings also provided data on a range of other costs that made a significant contribution to total costs for their particular settings. These typically included staff training, administrative costs, and building maintenance and repairs.

A breakdown of the average proportion of total costs accounted for by each cost element is presented in Figure 2.

**Figure 2: The average proportion of total costs accounted for by each cost element**



Qualitative interviews highlighted the importance of staffing costs as the key driver of total business costs for all settings that participated in this study. The majority of settings drew attention to their setting's sensitivity to changes in the cost of childcare staffing, and the implications of this for their setting's viability and sustainability. Typically, they were concerned about increases in the national minimum wage and the cost of pension auto-enrolment for their settings. The majority of settings were concerned about their ability to remain viable if staffing costs increased, particularly if the rate of local authority funding for the free entitlement did not increase. As one setting representative stated:

*“Them upping the minimum wage, you always feel like you’re battling against everything, you always get everything thrown at you all the while – it’s just a continual struggle. That’s [increase in the national minimum wage] going to have a huge financial impact.”*

PVI setting representative

Concerns about the cost of staffing were compounded by the fact that many settings felt unable to raise the fees that they charged to their parents, as they felt that parents would not be able to afford those fees and that raising fees would make them uncompetitive, resulting in a decline in customers.

Approximately three-quarters of settings interviewed expressed concern about what they viewed as a low level of wages within the early years childcare sector. These settings typically felt that they were not able to pay staff a level of wages that reflected their skills, experience, responsibility and commitment. For a number of settings, this meant that they had difficulty recruiting or retaining good quality childcare staff, of the skill or qualification level they desired. As one setting commented:

*“You are expected to deliver a high level of education, not just care, and if you want a high level of teaching input you’ve got to pay for that, and we can’t afford graduates. We can’t even afford to have all level 3 staff.”*

PVI setting representative

Forty-nine per cent of the settings that participated in this study stated that they had a setting leader or member of childcare staff with a childcare related degree, who was a qualified teacher, or who had Early Years Professional or Early Years Teacher status. The issue of being able to pay staff a competitive wage was more acute for some settings with a more highly qualified childcare workforce, although concerns about settings’ ability to pay staff a reasonable wage were also voiced by many settings with less well academically qualified staff.

One setting representative, who ran a setting with a number of staff qualified at level 5 and above, stated:

*“It’s very frustrating...it’s just not realistic because we’ve got level 5s, we’ve got teachers, we’ve got absolutely fantastic staff who all want a really good salary.”*

PVI setting representative

Another stated:

*“I’m not saying that you can’t do things without loads and loads of money, but it’s the staffing really. We’ve got good quality staff, staff who are still willing to train, people who are doing the foundation degree...They’re really passionate about what they do but we can’t pay them what they deserve.”*

PVI setting representative

Interestingly, analysis of the proportion of total costs accounted for by staffing costs is consistent across settings with childcare staff with a childcare related degree, a qualified teacher, or Early Years Professional or Teacher status, and those settings

without staff qualified at that level. As table 2 shows, the proportion of total costs accounted for by staffing costs was 73.01% for the former group of settings and 72.73% for the latter. This suggests that the proportion of total costs accounted for by staffing costs is not greater for settings with staff with higher academic qualifications.

**Table 2: Staffing as a proportion of total costs by staff qualifications**

	Staffing as a proportion of total costs
Staff <u>with</u> degree/qualified teacher/ EYP/EYT	73.7%
Staff <u>without</u> degree/qualified teacher/ EYP/EYT	72.1%

It was clear from interviews that a key priority for settings was managing their staffing costs. This priority was set against a backdrop of needing to ensure a high quality provision for children in their care, and maintain adequate staffing levels at all time.

Approximately one-third of the settings who participated in this study had ‘flexible’ staffing in place within their setting. These settings typically felt that this labour flexibility assisted them in managing staffing costs and responding to daily, weekly, or seasonal fluctuations in setting occupancy levels. Examples of approaches to flexible staffing employed by settings included employing larger numbers of part-time than full-time staff, employing staff on contracts with annualised hours, and employing their own ‘bank’ staff. In addition, a very small number of settings employed most staff on flexible ‘zero hours’ contracts. The vast majority of settings stated that they tried to avoid using agency childcare staff because of the typically high costs associated with it.

Although a number of settings highlighted the benefits of flexible staffing for their setting’s ability to control staffing costs, a minority of both privately-owned and VCS settings stated that they had avoided implementing a great deal of flexibility into their staffing as they felt that this would have a number of negative impacts for their settings. These included negative impacts on staff morale and on the quality of care provided for children within the setting, who they felt benefitted from consistent staffing. As one setting stated:

*“Looking at childcare as a business and then following what’s best for the children, there is a conflict. Because best for business I’d take everyone on flexible and then my costs are down and have less qualified people which costs me less. But ultimately, the children need people that they know, they need consistency, their keyworkers, and that is the constant juggling. And it’s hard because it’s not like another business, it’s children’s lives, it’s not a ‘product’.”*

PVI setting representative

### 3.2 Settings' staff:child ratios

#### KEY FINDINGS

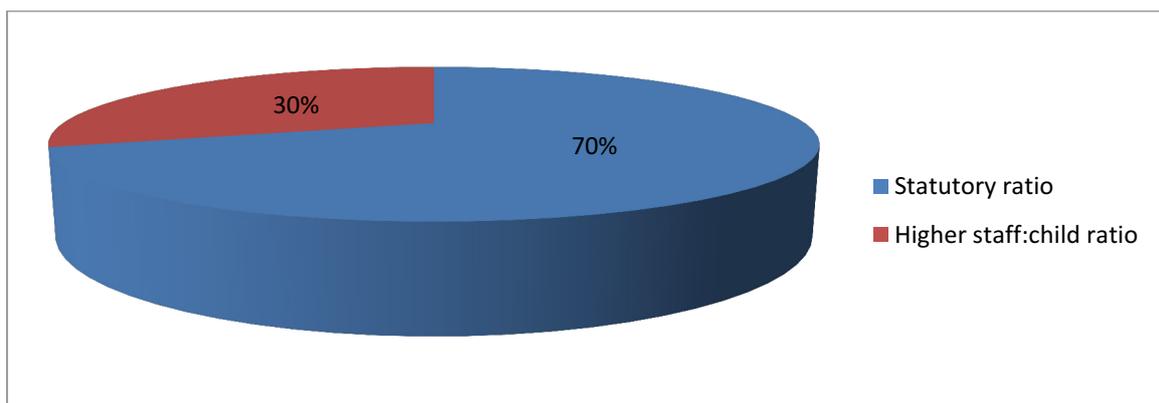
- 30% of settings operated at a higher staff:child ratio than the statutory requirement when delivering care for two-year-olds.
- 74% of settings operated at a higher staff:child ratio than the statutory requirements when delivering care for three- and four-year-olds.

As stated above, staffing costs were the largest single factor contributing to settings' total costs. This section provides further analysis of settings' staffing, by exploring the staff:child ratios in operation within settings that participated in this study. This is particularly important since, as described in section 3.3.3.2, settings' staff:child ratios were utilised in calculating setting's unit costs for delivering childcare.

Figures 3 and 4 show the number of participant settings for whom unit cost analysis was conducted, that were operating statutory ratios in delivering childcare for two-year-olds and three- and four-year-olds, compared with the number operating a higher staff:child ratio (that is, settings that operated with a greater number of staff per child than the statutory requirements).

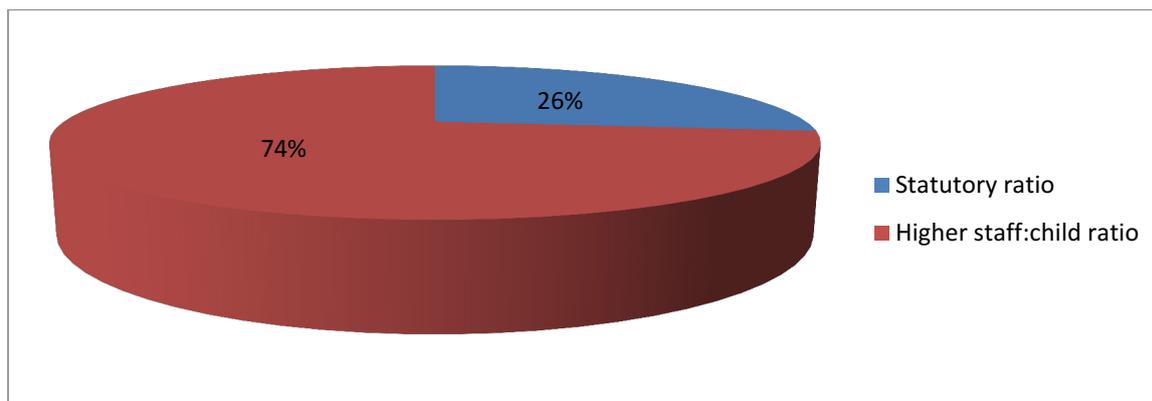
As figure 3 shows, of the 47 settings for whom unit cost analyses were conducted, 30% (14 settings) operated at a higher staff:child ratio than the statutory requirements when delivering care for two-year-olds.

**Figure 3: Ratios operated by settings in delivering care for two-year-olds**



As figure 4 demonstrates, the proportion of these settings operating at a higher staff:child ratio than the statutory requirements when delivering care for three- and four-year-olds was 74% (35 settings).

**Figure 4: Ratios operated by settings in delivering care for three- and four-year-olds**



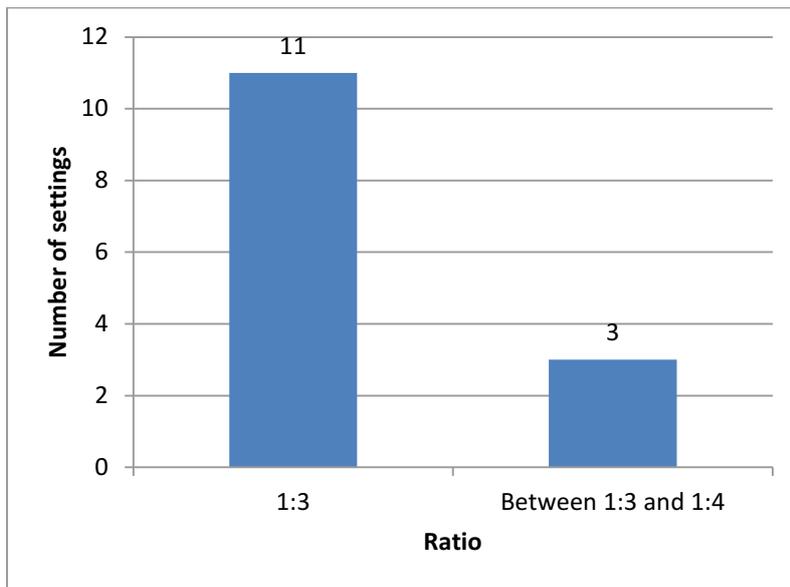
A similar pattern of results was found when data for the whole sample of participant settings was analysed. Analysis showed that 30% of settings who provided details of the ratios they operated to, operated at a higher staff:child ratio than the statutory requirements when delivering care for two-year-olds (n=53). The corresponding figure for three- and four-year-olds was 69% (n=54).

A similar pattern of results was also found when comparisons were made between privately-owned and VCS settings.

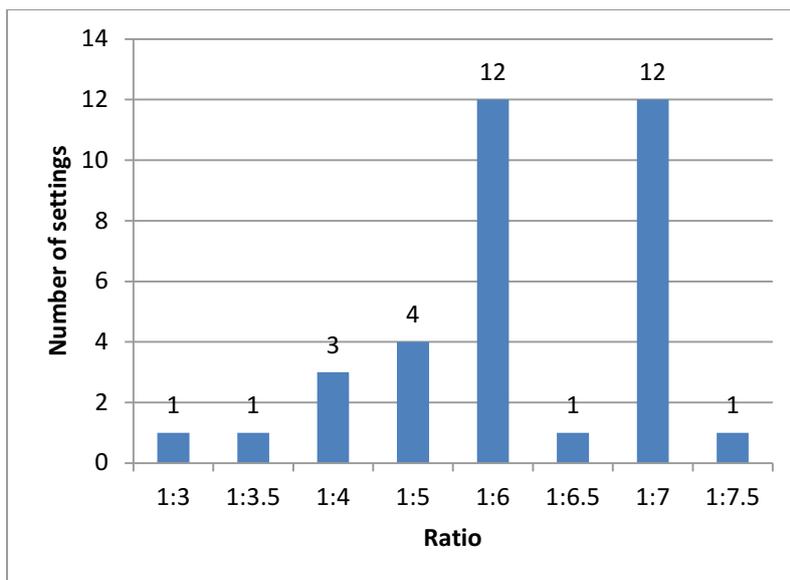
Figures 5 and 6 below, provide additional information about the actual ratios that settings adopted when providing care for two-year-olds and three- and four-year-olds, for settings for whom unit cost analyses were conducted. As Figure 5 shows, of the 14 settings that operated at a higher staff:child ratio when providing care for two-year-olds, 11 operated at a ratio of 1:3 with the remaining three settings operating at a ratio between 1:3 and the statutory ratio of 1:4.

Figure 6 shows that the majority of settings that operated at a higher staff:child ratio when providing care for two-year-olds and three- and four-year-olds tended to operate at ratios of about 1:6 or 1:7, with a small number of settings at higher ratios than these. Typically, settings that operated very high staff:child ratios when caring for three- and four-year-olds (for example 1:3 or 1:4), stated that they were doing so because of the extra staffing required to provide appropriate support to children with additional needs.

**Figure 5: Ratios adopted within settings with higher than statutory ratios when providing care for two-year-olds (n=14)**



**Figure 6: Ratios adopted within settings with higher than statutory ratios when providing care for three- and four-year-olds (n=35)**



Statutory guidance<sup>13</sup> states that, for three and four-year-olds, where a worker with 'Qualified Teacher Status, Early Years Professional Status, Early Years Teacher Status or another suitable level 6 qualification is working directly with the children', they are able to provide care for up to 13 children (a staff:child ratio of 1:13). It might be expected then, that settings with an early years teacher/professional, would tend to operate at lower staff:child ratios than those without such as member of staff. To explore this further, data on the ratios operated by settings was

<sup>13</sup> DfE (2014) Statutory framework for the early years foundation stage , Department for Education, March 2014

compared for settings with an early years teacher/professional ('graduate-led' settings) and those without. In total, 52 settings that participated in this study provided data on both the ratios used within their setting and whether or not their setting included a member of childcare staff who was a qualified teacher, or held a childcare related degree or Early Years Professional or Teacher status.

As table 3 shows, analysis of this data indicated that there was little difference between the proportions of 'graduate-led' and non-graduate-led settings that operated at above statutory staff:child ratios when caring for two-year-olds. The percentages of these settings that provided care for two-year-olds and operated at above statutory staff:child ratios were 31% and 32% respectively.

**Table 3: The proportions of 'graduate-led' and 'non graduate-led' settings operating statutory and above statutory staff:child ratios when caring for two-year-olds (n=52)**

	Operating at statutory staff:child ratio	Operating at higher than statutory staff:child ratio	Not applicable (not delivering care for two-year olds)	Total
Graduate-led	20 (69%)	9 (31%)	0 (0%)	29
Non graduate-led	15 (68%)	7(32%)	1 (n/a)	23

As table 4 shows, analysis of data from this study highlighted a difference between the proportions of 'graduate-led' and non graduate-led settings that operated at above statutory staff:child ratios when caring for three and four-year-olds. The data show that a higher proportion of graduate-led settings than non graduate-led settings that participated in this study, operated higher staff:child ratios (76% and 61% respectively). It should be noted however, that the small number of graduate-led and non graduate-led settings included in this analysis (28 and 23 respectively), means that this percentage difference should be treated with some caution, and that it is not possible to draw robust conclusions from this finding. However, this relatively small difference between 'graduate-led' and non graduate-led settings, suggests that both types of setting may be operating at broadly similar ratios when caring for three- and four-year-olds, and that graduate-led settings may not be operating at the much lower staff:child ratios that the minimum legal requirements allow.

Indeed, qualitative findings from this study indicated that very few settings may be operating at much lower staff:child ratios as a result of having a qualified teacher, EYP, EYT, or staff member with a childcare related degree within their setting. None of the settings involved in this study indicated that they ever operated at a staff:child ratio close to 1:13.

The finding may also be explained by the fact that in this study, staff within settings who were qualified teachers, or held a childcare related degree or Early Years Professional or Teacher status, were not always full-time childcare staff. Their impact on their settings' ability to implement lower staff:child ratios may therefore have been limited.

**Table 4: The proportions of ‘graduate-led’ and ‘non graduate-led’ settings operating statutory and above statutory staff:child ratios when caring for three- and four-year-olds (n=52)**

	Operating at statutory staff:child ratio	Operating at higher than statutory staff:child ratio	Total
Graduate-led	7 (25%)	22 (76%)	29
Non graduate-led	9 (39%)	14(61%)	23

During in-depth interviews, settings gave a number of reasons for adopting higher staff:child ratios within their settings. The most commonly cited reason was the issue of maintaining good quality teaching and care within the setting. Settings that cited this as their main reason for having a higher staff:child ratio, typically stated that they felt that such a ratio (for example, 1:6 rather than 1:8 for three- and four-year-olds) was necessary in order to maintain a high quality of teaching and care for children within their setting. As one interviewee, whose setting operated a 1:6 ratio for three- and four-year-olds commented:

*“We are an outstanding setting and in order to maintain that outstanding, I don’t think we could if we reduced our staffing...”*

PVI setting representative

The next most commonly reported reason for higher staff:child ratios related to the level of staffing that settings stated they needed in order to run their setting day-to-day. A number of settings stated that a higher ratio was generally required in order to operate the setting on a day-to-day basis. These settings typically stated that higher ratios were needed in order to allow staff to work effectively with children and complete work related to the EYFS, and to account for unforeseen circumstances such as children’s illness during the day, staff absence, and parent’s calling into the setting unannounced. As one participant stated:

*“If anyone’s off sick or on holiday, you’ve got that back-up. If a child’s suddenly unwell, they need a one-to-one, if you get parent’ in to visit, you’ve got to give attention, Key Workers need to be doing profiles with new people. You’ve got to have flexibility. So I do like to be over [ratio] from 9[am] until 4[pm].”*

PVI setting representative

In addition, a number of settings stated that they needed to implement higher staff:child ratios in order to appropriately support children with additional needs. Many of the participant settings that had children within their setting with additional needs stated that they needed to operate at higher staff:child ratios in order to ensure that they were able to provide the additional, and sometimes one-to-one, support that these children required. This was particularly the case for settings that provided care for a number children with additional needs, with the vast majority of these settings stating that they needed to operate at higher staff:child ratios in order to provide appropriate care and support. In some cases, this additional staffing was wholly or partially funded (for example, through local authority funding for support for children with an Education, Health and Care Plan), but in a number of cases settings described having to meet the needs of this additional staffing resource themselves.

Since staffing costs are the single greatest contributor towards settings' total costs, the adoption of larger staff:child ratios is likely to significantly contribute to settings' staffing costs, total costs, and unit costs for delivering the free early education entitlement.

### 3.3 Costs of delivering the free entitlement

#### KEY FINDINGS

- Very few participants stated that they had conducted any unit costing within their current setting.
- Approximately three-fifths of settings felt that they were making a 'loss' on the local authority free entitlement funding rate for two-year-olds.
- Approximately three-quarters of settings felt that they were making a 'loss' on the local authority free entitlement funding rate for three- and four-year-olds.
- Unit cost analysis conducted for this study indicated that weighted, the unit cost for delivering an hour of childcare for two-year-olds was £5.39, and for three- and four-year-olds was £3.51. Unweighted, unit costs were £5.40 and £3.71 respectively.
- Unit cost analysis provided the following ranges for unit costs at a 95% confidence level:  
Two-year-olds: £4.92 to £5.86  
Three- and four-year-olds: £3.17 to £3.85
- Unit costs of delivering childcare for both age groups were significantly greater for VCS settings than for privately-run settings.
- Analysis highlighted an average surplus in funding of £0.22 when settings' unit costs for delivering childcare for three- and four-year-olds were compared with local authority funding rates. Unweighted, the surplus was £0.03.
- Analysis highlighted an average shortfall in local authority funding rates for two-year-olds of £0.43 (weighted). Unweighted, the shortfall was £0.34.
- Although, on average, findings indicate a surplus of £0.22 in terms of delivering childcare for three- and four-year-olds, there were wide variations. 34% of settings experienced a shortfall in funding and 66% reported a surplus.

#### 3.3.1 Settings' measurement of the costs of delivering the free entitlement

All participants who were interviewed face-to-face, and the majority of those interviewed by telephone, were asked whether or not they had conducted any cost analysis within their setting to explore their unit costs for delivering childcare. Very few participants stated that they had conducted any unit costing, either in the past or within their current setting. In total, representatives from four settings stated that they had conducted some type of unit cost analysis.

In one case the interviewee had conducted a unit costing exercise after attending a local authority training session, whilst another participant had conducted a unit cost analysis following a request from a member of her management committee. Two other participants stated that they had conducted some calculation of unit costs at

some point in the past, but that they did not have an accurate picture of their settings' current unit costs. Another participant stated that she had conducted some unit costing at previous settings, but not yet within her current setting.

No detailed exploration was carried out during interviews, of the precise calculation that settings used to arrive at unit cost figures. However, settings that had conducted unit cost analysis described a general method that involved calculating total costs and dividing these by the number of hours of childcare delivered, suggesting that a top-down approach to calculating unit costs was taken by these settings. None of the settings interviewed described an attempt to break down unit costs by childcare age group (for example for under twos, two-year-olds, and three- and four-year-olds).

A number of settings highlighted the difficulty that they saw in attempting to calculate the unit costs of their childcare delivery. They stated that they would be uncertain about how to calculate unit costs and that due to the range of variables involved it was a task that they did not feel they would be able to undertake. As one participant stated:

*"I really would struggle to know where to start to work it [unit costs] out. And all these people who say it costs us 'x' to deliver it...for me it would be almost impossible to work it out."*

PVI setting representative

Settings typically saw the calculation of unit costs as a potentially time-consuming process. Although approximately half of interviewees stated that they saw a great deal of benefit in the calculation of unit costs, and felt that a clear understanding of unit costs would be of great use to their childcare business, calculating unit costs tended not to be a business priority. This is reflected in the fact that very few settings set their fee rates with reference to a calculated unit cost.

It was clear from in-depth interviews that settings tended to take a 'whole-business' approach to the task of assessing their business costs and the issue of remaining generally sustainable. Most settings stated that they focused on generating a surplus or remaining sustainable, and that their focus was on how the business was performing overall. Thus, settings typically based their business planning around a range of practical issues that were viewed as essential for the business to remain sustainable, such as calculating projected income and costs, required occupancy levels, and staffing requirements. Calculating unit costs was not generally viewed as an essential part of settings' business planning.

In-depth interviews also highlighted a lack of clarity amongst many interviewees about what constitutes a 'unit cost'. Many interviewees conceptualised unit costs as identical to the settings' price for childcare. These settings viewed their setting's fee rates as the unit cost to the setting of delivering childcare. This view of what constitutes a unit cost may be a result of settings setting their fee rates at a level that allows them to meet their overall costs of delivery.

### **3.3.2 Settings' perspectives on the costs of delivering the free entitlement**

During face-to-face and telephone interviews, all interviewees were asked about their perceptions of whether or not the hourly funding rate that they received from their local authority for delivering free entitlement places, was sufficient to meet their costs of delivery. In terms of free early education entitlement funding for two-year-olds, approximately three-fifths of settings stated that they thought that the costs to their setting of delivering an hour of childcare exceeded the rate they received from the local authority - that is, that they were making a 'loss' on the local authority funding rate. Approximately a quarter of settings felt that they were 'breaking even', with fewer than 10 per cent stating that they felt they were making a 'profit' or surplus.

Settings' perceptions of the sufficiency of the local authority hourly funding rate for three- and four-year-olds was broadly similar to that for two-year-olds, although a greater proportion felt that the costs to their setting of delivering an hour of childcare exceeded the rate they received from the local authority. Approximately three-quarters of settings stated that they thought they were making a 'loss' on the local authority free entitlement funding rate for three- and four-year-olds, with approximately 10 per cent stating that they were 'breaking even', and only one setting stating that the funding rate exceeded the cost incurred by them.

Settings' perceptions of the sufficiency of local authorities' funding for the free entitlement suggest that the majority of settings feel that the local authority funding rate fails to meet the costs incurred by settings in delivering the free entitlement, and that this is especially the case for funding for three- and four-year-olds. The hourly funding rate for three- and four-year-olds was less than that of two-year-olds in all local authorities included in this study, which may help to explain why a greater proportion of settings perceived a shortfall in the funding rate for three- and four-year-olds.

### **3.3.3 The adequacy/sufficiency of Local Authority funding**

#### **3.3.3.1 Calculating unit costs**

In total, 47 settings provided data that met the quality criteria for inclusion in the unit cost analysis presented below.

A top-down approach to unit-costing was taken in calculating the unit costs for PVI settings. Top-down approaches to unit costing involve drawing together all relevant expenditure and dividing this expenditure by 'units of activity'.<sup>14</sup> By embedding the cost analysis within the broader framework of an in-depth, qualitative study of settings' experiences of delivering the free early education entitlement, this study aimed to provide a detailed understanding of the way that the free entitlement is delivered, the unit costs of delivery, and any differences in unit costs.

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<sup>14</sup> Beecham, J. (2000), *Unit costs – not exactly child's play: A guide to estimating unit costs for children's social care*, University of Kent: Department of Health, Dartington Social Research Unit and the PSSRU..

The unit costing approach used in this study generates a separate unit cost for each setting, for providing an hour of childcare for two-year-olds and three-and-four year olds. It includes two cost components - fixed costs and variable costs.

The fixed cost element of settings' costs (which includes cost elements such as mortgage and rent costs, utility costs, and administrative charges) is apportioned to specific age ranges of children (two-year olds and three-and four-year-olds), based on the number of hours of childcare delivered by the setting for that age range per year.

Settings' main variable cost is staffing, which can vary considerably depending on occupancy levels and the age groups of children attending. Childcare staff:child ratios are a major factor affecting the staffing costs of settings. In calculating unit costs, staffing costs have been apportioned according to the staff:child ratios operated by settings, in order to accurately reflect the distribution of costs within settings.

Settings' fixed and variable costs have been apportioned as described above, and combined with data provided by settings on the total number of hours of childcare delivered annually for children within each age group, in order to calculate a separate unit cost for each setting, for the providing an hour of childcare for two-year-olds and three-and-four year olds

### **3.3.3.2 Apportioning staffing costs based on staff:child ratios**

In order to accurately calculate settings' unit costs, staffing costs were apportioned based on the staff:child ratios that settings operate rather than on the statutory staff:child ratios.<sup>15</sup> Thus, interviews with staff involved gathering detailed information about the precise staff:child ratios in operation within settings.

### **3.3.3.3 Settings' unit costs and the sufficiency of local authority funding**

#### **Settings' unit costs**

As shown by table 5 below, the weighted, average hourly local authority fee rates received by the 47 settings that were included in the unit cost analysis were £5.06 for two-year-olds and £3.74 for three- and four-year-olds. These rates are broadly similar to the average, England-wide, fee rates (including supplements) paid to PVI settings by local authorities in 2014/2015.<sup>16</sup>

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<sup>15</sup> Statutory staff:child ratios: Children aged under two: 1:3; children aged two: 1:4; children aged three and over: 1:8. In addition, for children aged three and over, where a worker with 'Qualified Teacher Status, Early Years Professional Status, Early Years Teacher Status or another suitable level 6 qualification is working directly with the children', they are able to provide care for up to 13 children (a staff:child ratio of 1:13)

Source: DfE (2014) Statutory framework for the early years foundation stage, Department for Education, March 2014

<sup>16</sup> Source: Department for Education Statistics on local authorities' planned expenditure for the financial year 2014 to 2015

**Table 5: Hourly rate received by settings included in the unit cost analysis – comparison with average England-wide fee rate (n=47)**

Age group	Settings included in this study	Average England-wide fee rate (including supplements)
Two-year-olds	£ 4.96 (weighted)	£5.15
Three- and four-year-olds	£ 3.73 (weighted)	£3.95

Table 6 below, presents figures for participant settings' unit costs calculated using the staffing ratios in operation within the settings. As stated in section 2.2.1, the sample of 47 settings that met the quality criteria for inclusion in the unit cost analysis, was weighted in order to ensure representativeness in terms of region, deprivation level (as measure by IDACI), and ownership type (Private or VCS).

As table 6 shows, the average (mean) unit cost for delivering an hour of childcare for two-year-olds was £5.39, and the corresponding figure for three- and four-year-olds was £3.51. The standard deviation for these unit costs was £1.71 and £1.20 respectively.

Unit costs calculated on the sample of 47 settings without weighting gave rise to unit costs of £5.40 for two-year-olds and £3.71 for three- and four-year-olds.

**Table 6: Overall average unit costs of delivering an hour of childcare for two-year olds and three- and four-year-olds (n=47)**

Age group	Unit cost
Two-year-olds	£5.39
Three- and four-year-olds	£3.51

As these unit cost figures are based on a sample of PVI settings, confidence interval calculations were conducted to provide an indication of the range within which the true population means lie. This analysis provided the following ranges for unit costs at a 95% confidence level:

- Two-year-olds: £4.92 to £5.86
- Three- and four-year-olds: £3.17 to £3.85

This indicates that we can be 95% confident that the true population means lie within the ranges stated above.

Figure 7 provides a breakdown of average unit costs by the proportion of total costs accounted for by each cost element, as presented in section 3.1.2. As the figure shows, the 'non-labour' element of unit costs accounts for £0.96 and £1.47 of the cost for settings of delivering childcare for three- and four-year-olds and two-year-olds respectively.

**Figure 7: Average unit costs broken down by cost component**

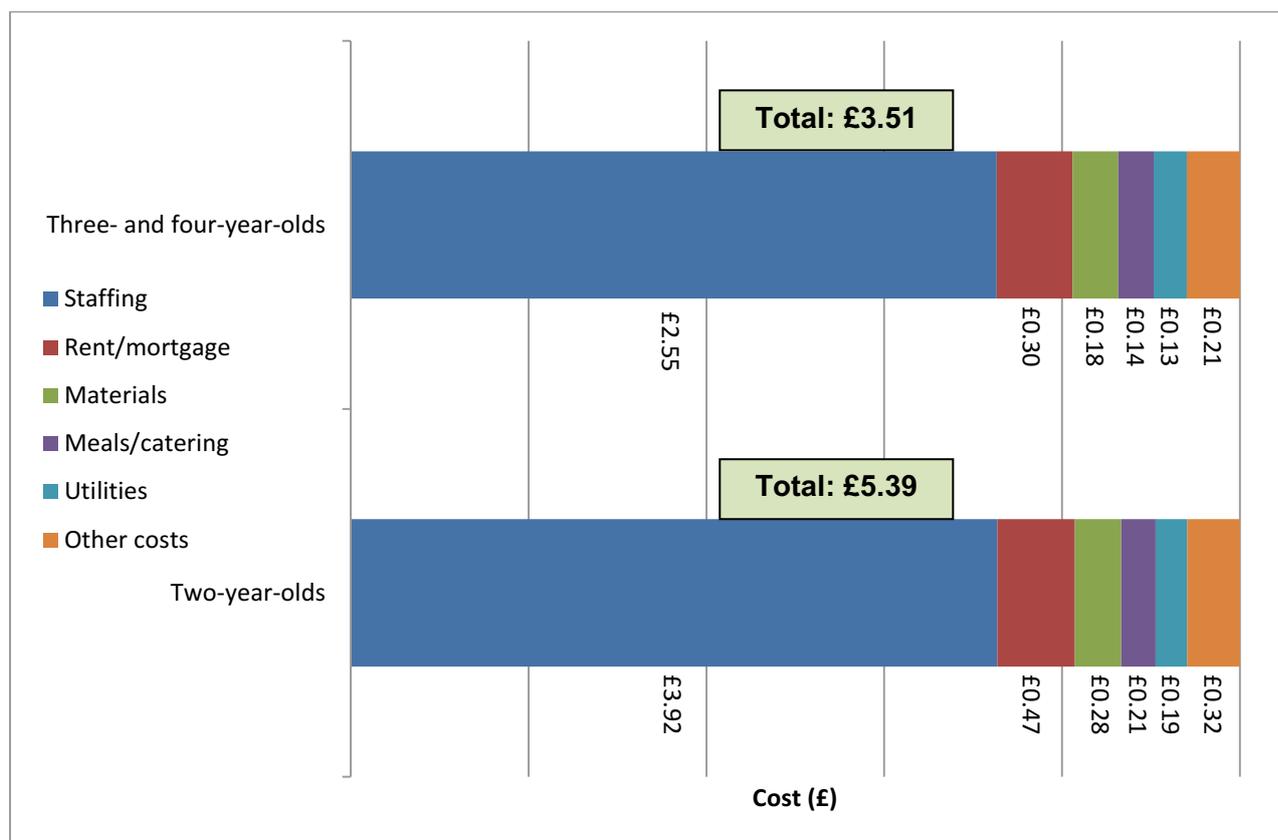


Table 7 below, presents the data from a comparison of the average unit costs of privately-owned and VCS-run settings. The data suggest that the unit costs of delivering childcare for both age groups are significantly greater for VCS settings than for privately-run settings.

**Table 7: Average unit costs of delivering an hour of childcare for two-year olds and three- and four-year-olds, by setting ownership type (n=47)**

Ownership type	Two-year-olds	Three- and four-year-olds
Private (n=27)	£4.98	£3.21
VCS (n=20)	£6.09	£4.00

Table 8 below, presents data from a comparison of the average unit costs of settings that deliver sessional care only, compared with those that also deliver full day care. The data show that on average settings delivering sessional care only have a higher unit cost for delivering that care for two-year-olds than settings that also deliver full day care. This pattern of results is similar for three- and four-year-old childcare, with settings delivering sessional care only, again, having a higher unit cost. It should be noted that the relatively small number of settings within our sample that offered sessional care only, means that these findings should be treated with some caution.

**Table 8: Average unit costs of delivering an hour of childcare for two-year olds and three- and four-year-olds, by type of care delivered (n=47)**

<b>Ownership type</b>	<b>Two-year-olds</b>	<b>Three- and four-year-olds</b>
Sessional only (n=13)	£5.62	£3.72
Full day care (n=34)	£5.26	£3.39

Table 9 below, presents the data from a comparison of the average unit costs for settings that were single settings, compared with those that were part of a larger group. As table 9 shows, on average, settings that were part of a group had lower unit costs for delivering care for two-year-olds than single settings (£4.89 compared with £5.60).

However, single settings and those that were part of a larger group had similar unit costs for delivering childcare for three- and four-year-olds for (£3.53 compared with £3.46). This result is perhaps surprising, as one might expect economies of scale to mean lower unit costs across all age ranges for settings that are part of a larger group. However, this finding might be explained by the fact that a large majority of the settings that participated in this study that were part of a larger group, were operated by organisations that operated a relatively small number of settings (fewer than 6). Economies of scale and associated unit cost reductions may therefore be less apparent, given the nature of the sample.

**Table 9: Average unit costs of delivering an hour of childcare for two-year olds and three- and four-year-olds, by whether setting was part of a larger group (n=47)**

<b>Ownership type</b>	<b>Two-year-olds</b>	<b>Three- and four-year-olds</b>
Single (n=27)	£5.60	£3.53
Part of larger group (n=20)	£4.89	£3.46

Table 10 provides figures comparing the unit costs of delivering the free entitlement for settings that were graduate-led and those that were not. As the table shows, unit costs were broadly similar for graduate-led and non graduate-led settings, with some small differences. Graduate-led settings had a unit cost of £5.35 for delivering childcare for two-year olds, compared with £5.45 for non graduate-led settings, indicating a slightly lower unit cost for graduate-led settings.

For three- and four-year-olds, the unit costs were again similar - £3.53 for graduate-led settings and £3.47 for non graduate-led settings.

**Table 10: Average unit costs of delivering an hour of childcare for two-year olds and three- and four-year-olds, by whether or not setting was ‘graduate-led’ (n=47)**

Type of setting	Two-year-olds	Three- and four-year-olds
Graduate led (n=28)	£5.35	£3.53
Not graduate-led (n=19)	£5.45	£3.47

This study also explored the relationship between settings’ unit costs and their occupancy levels. This involved calculating settings’ capacity based on the number of hours of childcare that are taken up annually within a setting, as a proportion of the maximum, theoretical number of hours of childcare that a setting could deliver. A correlational analysis was conducted of settings’ occupancy levels and their unit costs.

Results showed a significant negative correlation between settings’ occupancy levels and their unit costs for delivering childcare for both two-year-olds and three- and four-year-olds ( $p < 0.01$ , 2-tailed,  $n = 47$ ). The correlation coefficients were  $-0.61$  and  $-0.69$  respectively, and the significant result indicates that there is a significant (negative) relationship between settings’ occupancy levels and their unit cost. That is, that as settings’ occupancy levels rise, their unit costs tend to fall.

Correlational analyses were also conducted of settings’ unit costs and the actual ratios used by settings when delivering childcare. Correlational analyses of the unit costs for these settings of delivering childcare for two-year-olds and three- and four-year-olds, and the number of children cared for per staff member (staff:child ratio), found that there was no significant correlation between unit costs and actual ratios for either age group. The correlation coefficients were  $-1.08$  for two-year-olds and  $1.52$  for three- and four year olds, indicating that there was a weak negative correlation between the number of children cared for per staff member and unit costs – that is, as the number of children cared for per staff member rise, unit costs tended to fall. However, these correlations were weak and therefore not statistically significant.

It is important to point out that there may be a number of reasons for the lack of a statistically significant correlation between unit costs and staff:child ratios. For instance, the weak correlation may be due in part to factors such as the relatively narrow range of different ratios in operation within settings, or it may be the case that settings tend to pay staff members less in order to achieve higher staff:child ratios. Staff:child ratios may be therefore be a key cost driver for settings, even though this study found no significant correlation between staff:child ratios and unit costs.

### **Comparison between settings’ unit costs and local authority fee rates**

In order to explore the extent to which settings’ unit costs were met by local authority fee rates for delivery of the free early education entitlement, the hourly fee rate received by settings from their local authority for providing childcare for each age group of children, was compared with settings’ unit costs of delivering that care.

As table 11 below shows, this analysis highlighted an average shortfall in local authority funding rates for two-year-olds of £0.43. This indicates that there was an average (mean) ‘gap’ between settings’ unit costs for delivering childcare for two-year-olds and the fee rate that they received from local authorities for delivering the free entitlement of £0.43 per hour of care delivered.

As table 11 shows, the analysis also showed an average surplus in funding of £0.22 when settings’ unit costs for delivering childcare for three- and four-year-olds were compared with local authority funding rates. This indicates that, on average, the fee rate that settings received from local authorities for delivering the free entitlement for three- and four-year-olds was £0.22 above their unit costs of delivery.

Analysis based on the sample of 47 settings without weighting gave rise to overall differences between local authority funding rates and settings’ unit costs of -£0.34 for two-year-olds and £0.03 for three- and four-year-olds.

**Table 11: Overall difference between settings’ unit costs and local authorities’ fee rates (n=47)**

Age group	Difference
Two-year-olds	-£0.43
Three- and four-year-olds	£0.22

A closer analysis of the data comparing settings’ unit costs with local authorities’ funding rates for the free entitlement also highlighted variation in whether or not settings were experiencing a shortfall or surplus. Table 12 below, presents data on the numbers of settings that were experiencing a shortfall and the number that were experiencing a surplus, when their per hour unit costs were compared to the hourly fee rate they received from the local authority.

As the table shows, in 22 of the 47 settings, the local authority fee rate for providing free entitlement places to two-year-old children was in excess of the setting’s unit costs. In the case of providing free childcare for three- and four-year-old children, the local authority fee rate for providing free entitlement places to two-year-old children was in excess of the setting’s unit costs in 31 of the 45 cases.

**Table 12: Number of settings experiencing a ‘shortfall’ and ‘surplus’ when unit costs are compared with local authority fee rates (n=47)**

Age group	Two-year-olds	Three- and four-year-olds
Shortfall	25 settings	16 settings
Surplus	22 settings	31 settings

It is clear then, that although settings may experience a shortfall in funding on average, in terms of providing care to two-year-olds, and a surplus, in terms of providing care to three- and four-year-olds, the experiences of individual settings may be quite different. For instance, even though, on average, findings indicate a

surplus of £0.22 in terms of delivering childcare for three- and four-year-olds, a significant number of settings (16 settings, 34%) experienced a shortfall in funding.

Analysis of data for this study indicates that VCS settings tended to be more likely to experience a shortfall in free early entitlement funding than their privately-owned counterparts. This was particularly apparent in the case of delivering childcare for two-year-olds, where 37% of privately-owned settings and 75% of VCS settings experienced a funding shortfall.

### 3.3 Subsidisation and cross-subsidisation

#### KEY FINDINGS

- 19 of the 47 settings whose data was analysed for the unit cost analysis, experienced no shortfall in funding of the free early education entitlement for either two-year-olds or three- and four-year-olds
- None of the settings interviewed stated that they had actively or explicitly increased their pricing in order to compensate for losses as a result of the free early education entitlement.
- The ability to sell additional childcare hours above the free entitlement was important to many settings, who felt that any reduction in their ability to cross-subsidise in this way would be detrimental to their setting's viability.
- A large number of settings had implemented strategies that they felt allowed them to re-coup the perceived shortfall in local authority funding for the free entitlement.
- A number of settings stated that they were subsidising the free entitlement through other services that they delivered as an organisation.

The data presented above on the numbers of settings that were experiencing a shortfall and those that were experiencing a surplus, allows for an exploration of the extent of cross-subsidisation of the free early education entitlement.

In total, 19 of the 47 settings whose data was analysed for the unit cost analysis, experienced no shortfall in funding of the free early education entitlement for either two-year-olds or three- and four-year-olds. In these settings there will have been no cross-subsidy of the free early education entitlement since cross-subsidy occurs where there is funding shortfall. In the remaining 28 settings some cross-subsidy may be occurring.

Analysis of settings' cost data indicates that 13 of these settings were experiencing a shortfall in free entitlement funding that occurred across both age groups of children. Twelve settings were experiencing a situation where a shortfall in free entitlement funding for two-year-olds was occurring alongside a surplus in funding for three- and four-year-olds, suggesting that the funding for three- and four-year-olds may have been cross-subsidising this shortfall. In the case of three settings, there was a reversed situation, with a shortfall in funding for three- and four-year-olds occurring alongside a surplus for the younger age group.

On average, 55% of the total number of childcare hours delivered by the 47 settings that provided accurate data on the number of hours of childcare they delivered annually, were delivered as part of the free early education entitlement.

Some settings delivered as few as 7% of their total childcare hours as free entitlement hours. Such settings had a great deal of scope to sell additional hours over and above their free entitlement delivery, and cross-subsidise any potential shortfall in free entitlement funding.

At the other end of the spectrum, some settings delivered almost 100% of their childcare hours as part of the free entitlement, selling very few ‘additional’ hours. These settings tend to be those offering care for over-twos only, and tended to be in areas of greater ‘deprivation’, where understandably, parents were less able to afford to purchase additional childcare hours.

Table 13 below, shows the proportion of total childcare hours delivered by settings as part of the free entitlement.

**Table 13: Proportion of total childcare hours delivered that were free entitlement hours (n=47)**

Proportion of total hours	Number of settings
Less than 25%	10 settings
25-49.9%	10 settings
50-74.9%	14 settings
75% or greater	13 settings

During in-depth interviews, settings discussed cross-subsidisation issues. None of the settings interviewed stated that they had actively or explicitly increased their pricing in order to compensate for losses as a result of the free early education entitlement. Rather, settings tended to set prices that allowed them to make a surplus or remain sustainable overall, using a general ‘whole business’ approach as described earlier. Rather than setting fees according to the actual costs of delivering childcare for different age groups, settings tended to attempt to set fees so that these costs were dispersed across age groups.

Indeed, in a very small number of cases, rather than cross-subsidising an actual or perceived shortfall in free entitlement funding by adopting higher fees for under-twos, settings stated that they elevated the fees charged for three- and four-year-olds in order to keep down costs for under-twos childcare. For these settings, this strategy acted to help them attract more under-twos into their setting – these settings’ key, target client group.

For a number of settings, an important aspect of remaining sustainable was their ability to sell additional childcare hours above the free entitlement and for some settings, this enabled them to re-coup any shortfall in local authority funding by charging parents at their own fee rate. Some of these settings felt that any reduction in their ability to cross-subsidise in this way, would be hugely detrimental to their setting’s viability, as they felt that selling these additional hours helped to subsidise the free entitlement places they provided. As one setting stated:

*“The problem is where they want me to take these funded kids who don’t buy any surround care, that’s the bit where I lose money, and who pays that money? The people who are paying the surround care, because I’ve got to get that money from somewhere.”*

PVI setting representative

This study also highlighted the fact that a large number of settings had implemented strategies that they felt allowed them to re-coup the perceived shortfall in local authority funding for the free entitlement. For these settings, this was necessary in order to remain sustainable or viable, whilst offering free entitlement places, the cost of which they felt was not being fully met by local authority funding. For example, some settings typically charged for meals, activities, or hours of care between sessions, in order to re-coup the perceived shortfall. In order to meet this shortfall, a number of settings had implemented pricing and delivery strategies that meant that parents would typically make some financial contribution whilst their children were accessing the free entitlement.

In addition, a number of settings stated that they were subsidising the free entitlement through other services that they delivered as an organisation. Seven of the settings involved in this study were part of organisations that delivered a broad range of services beyond early years childcare. Most of these settings stated that a shortfall in free entitlement funding was being subsidised by other areas of their organisations' work. As one independent school setting stated:

*“The reason that we’re just about delivering the [free entitlement] service that we’re delivering for three and four year olds, is that the nursery is part of the school, and obviously people are paying fees in the main school and the money goes into one pot, so in a sense the school as a whole is subsidising the fact that for three and four year olds, it isn’t really adding up.”*

PVI setting representative

### 3.4 The Ability to expand provision

#### KEY FINDINGS

- Eleven of the 57 settings represented in this study stated that they would be able to expand the amount of childcare that they provided in their current setting.
- Approximately one-third of the 57 settings (21 settings) stated that they would be both interested in, and able to, expand the amount of childcare that they offered either by expanding on-site or by taking on additional venues, settings or spaces.
- Just over half of the settings that were interested in, and able to, expand stated that they would be able to access the funding required to support this expansion.
- The vast majority of settings that were interested in expanding their provision stated that capital investment would be necessary in order for this expansion to take place. Regardless of ability to access capital finance, these settings were very interested in the possibility of accessing capital finance through a Government initiative, with grants being the preferred route.
- A key barrier to expansion highlighted by settings was the difficulty that they had found in recruiting suitably qualified or experienced staff.
- Findings suggest that there may be a significant amount of spare childcare capacity available within PVI settings, which could be utilised for the expansion of the free early education entitlement.

#### **.4.1 Settings' capacity for expansion**

During in-depth interviews, settings discussed their ability to expand the number of children that they provided care for within their current setting and/or expand their childcare business to provide additional childcare capacity. In total, 11 of the 57 settings represented in this study stated that they would be able to expand the amount of childcare that they provided in their current setting, either because they felt that they had adequate floor space to increase the number of children in their setting, or because they would potentially be able to conduct building work or renovations that would allow the capacity of the setting to be expanded.

Settings' reasons for an inability to expand within their current setting included:

- Planning regulations that, for example, limited settings' ability to carry out building modifications that would be required.
- Landlords precluding the setting from expanding on site.
- Settings feeling that the quality of childcare would be compromised if more children were cared for within their current setting, despite potentially having the floor space to increase capacity.

Settings that felt able to expand within their current settings without renovations or building work, typically stated that they would be able to provide a relatively small number of additional childcare spaces, typically less than 10% of their current capacity.

In total, 21 of the 57 settings stated that they would be both interested in, and able to, expand the amount of childcare that they offered either by expanding on-site or by taking on additional venues, settings or spaces. Settings that stated that they would not be interested in such expansion typically gave one of the following reasons:

- Settings having recently expanded their provision and a lack of any intention to expand again for the foreseeable future.
- Settings' satisfaction with their current size and capacity, and a lack of interest in expanding.
- Settings viewing expansion as a risk, and feeling that their business is in such a precarious situation in terms of sustainability that taking on such a risk would be ill-advised.
- A surfeit of local childcare spaces and a lack of demand for additional places of the type offered by the setting.

Of the 21 settings who stated that they would be interested in expanding their childcare provision, 13 stated that they would be able to access the funding required to support this expansion. These settings tended to be privately owned childcare provider able to access finance through their banks, or else were organisations that

delivered a broad range of services beyond early years childcare, and were able to expand by utilising resources available within these organisations.

Of the eight settings that stated that they were unable to access the funding required to support expansion, two stated that they had found difficulty in accessing capital finance through banks, due to the lending criteria that banks applied. The other six settings that stated that they were unable to access such finance were VCS settings who felt unable to take on the risk of taking out a mortgage or loan in order to expand.

The vast majority of settings that were interested in expanding their provision stated that capital investment would be necessary in order for this expansion to take place. Some of these settings stated that they would be able to access the funds necessary for this capital investment (for example, through banks or their organisation's financial reserves). However, regardless of ability to access capital finance, the vast majority of settings that were interested in, and able to, expand their provision, were very interested in the possibility of accessing capital finance through a Government initiative, with grants being the preferred route.

Settings highlighted a number of different ways that they would use any capital finance that was available, in order to expand their childcare business. These included: renovations to existing buildings (for example, toilet facilities and outside space), purchasing new childcare premises, and the construction of extensions to existing childcare premises. It was clear from this that any capital finance offered would need to allow settings some flexibility to use it according to the specific needs of their childcare business.

In addition to the barriers to expansion for settings highlighted above, another key barrier highlighted by settings was the difficulty that they found in recruiting suitably qualified or experienced staff. This was a barrier to expansion for a small number of privately-owned settings that were actively exploring the possibility of expanding their childcare provision, and that had found great difficulty in recruiting staff of the required calibre. As one setting stated:

*“We’re using the apprenticeship scheme and effectively growing our own, because we can’t get people of the right calibre who we feel can fit into our setting and have got the experience and that that we need.”*

PVI setting representative

This study also explored the amount of ‘unused capacity’ within settings. This involved calculating settings’ capacity based on the number of hours of childcare that are taken up annually within a setting, as a proportion of the maximum, theoretical number of hours of childcare that a setting could deliver<sup>17</sup>.

On average, settings had 40.1% spare capacity, based on these calculations (n=47). This finding should be treated with some caution, as it is based on the ‘theoretical’ number of hours available annually within a childcare setting, and it is unlikely that settings will be able to achieve occupancy levels close to their theoretical maximum.

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<sup>17</sup> The maximum, theoretical number of hours of childcare that a setting could deliver annually was calculated based on place capacity multiplied by annual hours of operation.

However, these findings do suggest that there may be a significant amount of spare childcare capacity available within PVI settings, which could be utilised for the expansion of the free early education entitlement.

### **3.5 Barriers to the effective delivery of the current free entitlement**

#### **KEY FINDINGS**

- By far, the most frequently cited barrier to effective delivery of the free entitlement was settings' abilities to effectively support children with additional support needs within their settings.
- A number of settings highlighted the significant numbers of children who are eligible for the two-year-old free entitlement, who require additional support.
- A number of settings stated that they faced significant challenges in effectively supporting children with additional support needs, and that they typically bore the cost of this support without adequate additional funding.
- This study highlighted the risk that some settings may limit the amount of two-year-old funded early education they provide because of additional costs incurred through providing unfunded additional support for children and families.
- This study highlighted a lack of flexibility in the way in which some settings offered the free early education entitlement to local parents.
- A number of these settings stated that a reduction in the amount of administrative work that was necessary as a result of delivering the free entitlement, would make a significant difference to staff workloads and costs.

This section outlines the key barriers to settings' abilities to effectively deliver the current free early education entitlement, at their current local authority funding rates.

#### **3.5.1 Effectively supporting children with additional support needs**

By far, the most frequently cited barrier to effective delivery of the free entitlement was settings' abilities to effectively support children with additional support needs within their settings. A large number of settings stated that a significant number of the children who accessed the two-year-old free entitlement through their setting had some sort of additional support need.

This meant that these settings were required to provide additional support for these children or their families, resulting in an additional workload for setting staff and additional staffing costs for settings. The types of additional work related to the care and support for children with additional support needs varied, but included providing one-to-one or additional support for children with disabilities or special educational needs, competing paperwork and administrative work related to the care of children with additional needs, and attending meetings with social care staff where children

were subject to a Child Protection or Child in Need Plan. One setting described the implications of this additional workload in the following way:

*“Running the nursery is nigh on impossible, as they’re [staff] always at core groups, they’re always at meetings with the different agencies, case conferences...and you’re not just there for an hour, you could be there for two hours sometimes.”*

PVI setting representative

Although funding is sometimes available for some children with additional support needs (for example, where they have an EHC in place), settings typically stated that they bore the cost of this additional support without any additional funding. In addition, the process of applying for funding for children with additional needs was described as onerous by a number of settings.

A number of settings stated that they were considering, or had already begun to, limit the number of free early entitlement-funded two-year-olds that they cared for within their settings, as the additional workload and cost had become prohibitive. Other settings had made a business decision not to offer free entitlement places for two-year-olds because of the additional workload sometimes involved in caring for them. One setting said:

*“The two-year old funded children that we’re getting, I’m going to have to put a stop on them because the children that we’re getting are so in need of extra support that the [LA fee rate] doesn’t cover it ...We’re at our limit where we can’t take any more.”*

PVI setting representative

Another participant, who stated that more than one-quarter of the free early entitlement-funded two-year-olds within her setting had some type of additional support need, and had had to limit the number of hours of childcare she could offer to certain children, stated:

*“I can’t magic up a member of staff to provide one-to-one support for this child...it put’s extra pressure on the staff...we’ve had to say ‘Well, this is what we can offer you’.”*

PVI setting representative

### **3.5.2 Lack of flexibility of the offer**

This study highlighted a lack of flexibility in the way in which some settings offered the free early education entitlement to local parents. Whilst some settings were extremely flexible, and allowed children to receive their free entitlement hours in a way that suited them and their families, some others settings were far more restrictive in their offer. This was particularly apparent where settings’ occupancy was high and/or where children required only their 15 hours of free entitlement, and their parents were not buying additional hours of childcare.

In these circumstances settings often gave priority over sessions to children whose parents were buying additional hours (for example, where children were in full-time

day care), and some settings placed other restrictions on the free entitlement hours available to children who only accessed 15 hours of childcare. As one interviewee stated:

*“We’ve got to the point where we’re saying to parents who just want the 15 hours: ‘this is what we’ve got left’...they can’t really pick and choose.”*

PVI setting representative

Settings typically stated that low local authority fee rates meant that they needed to place restrictions on the free entitlement offer, in order to remain sustainable. However, such restrictions in the free entitlement offer have the potential to result in some children being unable to access free entitlement hours in the way that best suits their needs.

### **3.5.3 The administrative burden**

A number of settings stated that they felt that the amount of paperwork and administrative work involved in delivering the free early education entitlement, documenting children’s attendance, and claiming fees from local authorities was too great. Some of this administrative work related to children who were accessing the two-year-old free entitlement and who had additional support needs. For example, in cases where a significant number of the two-year old free entitlement places offered by a setting were accessed by children with additional support needs, the setting typically stated that the additional support required gave rise to a significant amount of additional administrative work. Examples of this administrative work included, work related to applying for Education Health and Care Plans or additional funding to support children with Special Educational Needs or disabilities, and work related to supporting children where a Child Protection or Child In Need Plan was in place.

Settings also tended to draw attention to the high, general administrative workload generated by the free entitlement. This included administrative work necessary in order to complete ‘headcount’ information and submit early education entitlement funding claims to local authorities.

Although some settings representatives (for example, nursery owners) stated that some of this administrative work was sometimes done in their own time, and therefore unpaid, settings typically highlighted the additional staffing costs generated for settings by administrative work for the free entitlement. As one setting stated:

*“I now have someone to do the admin around the funded three and four year old children, which is an additional cost.”*

PVI setting representative

A number of these settings stated that a reduction in the amount of administrative work that was necessary as a result of delivering the free entitlement, would make a significant difference to staff workloads and costs.

## 3.6 The expansion to 30 hours

### KEY FINDINGS

- The vast majority of settings were positive, in principle, about expansion to 30 hours, although most were keen to highlight the importance of an increase in the local authority rate.
- Findings suggest that the implications for settings will depend on a complex range of factors, including: occupancy rates; settings' current fee rates and how these compare with the local authority funding rate; number of hours typically sold by settings over and above the current free entitlement; and the mix of age ranges typically cared for within the setting.
- A key concern for settings regarding the expansion to 30 hours was the effect that it would have on their ability to generate revenue by selling additional hours of childcare.
- Many settings were concerned that an increase in the free entitlement to 30 hours would mean they would be able to offer childcare to fewer three- and four-year-olds, and fewer children overall.
- A number of preschool settings that offered fewer than 30 hours of childcare per week expressed concern about their ability to remain sustainable when the free entitlement is increased to 30 hours.
- For a few settings the potential impact of the expansion to 30 hours appeared to be minimal.

### 3.6.1 Settings' views on the expansion

The vast majority of settings were positive, in principle, about expansion to 30 hours of free early education for working parents of three- and four-year-olds, although most were keen to highlight the importance of an increase in the hourly rate that they received from the local authority for providing this childcare, if they were to remain viable and sustainable whilst offering the 30 hours.

The vast majority of settings stated that they were intending to deliver the 30 hours of free entitlement, although for some of these, this intention was predicated on the assumption that the local authority fee rate would rise. Without a rise in fee rates, a small number of settings stated that they would not be able to deliver 30 hours of free entitlement. Approximately one-fifth of settings stated that whether or not they decide to offer the 30 hours expanded free entitlement will depend on the fee rate that they would receive from the local authority.

Approximately one-quarter of the settings that took part in this study stated that they had started to prepare and conduct business planning ahead of the introduction of the 30 hour entitlement. The remaining settings stated that they were waiting for more clarity and detail about the specific eligibility criteria relating to 'working parents', and would begin to plan once they were clearer about this.

Settings that had begun to plan for the expansion to 30 hours, typically tended to be those settings that currently offered sessional care only, particularly where they did not currently offer 30 hours of childcare per week.

### 3.6.2 Implications of expansion to 30 hours for settings

During interviews, settings were probed about the implications of an expansion to 30 hours for their setting. Findings suggest that the implications for settings will depend on a complex range of factors, including:

- Settings' occupancy rates.
- The proportion of settings' current childcare hours that are taken up by children accessing the free entitlement.
- Settings' current fee rates, and how these rates compare with the local authority funding rate.
- The number of working parents whose children currently access the setting, and how this is likely to change over time.
- The likelihood of local parents who are currently not working, entering the labour market as a result of the expansion to 30 hours.
- The number of hours typically sold by settings, over and above the current free entitlement
- The mix of age ranges typically cared for within the setting.

A key concern for settings regarding the expansion to 30 hours was the effect that it would have on their ability to generate revenue by selling additional hours of childcare. A number of settings, and particularly those that had high levels of occupancy, were concerned that unless the local authority fee rate rose to a level approaching their own fee rate, they would lose a significant amount of revenue, as the number of hours that they had available to charge for at their own fee rate fell. As one setting stated:

*"If they all suddenly get 30 hours, then that's it, I'm gone [out of business], if it [local authority fee rate] doesn't go up...I'll be out of business in three months... They're shrinking the bit that I can actually make that money back on."*

PVI setting representative

Another particular issue of concern for many settings was that an increase in the free entitlement to 30 hours would mean they would be able to offer childcare to fewer three- and four-year-olds, and fewer children overall, as each three- or four-year-old child would now be potentially entitled to 30 hours of free childcare rather than 15. A number of settings were concerned about their capacity to provide enough childcare for all of the children within their setting that might require it, and about the 'displacement' effect that the expansion to 30 hours might have. As one setting said:

*“It [expansion to 30 hours] would mean that for us we’d be able to offer less children places, because ultimately you either take two children on for 15 hours each or two children for 30 – you can’t sort of say, ‘oh, I’ll have two children at 30 hours’, because there’s not the room to do that.”*

PVI setting representative

A number of settings that offered full day care highlighted the importance of younger children within their setting to their business model and sustainability, and felt that the expansion to 30 hours might threaten their ability to maintain the balance of babies and under-tuos within their setting. For these settings, increasing the number of three- and four-year-olds within their setting, as a result of the expansion to 30 hours, would inevitably mean a reduction in the number of younger children within the setting, and a likely reduction in revenue, especially in settings with large numbers of fee-paying two-year-old and babies.

Some settings were also concerned with the prospect of having a relatively large proportion of the children within their setting aged 3 and 4, due to fact that this could result in low occupancy within the setting if large numbers of children left during the summer to attend school. As one setting said:

*“If you have the 30 hours and the children are all 3 and 4 year olds, which they possibly will be, those 3 and 4 year olds will all leave in the summer which will then wipe me out totally, and I have to replace all those children and that’s a lot of children to replace. And you haven’t got the younger children feeding through.”*

PVI setting representative

A number of preschool settings that offered fewer than 30 hours of childcare per week expressed concern about their ability to remain sustainable when the free entitlement is increased to 30 hours. This was particularly the case for those that stated they would be unable to increase the number of hours of childcare that they delivered each week. For these settings, an expansion to 30 hours would mean that they would either need to find new or additional premises from which to deliver childcare, or else not offer the expanded 30 hour entitlement. These settings were clear however, that failure to offer the expanded entitlement would be likely to result in them losing clients to other settings that were able to offer it. One such setting, that was potentially able to expand its hours to 30 commented:

*“For us, the way we’re running at the moment, we couldn’t offer the 30 hours, so we would have to totally look at the way we run, we would have to look at extending our hours...we wouldn’t want us to lose out because parents would go to other settings that are offering those 30 hours and we’re not. But we would need to be sure that we would actually get that number of people to make it worthwhile.”*

PVI setting representative

Another preschool setting, that was concerned about the risks of expanding its provision to 30 hours per week said:

*“My concern is that we set this up to run at 30 hours per week and then we sit here with empty places and then the cost of that wipes us out. That would be our concern.”*

PVI setting representative

For a few settings, however, the impact of the expansion to 30 hours appeared to be minimal. For instance, for settings whose clients were typically not working parents, and who would be unlikely to be encouraged back into the labour market as a result of the expansion to 30 hours, the effect of the expansion to 30 hours may be minimal. This was especially the case for settings where few parents purchased additional hours above the free entitlement. As one setting said:

*“It will have very minimal impact on our families because we have very few families where both parents are working, so we don’t expect it to have a big impact. Most of our parents will stay on 15 hours...for us it’s those who have chosen to buy places already for children under 3 who we think would then expand into taking up the full 30 hours, but the number who do that is very limited.”*

PVI setting representative

Interview data was used to construct a typology of settings, in order to illustrate some of the variation in settings’ characteristics, and the potential implications that an expansion to 30 hours might have for them.

For instance, setting type A in table 14, demonstrates the potential impact of an expansion in the free entitlement for a setting with a relatively low occupancy rate, and hourly fee rates for three- and four-year-old childcare below the hourly rate paid by the local authority for the free entitlement. Data from this study showed that 15 of the 57 settings that participated in this study, had a fee rate for three- and four-year-old childcare that was below that of the local authority fee rate for the free entitlement. In these cases, settings typically stated that the expansion would be beneficial for their setting, as it would help to increase occupancy, and allow the setting to receive a higher fee rate than it typically charged for additional hours outside of the free entitlement.

Table 14 presents a range of other setting types identified through this study, and the potential implications of the expansion to 30 hours for them.

**Table 14: Setting types and possible implications of an expansion of the free entitlement to 30 hours**

Type of setting	Impact of expansion to 30 hours
<p><b>A</b></p> <ul style="list-style-type: none"> <li>• Fee rate below local authority delegated rate</li> <li>• Relatively low occupancy levels</li> <li>• Some working parents of three- and four-year-olds buying additional hours</li> </ul>	<ul style="list-style-type: none"> <li>• Beneficial for setting</li> <li>• Allows setting to increase occupancy</li> <li>• Increase in revenue as fee rate for additional hours increases to local authority rate</li> </ul>

Type of setting	Impact of expansion to 30 hours
<b>B</b> <ul style="list-style-type: none"> <li>• Pre-school setting</li> <li>• Delivering only 15 to 25 hours per week</li> <li>• Not able to deliver additional hours within current setting</li> </ul>	<ul style="list-style-type: none"> <li>• Potentially detrimental to setting if unable to deliver 30 hours</li> <li>• May lose clients to competitors</li> <li>• Sustainability under threat</li> </ul>
<b>C</b> <ul style="list-style-type: none"> <li>• Nursery or preschool</li> <li>• Very few two-year-old funded children</li> <li>• High occupancy</li> <li>• Large number of children attending full-time</li> </ul>	<ul style="list-style-type: none"> <li>• Potential reduction in revenue from additional hours if local authority rate does not meet setting's fee rate</li> <li>• May lose clients to competitors if fails to offer 30 hours</li> <li>• Reduction in the number of hours available to 'cross-subsidise' any shortfall in local authority funding</li> <li>• Potential loss of large numbers of three- and four- year old children in summer leading to low autumn occupancy</li> </ul>
<b>D</b> <ul style="list-style-type: none"> <li>• Community based setting</li> <li>• Very few working parents</li> <li>• Very few families buying additional hours</li> </ul>	<ul style="list-style-type: none"> <li>• Potentially little impact on setting unless entitlement encourages parents into labour market</li> </ul>
<b>E</b> <ul style="list-style-type: none"> <li>• Nursery setting</li> <li>• Most children only accessing 15 hours of childcare</li> <li>• Few additional hours purchased by parents</li> </ul>	<ul style="list-style-type: none"> <li>• Potential 'displacement' as three and four-year-olds access 30 rather than 15 hours</li> <li>• Potential capacity issues for setting</li> </ul>

## **Appendix 1: List of local authorities whose settings participated in this study**

Blackburn with Darwen Council  
Calderdale Council  
Cambridgeshire County Council  
Central Bedfordshire Council  
City of York Council  
Derbyshire County Council  
East Sussex County Council  
Essex County Council  
Gloucestershire County Council  
Hertfordshire County Council  
Hull City Council  
Lancashire County Council  
London Borough of Barking and Dagenham  
London Borough of Enfield  
London Borough of Hackney  
London Borough of Lewisham  
London Borough of Southwark  
London Borough of Tower Hamlets  
Luton Borough Council  
Norfolk County Council  
Plymouth City Council  
Thurrock Council

## Appendix 2: Project pro forma

1	Please indicate whether you offer full day care or only sessional care.	<input type="checkbox"/> Sessional care only	<input type="checkbox"/> Full day care
2	Please indicate the ownership structure of your setting.	<input type="checkbox"/> Privately owned and managed <input type="checkbox"/> Voluntary sector <input type="checkbox"/> Other form of ownership (Please state).....	
3	Are you a single setting or does your organisation have settings on different sites/form part of a larger group of settings?	<input type="checkbox"/> Single setting <input type="checkbox"/> Settings on different sites/part of a larger group of settings (Please state total number of nurseries/settings in the group) .....	
4	Please state the number of places your setting is registered with Ofsted for currently.	Registered place capacity: ..... places	
5	What is the maximum place capacity your building could hold based on your usual mix of age ranges cared for?	Maximum building capacity: ..... places	

6	Please specify the age ranges of children who your care for in your setting (Please tick all that apply).	0-2 year olds <input type="checkbox"/>	2 year olds <input type="checkbox"/>	3 and 4 year olds <input type="checkbox"/>
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7	Please tick to indicate the days that you open for each week.	Mon <input type="checkbox"/>	Tues <input type="checkbox"/>	Weds <input type="checkbox"/>	Thurs <input type="checkbox"/>	Fri <input type="checkbox"/>	Sat <input type="checkbox"/>	Sun <input type="checkbox"/>
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8	Please state your opening and closing times: (Please use the 24 hour clock)	
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9	How many weeks per year do you open for?	..... weeks
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10	Please indicate the number of childcare staff who work within your setting.	Full-time	Part-time	Bank staff

11	Please indicate the qualification levels of your full-time and part-time childcare staff.	No formal qualifications	Apprentice	Level 2	Level 3	Level 4	Level 5	Level 6 (Degree)	Level 7 (Postgrad)

12	<p>Please provide your total income for your latest full year accounts – please include all sources of income.</p> <p>Please indicate the accounting year that this income relates to and whether or not the figure is an estimate.</p>	Total income: .....	<p>Is this figure an 'estimate'?</p> <input type="checkbox"/> Yes <input type="checkbox"/> No
		<p>Accounting year this figure relates to:</p> <p>.....</p>	

13	What proportion of your income is Local Authority funding for the free early education entitlement?	0-25%	26-50%	51-75%	76-100%
		<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

14	Please provide your total costs for your latest full year accounts.	Total costs: .....	<p>Is this figure an 'estimate'?</p> <input type="checkbox"/> Yes <input type="checkbox"/> No
		<p>Accounting year this figure relates to:</p>	

15	Please provide a breakdown of the following costs, starting with staffing costs and based on your latest full year accounts.	<b>Cost</b>	<b>Amount</b>
		A) Staffing Costs	£
		B) Rent or mortgage payments	£
		C) Materials used during provision	£
		D) Meals/catering	£
		E) Utilities	£
		F) Business rates	£
		G) Insurance	£
		Accounting year these figures relate to:	
16	<p>How many hours have you delivered for <b>0-2 year olds</b> in the last month, term or year (depending of which is easier for you to calculate)?</p> <p>This is the figure for children who are <b><u>under 2 years</u></b> old and too young to access the free entitlement for 2 year olds.</p>	Number of hours: .....	
17	<p>How many hours have you delivered for <b>2 year olds</b> in the last month, term or year (depending of which is easier for you to calculate)?</p> <p>This is the number of hours delivered for <b><u>all 2 year olds</u></b>. It includes children whether they are eligible for the free entitlement or not, and any extra hours bought by the parents of eligible children.</p>	Number of hours: .....	

18	<p>How many hours have you delivered for <b>3 and 4 year olds</b> in the last month, term or year (depending of which is easier for you to calculate)?</p> <p>This is the number of hours delivered for <b><u>all 3 and 4 year olds</u></b>. It includes children receiving the free entitlement and any extra hours bought by the parents of 3 and 4 year olds.</p>	Number of hours: .....	
19	<p><b>How many free entitlement hours have you delivered for 2, 3 and 4 year olds</b> in the last month, term or year (depending of which is easier for you to calculate)?</p>	Number of hours: .....	
20	<p>What are your prices per hour for additional hours bought by parents whose children are accessing the free education entitlement?</p>	2 year olds	£ .....per hour
		3 and 4 year olds	£ .....per hour



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