



# **POTENTIAL UNREALISED ACTIVITY TEST UNDERMINING BENEFITS OF UNIVERSAL PRE-SCHOOL**

**IMPACT ECONOMICS AND POLICY**

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## About Impact Economics and Policy

Impact Economics and Policy brings together a group of expert economists and policy specialists with experience working for government and non-for-profits. Established at the start of 2022, our mission is to partner with clients for impact through providing robust evidence, fresh analysis, and strategic communication to tackle Australia's biggest public policy challenges.

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## Acknowledgement of Country

*We acknowledge Aboriginal and Torres Strait Islander peoples as the Traditional Owners of Australia and their continuing connection to both their lands and seas. We also pay our respects to Elders – past and present – and generations of Aboriginal and Torres Strait Islander peoples now and into the future.*



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# OVERVIEW

Early childhood experts agree that every child would benefit from accessing early childhood education and care in the two years before commencing formal schooling. New modelling by Impact Economics and Policy estimates that the average benefits for each child of two years of pre-school are \$102,700 over the life course from increased educational attainment and the higher probability of completing school.

Realising these is benefits is one reason why state governments, led by New South Wales and Victoria, are moving to expand access to two years of universal pre-school. However, there are growing concerns that the operation of the Commonwealth Government's Activity Test will undermine the potential benefits of these state government efforts.

The Commonwealth Government's Activity Test limits access to the Child Care Subsidy if both parents are not engaged in sufficient work related activity. This increases the cost of early childhood education and care, and limits access particularly for children in families on low incomes.

As a result, every year Australian children are starting school developmentally behind their peers. Evidence shows that these children will never catch up, and will face the lifetime consequences of a policy that limits a child's access to early childhood education based on parental activity.

New estimates from Impact Economics and Policy using the Household Income and Labour Dynamic Survey finds that children subject to the Activity Test are less likely to be accessing adequate levels of early childhood education in the two years before formal schooling:

- 81.6 per cent of 3 year olds subject to the Activity Test are not receiving 15 hours per week; and
- 93.0 per cent of 4 year olds subject to the Activity Test are not receiving 30 hours per week.

Even with the New South Wales and Victorian state government policies to expand access to universal pre-school, families impacted by the Activity Test will face out of pocket costs of between \$7,000 and up to \$24,000 per child over two years to access pre-school. This will be unaffordable for many low to middle income families.

Impact Economics and Policy estimates that in New South Wales and Victoria up to 108,000 children risk missing out on universal access to pre-school each year and between \$5.9 billion and \$6.6 billion in lifetime benefits will be compromised due to the operation of the Commonwealth Government's Activity Test.

Previous research has shown that the Activity Test is largely impacting disadvantaged groups, and that it undermines workforce participation of mothers. This report provides further evidence to support growing calls including from the Productivity Commission, the Women's Economic Equality Taskforce, and the ACCC Childcare Inquiry to reform the Activity Test and ensure every child in Australia has access to quality early childhood education and care.

...every year Australian children are starting school developmentally behind their peers.

...in order to access Child Care Subsidy for their children, parents need to satisfy an Activity Test

# WHAT IS THE ACTIVITY TEST?

The Commonwealth Government provides support for families to access early childhood education and care, including pre-school in long day care settings, through the Child Care Subsidy. The Subsidy covers up to 90 per cent of the cost of early childhood education and care.

However, in order to access Child Care Subsidy for their children, parents need to satisfy an Activity Test. This test limits access to early childhood education and care of children if either parent is engaged in less than 24 hours per week of recognised activity.

Families can still access some Child Care Subsidy support if they fail the Activity Test but have family income below \$80,000 per annum. Even then the level of support is less than the recommended 30 hours of care in the year before school, with only 18 hours provided to low-income households. In most long day care settings, where 10 to 12 hours session times are the norm, this will only cover one full day of pre-school – well short of the recommended level for children to experience the positive outcomes from early childhood education and care.

TABLE 1 CURRENT ACTIVITY TEST REQUIREMENTS

Activity Test step	Hours of recognised activity per week	Hours of subsidised child care per week
	Up to 4 hour	0 hours
1	Up to 4 hours + means test	12 hours
1a	Exemptions for preschool	18 hours
2	4 hours to 8 hours	18 hours
3	More than 8 hours to 24 hours	36 hours
4	More than 24 hours	50 hours

Source: AIFS (2022), Child Care Package Evaluation: Final report: <https://aifs.gov.au/research/research-reports/child-care-package-evaluation-final-report>



## THE IMPORTANCE OF PRE-SCHOOL

Every child's development is influenced by a multitude of factors including their genetics, their family, their community, their environment, their access to health care and their access to education.<sup>1</sup> Ensuring every child has the best start and is developmentally on track at the start of school requires families and communities having access to the resources to support each child.<sup>2</sup>

Evidence highlights that children in lower income families often do not receive the same level of support in their development as children in higher income families.<sup>3</sup> Lower levels of parental education, higher levels of financial stress and less access to services all act to undermine the development of children in low income families.<sup>4</sup> In Australia this includes limitations on access to early childhood education and care based on parental labour market engagement due to the operation of the Activity Test.

Of all the government policies that aim to close the gap in developmental outcomes at age five, after reducing rates and severity of poverty, early childhood education and care has the strongest evidence base.<sup>5</sup> Other interventions such as parenting programs can be beneficial, but are not supported by the evidence as having the same long term impacts as early childhood education and care.<sup>6</sup>

### BENEFITS OF EARLY CHILDHOOD EDUCATION AND CARE

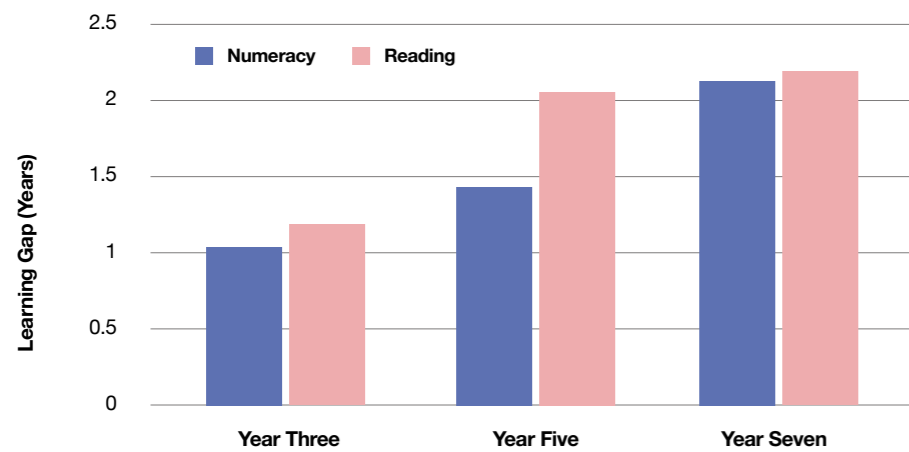
Children who start school developmentally vulnerable never catch up, with studies showing that these children fall further and further behind as they progress through school.

Four in five children that attend early childhood education are developmentally on track at the start of school, but only three in five who did not attend early childhood education are on track.<sup>7</sup> Once children are behind, it becomes very hard for them to catch up and evidence indicates they fall further behind during the school years.<sup>8</sup>

Lower levels of parental education, higher levels of financial stress and less access to services all act to undermine the development of children in low income families.

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FIGURE 1 LEARNING GAP BETWEEN THOSE DEVELOPMENTALLY VULNERABLE AND DEVELOPMENTALLY ON TRACK AT THE START OF SCHOOL (YEARS)



Source: Based on analysis of NAPLAN data by Murdoch's Children's Research Institute

It is well established in research studies that access to quality early childhood education and care, especially two years before school starts, is linked to improved child development at the start of the school, and long-term benefits including improved academic achievement, reduced delinquency, increased school completion, higher earnings in adulthood, and improved social and emotional well-being.<sup>9</sup>

A number of international studies show that pre-school is linked to positive cognitive and social development outcomes at school.<sup>10</sup> A major UK study tracked the progress of a broad range of children who attended two to three years of high-quality preschool in the late-90s. These children were six to eight months ahead in literacy when they started school, regardless of socio-economic background. At age 16, participating children scored higher in secondary exams, and were more likely to go on to higher education and

ultimately earn higher incomes.<sup>11</sup>

In the Australian context, one quasi-experimental study shows that preschool attendance at age four has a positive influence on children's cognitive development by as much as 15 NAPLAN points in Year 3, after taking into account a child's family background and innate ability.<sup>12</sup>

There is also evidence that access is even more important for children from low-socio economic families. Across a number of studies, in a number of different contexts research has found that children from lower socio-economic groups experience greater and more enduring benefits than children from higher socio-economic groups.<sup>13,14</sup> Because the current system is resulting in underrepresentation of children from disadvantaged groups attending pre-school, it is compounding existing disadvantage.<sup>15</sup>

A number of international studies show that pre-school is linked with positive cognitive and social development outcomes at school.<sup>10</sup>

8. The Centre for Adolescent Health, Murdoch Children's Research Institute (2018). The Effects on Schooling Outcomes of Early Developmental Vulnerabilities in Children, Canberra: Australian Government Department of Education and Training.
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A recent 2019 report on Australian-based Early Years Education Program demonstrated the benefits from access to quality care for disadvantaged children and their carers<sup>16</sup>:

- An increase in children's IQ scores of 5 points;
- A 31.6 per cent reduction in number of children with social and emotional scores in the clinical range; and
- A 1.5 point reduction in psychological distress scores of primary caregivers.

### How much early childhood education and care is optimal?

Attending two years of pre-school is linked to a higher probability of school completion<sup>17</sup>, which improves life-long outcomes across employment, education, health and other domains.<sup>18</sup> These impacts have been found to be particularly strong for children from low socio-economic backgrounds.<sup>19</sup>

In terms of the number of hours of early childhood education and care that is optimal evidence suggests positive effects up to 25 hours per week.<sup>20</sup> At very high levels of participation, where children exceed 35 hours per week in formal settings, there are potential negative impacts on socio-emotional outcomes, however, a more qualified workforce may mitigate these negative effects.<sup>21</sup>

All these benefits have led a number of experts – including a 2021 report by an Australian independent think tank Centre for Policy Development – to conclude that every Australian child should have access to a minimum three days a week of early childhood education and care.<sup>22</sup>

The Governments in NSW and Victoria and the Royal Commission in South Australia have recommended 15 hours of pre-school for three year olds and 30 hours of pre-school for four year olds.

16. Tseng YP, Jordan B, Borland J, Coombs N, Cotter K, Guillou M, Hill A, Kennedy A and Sheehan J. '24 months in the Early Years Education Program: Assessment of the impact on children and their primary caregivers', Changing the Trajectories of Australia's Most Vulnerable Children, Report No. 4 (May 2019).
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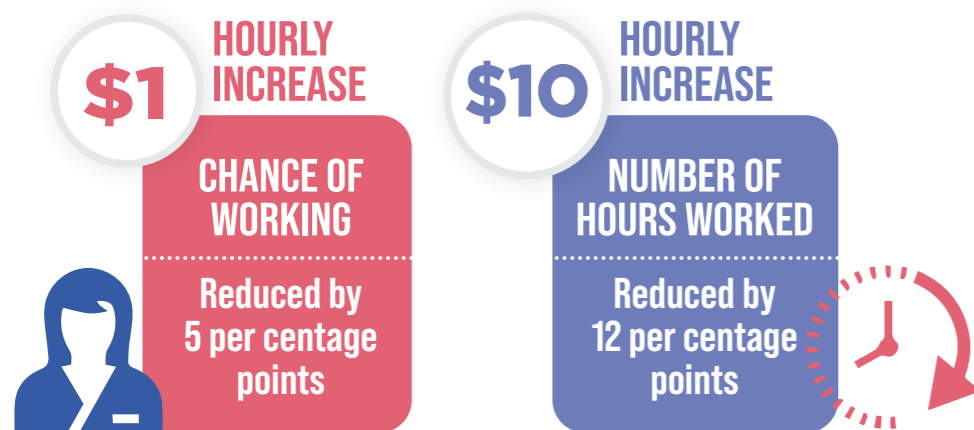
# IMPACT OF CHILD CARE ACCESS ON FEMALE PARTICIPATION

While all adult members of a family are responsible for childcare costs, research finds that it is the labour force participation of women, as the primary carers, that is impacted by both the accessibility and cost of early childhood education and care.<sup>23</sup>

As a result, greater access to early childhood education and care increases female participation in paid work.<sup>24</sup> Recent Australian research has found women living in regions characterized as “childcare deserts” where there is not ready access to early childhood education and care, have reduced rates of workforce participation.<sup>25</sup>

Lower female workforce participation in “childcare deserts” not only influences the demand for childcare services but may also result from the challenges associated with obtaining suitable childcare, leading to parents and caregivers opting out of the workforce during the early years of their children’s lives.

The cost of child care also has an impact on female participation in paid work. Various estimates exist in the literature, with a recent Australian study finding that a ten dollar per hour increase in child care costs reduced the probability of primary carer’s being employment by 5 per centage points. Where the primary carer was already employed, a ten dollar increase in hourly costs reduced the total hours worked by 12 per cent.<sup>26</sup>



Research by Impact Economics and Policy on the effect of the Activity Test on female participation found that it increased the search costs for women looking to return to work after having children, and that abolishing the Activity Test could increase female participation by up to 39,620 and deliver economic benefits of \$4.5 billion per year.<sup>27</sup>

...greater access to early childhood education and care increases female participation in paid work.<sup>24</sup>

23. Breunig, Robert, et al. "Child care availability, quality and affordability: are local problems related to labour supply?" *Economic Record* 87.276 (2011): 109-124; Bousselein A. Access to universal childcare and its effect on maternal employment. *Rev Econ Househ.* 2022;20(2):497-532. doi: 10.1007/s11150-021-09572-9. Epub 2021 Jul 1. PMID: 34226822; PMCID: PMC8245926; Landivar, Liana Christin, et al. "Do high childcare costs and low access to Head Start and childcare subsidies limit mothers' employment? A state-level analysis." *Social Science Research* 102 (2022): 102627.

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# AUSTRALIAN CHILDREN MISSING OUT

Australian children are currently guaranteed 15 hours of pre-school in the year prior to starting school under the National Partnership Agreement on Early Childhood Education.<sup>28</sup> However, this falls short of expert research which finds children benefit from having access to early childhood education and care in the two years before formal school.<sup>29</sup>

The South Australian Royal Commission into Early Childhood Education and Care heard evidence that there were benefits from children receiving at least 15 hours in 3 year old and 30 hours in 4 year old pre-school programs.<sup>30</sup>

Analysis by Impact Economics and Policy shows that under current arrangements Australian children are missing out. Using the the Household Income and Labour Dynamics Survey Impact Economics and Policy finds

that almost 400,000 three and four year old children are not receiving the recommended amount of early childhood education and care, this represents two-thirds of Australian children.

Children that reside in households with lower incomes, or have parents that are subject to the Activity Test are more likely to be missing out on the recommended level of early childhood education and care before starting formal schooling.

TABLE 2 CHILDREN NOT RECEIVING RECOMMENDED 15 HOURS OF THREE YEAR OLD AND 30 HOURS OF FOUR YEAR OLD EARLY CHILDHOOD EDUCATION AUSTRALIA

	All children	Impacted by Activity Test	< 80 k Household Income
Do not receive recommended level of care (%)	67 per cent	87 per cent	79 per cent
Do not receive recommended level of care (number)	399,000	201,000	99,100

Source: Impact Economics and Policy analysis of Wave 21 of Household Income and Labour Dynamics Australia survey.

28. The National Partnership is the agreement between the Commonwealth and State and Territory Governments that underpins universal access to 15 hours of four year old kinder.

29. Deloitte Access Economics (2023), Three-year-old Preschool Return on Investment Analysis, Royal Commission into Early Childhood Education and Care, Attorney General's Department

30. Ibid.

# STATE GOVERNMENT EXPANSION OF PRE-SCHOOL SERVICES

In recognition of the high number of Australian children missing out on adequate levels of early childhood education and care, a number of state and territory governments are taking action.<sup>31</sup> Policies have been announced in a number of jurisdictions to either implement or trial programs to provide universal access to early childhood education and care in the two years before formal school starts.

In June 2022 the Premiers of NSW and Victoria committed to universal 3 and 4 year old kinder programs by 2030. The programs will involve a new entitlement to 15 hours of 3 year old kinder, and an expanded access to 30 hours of 4 year old kinder. This announcement remains the most comprehensive commitment towards two years of universal pre-school, however other states are all making progress.

**South Australia**, informed by its Royal Commission into Early Childhood Education and Care, has announced a targeted aspiration to deliver universal access for 3 and 4 year olds that

prioritises higher need groups, including Aboriginal and Torres Strait Islander children.<sup>32</sup> The Royal Commission recommended a ‘progressive universalism’ approach offering 30 hours of preschool access for the most disadvantaged children, and 15 hours for all other children.

**Tasmania** has been running a pilot program offering 20 hours of free early childhood education and care for 48 weeks a year for around 300 disadvantaged 3 year olds in long day care settings.<sup>33</sup> The Government is also trialling an expansion of the 3 year old kinder program in a number of sites across the state.<sup>34</sup>

The **Australian Capital Territory** has announced it will fund preschool programs for 3 year olds in long day care services commencing in 2024, initially funding 7.5 hours of early childhood education and care with an aspiration to increase that over time.<sup>35</sup>

The **Northern Territory** Government provides an ongoing subsidy for all children in early childhood education and care services,<sup>36</sup> and has been trialling the provision of 3 year old preschool in six schools.<sup>37</sup>



TABLE 3 OVERVIEW OF STATE GOVERNMENT POLICIES

	Current Arrangements		Announced Policies	
	3 Year Old	4 Year Old	3 Year Old	4 Year Old
<b>NSW</b>	No provision	15 hours	15 hours	30 hours
<b>VIC</b>	No provision	15 hours	15 hours	30 hours
<b>QLD</b>	No provision	15 hours	No provision	15 hours
<b>WA</b>	No provision	15 hours	No provision	15 hours
<b>SA</b>	No provision	15 hours	15 hours*	15 hours/30 hours*
<b>TAS</b>	No provision	15 hours	Trials of 10 hours	15 hours
<b>ACT</b>	No provision	15 hours	15 hours*	15 hours
<b>NT</b>	No provision	15 hours	No provision	15 hours

\*for children that are developmentally vulnerable moving towards universal

31. See Appendix One for a full summary of state and territory policies

32. Royal Commission into Early Childhood Education and Care (2023), Report, South Australia 2023

33. Tasmanian Department for Education, Children and Young People (2023), Working Together – Information for Families <https://www.decyp.tas.gov.au/learning/early-years/working-together/working-together-for-families/>

34. Premier of Tasmania (2023), Media Release: Early Learning for Three Year Old trial sites revealed, 10 August 2023

35. ACT Government Department of Education, Coming Soon: Free three year old preschool, <https://www.education.act.gov.au/early-childhood/coming-soon-free-three-year-old-preschool>

36. NT Government, Information for Childcare Providers: <https://nt.gov.au/learning/early-childhood/information-for-child-care-providers/early-childhood-services-subsidy>

37. Chief Minister of Northern Territory Media Release, Three Year Old Preschool Delivering for Territory Kids, 22 March 2022

# HOW WILL EXPANDED PRE-SCHOOL SERVICES BE DELIVERED?

The majority of children currently using early childhood education and care in the two years before starting school are doing so at least in part in long day care centres rather than government run or community centres. As a result, the governments in New South Wales, Victoria, South Australia and Tasmania, have explicitly signalled that long day care centres will need to provide the bulk of additional hours of care in order to expand access for 3 year olds.

Pre-school is provided in a variety of settings in Australia, including government run programs, community run programs and long day care centres. Nationally, 42% of all children enrolled in preschool in the year before formal schooling do so exclusively in a long day care centre, with a further 13% attending both a government run or community centre and long day care preschool programs.<sup>38</sup> In aggregate, 55 per cent of children nationally attend pre-school in the year before formal schooling in a long day care setting.

## OUT OF POCKET COSTS FOR FAMILIES

Any efforts by state governments to expand access to pre-school through the use of long day care rely on children being supported by the Commonwealth Government's Child Care Subsidy. Where families cannot access this Commonwealth support due to the operation of the Activity Test, they will face much higher out of pocket costs, limiting access.

A single day of long day care costs \$120 on average without the Commonwealth Government's Child Care Subsidy. This is a substantial cost of up to \$28,000 over two years, and represents a risk to state government initiatives to expand access to pre-school.<sup>39</sup> Even with the NSW and Victorian Government reforms, out of pocket costs will remain very high for families ineligible for any support from the Commonwealth Government:

- In NSW families will face out of pocket costs of up to \$25,600 to access two years of pre-school in a long day care setting.
- In Victoria families will face out of pocket costs of up to \$24,000 to access two years of pre-school in a long day care setting.

A single day of long day care costs \$120 on average without the Commonwealth Government's Child Care Subsidy. This is a substantial cost of up to \$28,000 over two years, and represents a risk to state government initiatives to expand access to pre-school.

38. Productivity Commission (2023), Report on Government Services 2023, Early Childhood Education and Care Table 3A.17

39. As a conservative assumption this is based on people being able to access exactly 15 hours and 30 hours of care through long day care. In reality, long day care centres offer sessions of between 10 and 12 hours per day, so in order to access 15 hours families would need to enrol for 2 days or up to 24 hours and to access 30 hours families would need to enrol for a minimum of 3 days and up to 4 days.

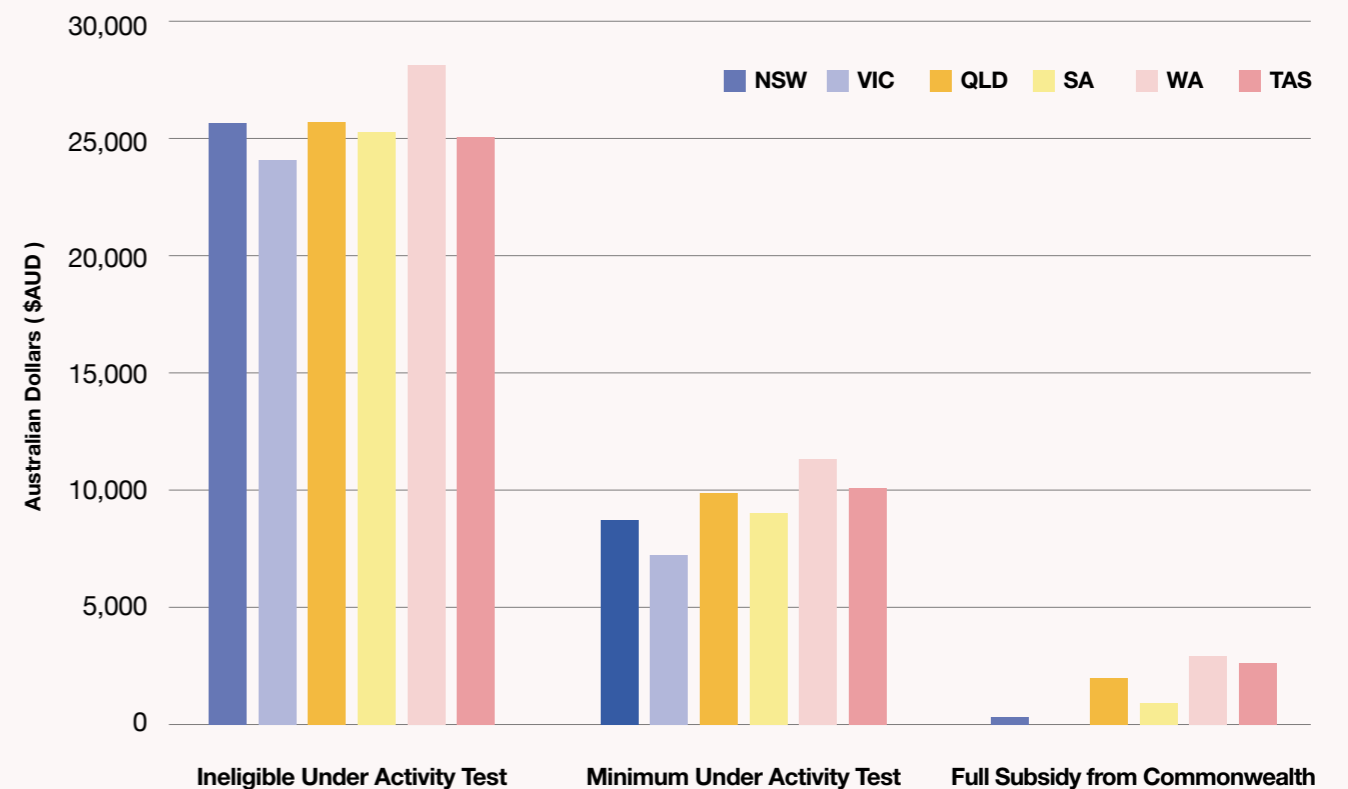
Families with household income under \$80,000 that can access the minimum hours under the Activity Test still face out of pocket costs of \$11,000 over the two years. The reforms announced in NSW and Victoria will reduce these costs, but they will remain unaffordable for many of these families:

- In NSW families will face out of pocket costs of up to \$8,600 to access two years of pre-school in a long day care setting.
- In Victoria families will face out of pocket costs of up to \$7,150 to access two years of pre-school in a long day care setting.

Even for families that can access the full Commonwealth subsidy, the costs of two years of pre-school without state government support is around \$3,000. This highlights the impact of the state government policies to improve affordability:

- In NSW families will face out of pocket costs of up to \$213 to access two years of pre-school in a long day care setting.
- In Victoria families will face no out of pocket costs to access two years of pre-school in a long day care setting.

FIGURE 1 OUT OF POCKET COSTS FOR PRE-SCHOOL



Source: Impact Economics and Policy analysis based on announced state government funding and average rebates under Child Care Subsidy for different groups.





## WHAT ARE THE POTENTIAL BENEFITS OF UNIVERSAL PRE-SCHOOL?

The benefits from expanding access to universal 3- and 4-year-old early childhood education and care accrue to children, families, the early childhood education and care workforce, government and broader society.<sup>40</sup>

In this report we focus on the benefits that flow from improved developmental outcomes for children. Some of these benefits accrue directly to children, while others accrue to families, workers, society and government.

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TABLE 4 POTENTIAL BENEFITS FROM ACCESS TO EARLY CHILDHOOD EDUCATION AND CARE

Children		Families	ECEC Workforce	Society	Government
School readiness	Further education	Identification and access to supports	Efficiencies from working with the same children	Human capital accumulation and productivity	Increased tax receipts
Academic outcomes	Workforce participation	Higher-quality interactions with children		Reduced criminal activity	Cost saving from criminal justice
School retention and completion	Lifetime earnings			Reduced inequality	Avoided school intervention costs
Early development outcomes	Health outcomes				Cost savings in health and social welfare system
Lower vulnerability	Parenting and 2nd generation effects				

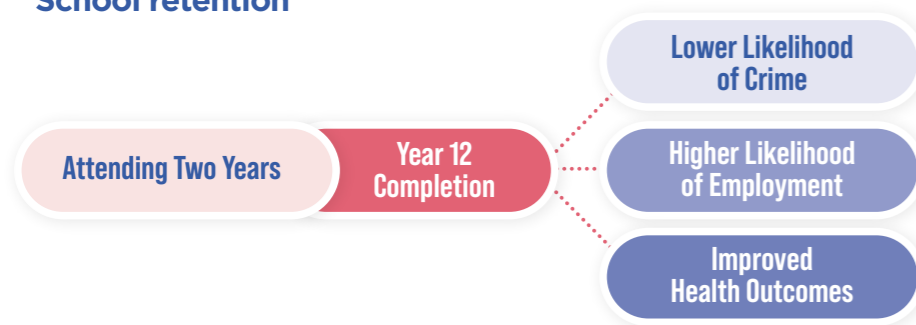
Source: Deloitte Access Economics (2023), Three-year-old Preschool Return on Investment Analysis, Royal Commission into Early Childhood Education and Care, Attorney General's Department

40. Deloitte Access Economics (2023), Three-year-old Preschool Return on Investment Analysis, Royal Commission into Early Childhood Education and Care, Attorney General's Department

A number of approaches have been developed to quantify the potential benefits of early childhood education and care. In this report we explore two avenues, which quantify the benefits from improved child outcomes on:

- School retention
- Lifelong earnings

### School retention



The economic and social cost of someone not completing school are high, with lower lifelong earnings and higher costs associated with health care and criminal justice. A 2017 study from the Mitchell Institute estimated that the costs of early school leavers and disengaged young people equated to \$1.1 million per person over the life course, in 2022 dollars.<sup>41</sup>

Based on international research that has established a causal link, Impact Economics and Policy estimates that the provision of two years of universal pre-school will increase school completion rates by 6 per cent.<sup>42</sup>

Across Australia, this equates to between an additional 18,100 and 23,900 children finishing school each year. This would deliver estimated lifetime fiscal and social benefits of \$20.6 billion to \$27.3 billion.

### Lifelong Earnings

A strong link has been established between educational attainment and lifelong earnings.<sup>43</sup> In the Australian context, it has been previously estimated that an additional year of schooling lifts lifelong earnings by 10 per cent.<sup>44</sup>



Research undertaken for the South Australian Royal Commission using the Longitudinal Survey of Australian Children found that the attending two years of pre-school lifted Naplan results across a number of domains of learning, by the equivalent of between 4 and 6 months of schooling in year 9.<sup>45</sup>

**Impact Economics and Policy estimates that the provision of two years of universal pre-school will increase school completion rates by 6 per cent.**

41. Impact Economics and Policy calculations using Lamb, Stephen and Huo, Shuyan (2017) *Counting the costs of lost opportunity in Australian education*. Discussion Paper. Mitchell Institute, Melbourne, Victoria and ABS (2023), Consumer Price Index  
 42. See Appendix for methodology  
 43. Card, D., & Ashenfelter, O. (Eds.). (1999). *Handbook of labor economics*.  
 44. Andrew Leigh, 2007. "Returns to Education in Australia," CEPR Discussion Papers 561, Centre for Economic Policy Research, Research School of Economics, Australian National University.  
 45. Deloitte Access Economics (2023) using LSAC data and conversion based on Equivalent Years of Learning measure developed by the Grattan Institute.

TABLE 5 AVERAGE EFFECT OF NAPLAN SCORES IN TERMS OF EQUIVALENT MONTHS OF LEARNING

Naplan Domain	Year 3	Year 5	Year 7	Year 9
Grammar	4.65***	4.11**	4.77*	2.44
Numeracy	1.89**	4.56**	6.19***	3.98*
Reading	5.20***	4.92**	5.30**	6.50***
Spelling	2.30*	2.10*	4.49**	3.89
Writing	2.11	1.77	4.43*	3.88**

Significance Levels: \*10%, \*\*5%, \*\*\*1%

Assuming conservatively that attending two years of early childhood education and care before starting school lifts educational attainment by the equivalent of 4 months, this would equate to a 3.3 per cent lift in lifetime earnings for all children that benefit.

If implemented across Australia, Impact Economics and Policy estimates that this would represent between \$10.9 billion and \$14.5 billion in additional earnings over the lifetime for children.

### Total benefits

The total benefits to a child comprise of both the higher probability of school retention and higher levels educational attainment. To avoid double counting we exclude the estimates of higher earning for the group that finishes school due to the policy.

On average the economic and social benefits of attending pre-school calculated in this report are \$102,706 per child that attends two years of pre-school. Our calculations are based on these benefits being realised with attendance of between 15 and 30 hours per week in both years prior to starting school.

If implemented across Australia, universal pre-school for 3 and 4 year olds could generate benefits of between \$30.9 and \$40.9 billion.

These potential benefits would occur in each state and territory. In NSW and Victoria, the potential lifelong economic and social benefits of the policy to provide universal access to pre-school in the two years before formal school are estimated at between \$19.4 billion and \$24.0 billion.

		Australia	NSW	VIC	QLD	SA	WA	TAS	ACT
Number of Children	Lower	302,000	120,500	68,750	67,500	11,600	23,700	7,800	1,600
	Upper	399,000	136,500	97,000	74,000	29,800	43,700	13,200	1800
Lifelong Benefits	Lower	\$30.9b	\$12.4b	\$7.1b	\$6.9b	\$1.2b	\$2.4b	\$0.8b	\$168m
	Upper	\$40.9b	\$14.0b	\$10.0b	\$7.6b	\$3.1b	\$4.5b	\$1.4b	\$185m

Source: Impact Economics and Policy Modelling (please see Appendix for methodology). Note NT sample size too small for reliable estimates.

# LOST BENEFITS DUE TO OPERATION OF ACTIVITY TEST

The potential benefits of the state government expansion in universal pre-school could be lost due to the operation of the Activity Test. Our analysis uses the benchmark as set by Victoria, New South Wales and the South Australian Royal Commission of 15 hours of pre-school for 3 year olds and 3 hours of pre-school for 4 year olds.

Analysis by Impact Economics and Policy of HILDA data estimates that of the 400,000 children not receiving adequate levels of early childhood education and care in the two years before school commences, close to half are impacted by the Activity Test.

The potential benefits of the state government expansion in universal pre-school could be lost due to the operation of the Activity Test.

TABLE 6 CHILDREN NOT RECEIVING ADEQUATE LEVELS OF PRE-SCHOOL BY STATE (3 YEAR OLD AND 4 YEAR OLD)

	Total children who do not pass activity test	Total children	Per cent
NSW	64,014	136,553	47%
VIC	44,586	97,059	46%
QLD	49,827	74,181	67%
SA	12,599	29,828	42%
WA	24,860	43,697	57%
TAS	3,687	13,166	28%
NT	673	2,831	24%
ACT	1,402	1,808	78%
Australia	201,647	399,123	51%

Source: Impact Economics and Policy Estimates Using HILDA (see Appendix for Methodology)

State government efforts to increase access therefore will be impacted by the operation of the Activity Test, with many families unable to access the Commonwealth Government's Child Care Subsidy.

## New South Wales and Victoria

The New South Wales and Victorian Governments have announced major reforms and an expansion in access to early childhood education and care, including the scaling up of community and government run providers. However, they will both rely heavily on the long day centre system and funding through the Child Care Subsidy to support access to universal pre-school.

The efforts of the NSW and Victorian governments will be undermined by the operation of the Activity Test that will limit access to universal pre-school for children in families that fail the test. Currently in both these states 108,000 of three and four year old children are not receiving the recommended level of pre-school are impacted by the Activity Test.

TABLE 7 CHILDREN IN FAMILIES THAT DO NOT MEET THE ACTIVITY TEST THAT DO NOT RECEIVE RECOMMENDED 15 HOURS OF THREE YEAR OLD AND 30 HOURS OF FOUR YEAR OLD EARLY CHILDHOOD EDUCATION - NEW SOUTH WALES AND VICTORIA

Families	All children	Impacted by Activity Test	<80 k household income
Do not receive recommended level of care (%)	67 per cent	89 per cent	68 per cent
Do not receive recommended level of care (number)	233,612	108,000	39,000

Source: Impact Economics and Policy analysis of Wave 21 of Household Income and Labour Dynamics Australia survey.

While a proportion of these children are likely to benefit from the NSW and Victorian Government policies to expand access through attending government run or stand alone pre-schools, many will miss out or face high out of pocket costs.

## Unrealised Benefits Due to the Activity Test

Impact Economics and Policy modelling estimates that if all state governments follow NSW and Victoria's lead and commit to two years of universal pre-school, between 97,000 and 111,000 will have their access impacted by the Activity Test. This estimate accounts for a proportion of children impacted by the Activity Test being able to attend government run or fully funded pre-schools.

The lifelong economic losses would equate to between \$10.1 billion and \$11.5 billion per year across Australia.<sup>46</sup> These losses would be concentrated in NSW, Victoria and Queensland because these states rely more heavily on long day care centres to deliver pre-school than in other states.

		Australia	NSW	VIC	QLD	SA	WA	TAS	ACT
Number of Children	Lower	97,000	35,900	21,700	31,000	1,700	9,500	790	560
	Upper	111,000	41,500	22,800	32,900	3,600	10,900	930	650
Lifelong Benefits	Lower	\$10.1b	\$3.7b	\$2.2b	\$3.2b	\$172m	\$1.0b	\$81m	\$67m
	Upper	\$11.5b	\$4.2b	\$2.3b	\$3.4b	\$367m	\$1.1b	\$95m	\$57m

Source: Impact Economics and Policy Modelling (please see Appendix for methodology). Note NT sample size too small for reliable estimates.

46. This assumes current attendance rates for pre-school at long day care are maintained.

## CONCLUSION

Australian children are missing out on the benefits of early childhood education and care, and government action is needed to increase access.

Families subject to the Activity Test face out of pocket costs for pre-school in long day care settings of up to \$24,000 over two years. This undermines state government attempts to expand access and reduces the potential economic and social benefits.

Abolishing the Activity Test will help ensure that all children have access to universal pre-school in the two years before starting school, and underpin significant long term economic and social benefits.

Families subject to the Activity Test face out of pocket costs for pre-school in long day care settings of up to \$24,000 over two years.



# APPENDIX 1

## OVERVIEW OF STATE GOVERNMENT POLICIES AND INTERACTION WITH THE ACTIVITY TEST

Jurisdiction	Policy entitlement (2024)	Key milestones	Contextual Information	Interaction with Activity Test
<p>Note: There is an Activity Test exemption for preschool, with children eligible to attend 36 hours of subsidised long day care per fortnight in the year before school. However, most long day care services (80%) offer 10 hour session lengths. Two days a week preschool at long day care would exceed the exemption by at least 4 hours.<sup>47</sup> National preschool reform agreement provides 15 hours preschool per week for 40 weeks a year (600 hours).</p>				
Victoria	<p>Free 5-15 hours/week <b>3 year old</b> kindergarten*</p> <p>Subsidised up to 15 hours/week in long day care*</p>	<p>Present to 2028: 5-15 funded hours based on geography. Early start kindergarten for vulnerable children provides 15 hours of funded 3 year old kindergarten<sup>48</sup></p> <p>2029: 15 hours funded 3 year old kindergarten all children<sup>49</sup></p>	<p>~64% 3 year olds in long day care across Australia<sup>50</sup></p> <p>3 year old preschool requires at least 2 days attendance per week in long day care</p>	<p>No exemption from Activity Test</p> <p>Based on 10 hours sessions, two days a week long day care would exceed 24 hour a fortnight Activity Test and 36 hour a fortnight for Aboriginal and Torres Strait Islander children Activity Test</p>
	<p>Free 15 hours/week <b>4 year old</b> kindergarten*</p> <p>Subsidised 15 hours/week in long day care*</p> <p>*Subsidies vary based on factors including enterprise agreement and location. In 2023 each 15 hour enrolment attracted base funding of \$3831 per child plus \$2500 per child to cover fees in kindergarten or \$2000 to offset fees in long day care. Long day care can still charge fees but must offset these by \$2,000<sup>51</sup></p>	<p>From 2025: Rollout 16-30 hours funded 4 year old kindergarten pre-prep commencing in rural shires, with new areas being added progressively</p> <p>2026: Aboriginal and vulnerable children eligible for 16-30 hours per week of 4 year old kindergarten pre-prep</p> <p>2028: Disadvantaged children eligible for 16-30 hours per week of 4 year old kindergarten pre-prep</p> <p>2030: All families in metropolitan Melbourne eligible to access 16-20 hours of pre-prep</p> <p>2032: All children eligible for 30 hours pre-prep<sup>52</sup></p>	<p>30 hours pre-prep likely to be based on at least 4 days of attendance per week</p> <p>43% Victorian children enrolled in 4 year old preschool through solely long day care<sup>53</sup></p>	<p>Activity test exemption provides 36 hours/fortnight subsidy for preschool – less than 2 days per week based on average session length</p>

47. <https://aifs.gov.au/research/research-snapshots/service-charging-practices-and-sessions-care>

48. <https://www.vic.gov.au/sending-child-kinder>

49. <https://www.vic.gov.au/sending-child-kinder>

50. <https://www.education.gov.au/early-childhood/resources/june-quarter-2023-data-tables>

51. <https://www.vic.gov.au/kindergarten-funding-rates>

52. <https://www.vic.gov.au/pre-prep>

53. ABS (2023) Preschool Australia <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>

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Jurisdiction	Policy entitlement (2024)	Key milestones	Contextual Information	Interaction with Activity Test
New South Wales	Funded 15 hours/week <b>3 year old</b> preschool in community preschools <sup>54*</sup>  \$500 subsidy towards 3 year old program in long day care <sup>55</sup>		~64% 3 year olds in long day care across Australia <sup>56</sup>	No exemption from Activity Test  Based on 10 hours sessions, two days a week long day care would exceed 24 hour a fortnight Activity Test and 36 hour a fortnight for Aboriginal and Torres Strait Islander children Activity Test
	Funded/subsidised 15 hours/week <b>4 year old</b> preschool in community preschools and long day care*  *In 2023 each 15 hour enrolment attracted variable based funding of up to \$7466 dependant on equity factors and funding of \$4220 per child in community preschool. For children in long day care \$960 per four year old enrolment plus or \$2000 plus to offset fees <sup>57</sup>	Universal preschool–30 hours per week/5 days a week announced by former government  New government has preserved funding for this	30 hours per week Pre-prep likely to be over 5 days a week to align with school  64% of NSW children were enrolled in 4 year old preschool solely in long day care <sup>58</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool. 5 days a week in long day care would greatly exceed this
Queensland	Free 15 hours/week Deadly Kinder for <b>3 and 4 year old</b> Aboriginal and Torres Strait Islander Children <sup>59</sup>  Funded KindyLinQ 6 hour/week facilitated playgroup for <b>0-3 year olds</b> <sup>60</sup>	3 Deadly Kinders		
	Free 15 hours/week <b>4 year old</b> kindergarten.* Subsidised 15 hours/week in long day care <sup>61*</sup>  *In 2023 funding provided to kindergarten varied according to family circumstances and service location, with a base amount of funding of \$5,524.50 per child <sup>62</sup>  Similarly in long day care payments varied according to family circumstances and service location, with a base amount of funding of \$1,919.50 per child <sup>63</sup>  Funding rates for 2024 are still to be announced but it is likely around \$4,600 will be provided to offset fees <sup>64</sup>	Universal preschool–30 hours per week/5 days a week announced by former government  New government has preserved funding for this	~70% of Queensland children were enrolled in 4 year old kindergarten solely in long day care <sup>65</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool – less than 2 days per week based on average session length

54. <https://education.nsw.gov.au/early-childhood-education/operating-an-early-childhood-education-service/grants-and-funded-programs/start-strong-funding>55. <https://www.nsw.gov.au/media-releases/500-preschool-fee-relief>56. <https://www.education.nsw.gov.au/early-childhood-education/resources/june-quarter-2023-data-tables>57. <https://education.nsw.gov.au/early-childhood-education/operating-an-early-childhood-education-service/grants-and-funded-programs/start-strong-funding/start-strong-for-long-day-care/2023-start-strong-for-long-day-care-program-guidelines#3.2>58. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>59. <https://www.deadlykindy.org.au/faqs/>60. <https://earlychildhood.qld.gov.au/early-years/options-for-care-and-early-learning/kindylinq>61. <https://statements.qld.gov.au/statements/97916>62. <https://earlychildhood.qld.gov.au/fundingAndSupport/Documents/kindy-funding-essentials-sessional-kindergartens.pdf>63. <https://earlychildhood.qld.gov.au/grants-and-funding/kindergarten-funding/funding-essentials-for-long-day-care-providers#grants>64. <https://www.abc.net.au/news/2023-06-13/kindy-to-be-made-free-for-all-queensland-families-state-budget/102470736>65. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>

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Jurisdiction	Policy entitlement (2024)	Key milestones	Contextual Information	Interaction with Activity Test
South Australia	Funded 12 hours/week <b>3 year old</b> preschool for Aboriginal children and children in care <sup>66</sup>	2026 - 2032: Royal Commission rec – 15 hr 3yo preschool in mixed settings (stand alone preschool and long day care)		No exemption from Activity Test. Based on 10 hours sessions, two days a week long day care would exceed 24 hour a fortnight Activity Test and 36 hour a fortnight for Aboriginal and Torres Strait Islander children Activity Test
	Free 15 hours/week <b>4 year old</b> preschool  Subsidies to of up to @\$2,530 per child enrolled in 15 hours long day care to offset teacher cost <sup>67</sup>	2024 - 2032: Move to longer hours – 30 hours 3 and 4 for children most vulnerable, mixed settings (stand alone preschool and long day care) <sup>68</sup>	32% of South Australian children were enrolled in 4 year old kindergarten solely in long day care <sup>69</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool. 30 hours a week would exceed this
Western Australia	Funded 6 hour/week Kindilink program – Aboriginal <b>3 year old</b> playgroup delivered by teacher and assistant with parental attendance			
	Funded 15 hours/week <b>4 year old</b> preschool at school or community preschool  Subsidised at non govt schools but not at long day care at present <sup>70</sup>		68% of Western Australian children were enrolled in kindergarten solely in school and under 6% solely in long day care <sup>71</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool – less than 2 days per week based on average session length
Tasmania	Funded places in long day care for 2-3 days a week for <b>3 year olds</b> who meet a variety of conditions, and are not currently at long day care as part of Working Together program <sup>72</sup>			
	Funded 15/hours a week <b>4 year old</b> kindergarten on school sites		58% of Tasmanian children were enrolled in kindergarten solely on a school site and 27% solely in long day care <sup>73</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool – less than 2 days per week based on average session length

66. <https://www.education.sa.gov.au/parents-and-families/enrol-school-or-preschool/preschool-and-kindergarten-enrolment/when-your-child-can-start-preschool>67. <https://www.education.sa.gov.au/docs/early-years/preschool/non-govt-preschool-funding-agreement-template.pdf>68. <https://www.education.sa.gov.au/department/research-and-statistics/reviews-and-responses/royal-commission-into-early-childhood-education-and-care#government-response-to-final-report-recommendations>69. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>70. <https://www.education.wa.edu.au/kindilink>71. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>72. <https://decyp.dev.ionata.com/learning/early-years/working-together/>73. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>

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Jurisdiction	Policy entitlement (2024)	Key milestones	Contextual Information	Interaction with Activity Test
Northern Territory	Remote and very remote preschool from <b>3 years old</b> , Three-year-old children from remote areas can attend preschool but must be accompanied by a parent until age 3.5			
	Funded 15 hours/week <b>4 year old</b> preschool in schools <sup>74</sup>	Moving to providing funding subsidies to follow the child to different settings <sup>75</sup>	54% of Northern Territory children were enrolled in preschool solely on a school site and 18% solely in long day care <sup>76</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool – less than 2 days per week based on average session length
Australian Capital Territory	Free 15 hours/week preschool in ECEC for eligible priority <b>3 year old</b> and Koori preschools <sup>77</sup>  \$2500 to providers for 1 day (7.5 hours) of ECEC for <b>3 year olds</b> <sup>78</sup>	2024-2030: Scale up of universal 3 year old preschool, commencing with 1 day ECEC in 2024	Only 5 sites for 3 year old preschool, majority delivery expected in long day care	No exemption from Activity Test
	Free 15 hours/week preschool in public schools for <b>4 year olds</b> <sup>79</sup>		38% of Australian Capital Territory children were enrolled in preschool solely through long day care and 35% through preschool <sup>80</sup>	Activity test exemption provides 36 hours/fortnight subsidy for preschool – less than 2 days per week based on average session length

74. <https://nt.gov.au/learning/early-childhood/age-your-child-goes-to-child-care-and-preschool>75. <https://federalfinancialrelations.gov.au/sites/federalfinancialrelations.gov.au/files/2022-03/2022%20Northern%20Territory%20Implementation%20Plan.pdf>76. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>77. <https://www.education.act.gov.au/early-childhood/set-up-for-success-an-early-childhood-strategy-for-the-act/quality-early-childhood-education-for-three-year-olds>78. <https://www.education.act.gov.au/early-childhood/coming-soon-free-three-year-old-preschool>79. <https://www.education.act.gov.au/early-childhood/preschool-reform-agreement>80. <https://www.abs.gov.au/statistics/people/education/preschool-education/latest-release>



# APPENDIX 2

## MODELLING METHODOLOGY

### Number of children missing out on early childhood education and care

- Using HILDA Wave 21, identify households with children aged 3 or 4.
- Estimate total number of children aged 3 and 4 using household weights from HILDA.
- Estimate total number of children who use any formal child care for work or non-work-related reasons.
  - Formal child care: Family day care, long day care centre at workplace, private or community long day care centre and/or kindergarten/pre-school.
- Estimate total hours of formal child care used (household level)
  - Because we do not observe the individual hours of child care that each child attends, to estimate the weekly hours of childcare use for each of the children within the household we used the rates of children who attend child care by age from the Department of Education (2022) and distributed the total hours of childcare used in the household to each child based on their age.
- Estimate the total number of children who are age 3 and use 30 hours or more and 4-year-olds who use 15 hours or more of child care a week.
- For these groups, we estimated the total children who pass (do not pass) the Activity Test.
  - Pass Activity Test means mom and dad work at least 8 hours a week each for couple families, and mom works at least 8 hours a week for single mother households.
    - For those parents who we know are employed but the number of hours they work is missing, we impute with the mean hours that a parent of a 3-year-old or 4-year-old work, respectively.
- We estimate the total number of children missing out on the benefits of child care as those who use less than the recommended hours of childcare a week (30 hours for 3-year-olds and 15 hours for 4-year-olds, respectively).

### Benefits from school completion (Lamb and Huo, 2017)

- With the total number of children who miss out on the recommended hours of child care we estimate the number of children who will become early lifetime leavers and the lifetime costs associated with them.
- Mogstad et al., (2015) find that children who attend child care have decreased probability of dropping out of high-school. Following ACARA 2022, we estimate a new Year 12 Retention Rate for Australia adjusted for the

effect of attending child care.

- We estimate the decrease in the total number of children who will not finish Year 12.
- We use the fiscal and social cost of an individual early leaver by Lamb and Huo (2017) to estimate the total fiscal and social costs associated to the change in number of early leavers.
- We adjust to current prices (\$2,022) using CPI for All groups, Australia.

### Benefits from education attainment (Leigh and Ryan, 2008)

- Leigh and Ryan (2008) estimate a 10% return on income per additional year of education.
- Using Deloitte (2023) we estimate the educational gains from two years of pre-school, as four months on average.
- Following ABS 2022 data on weekly income distribution for different age groups, we estimate an average weekly income and for the following groups: 15-19, 20-24, 25-34, 35-44, 45-54, 55-64. We assume that individuals who do not attend child-care are in the lower part of the earnings distribution so we use the lower bound of each income bracket per age group.
- We estimate the total yearly income (52 weeks) for the following age bands: 25-34, 35-44, 45-

64 for a total of 40 years of working life.

- We estimate the average lifetime income (25-64) using a discount rate of 4%, a wage increase of 3.5% and inflation rate of 3.5%.
- We estimate the loss in lifetime income per person by decreasing the average lifetime income in 10% as a result of the year of education they miss out on.
- With the total number of children who miss out on the recommended hours of child care we estimate the total loss in lifetime income from a year less of education.

### Total benefits

- The children that benefit through school completion are removed from the estimate of additional educational attainment.
- Our calculations are based on these benefits being realised with attendance of between 15 and 30 hours per week in both years prior to starting school.

### Application to Victoria and New South Wales

- Numbers impacted that meet Activity Test threshold are adjusted to account for long day care centre attendance using Productivity Commission (2023), ROGS Early Childhood Education Attendance Data.

**IMPACT**  
**ECONOMICS**  
**AND POLICY**