Roundtable on Economics and Child Care Background Paper

Child Care: Background and Context

Providers: Data from the 2019 National Survey of Early Care and Education (NSECE)[1] indicates that there are approximately 1.26 million child care providers in the formal, paid child care system in the United States, 121,000 child care centers and about 1.14 million paid home-based providers. About 91,000 paid home-based providers are listed on an official registry and another 1.1 million are paid but not listed on any registry.

Table 1. Child care providers, by type

Center	121,000
Home-based, paid, listed	91,200
Home-based, paid, unlisted	1,050,000
TOTAL, formal child care system	**1,262,200**

Source: National Survey of Early Care and Education, 2019

Type of Business and Auspices: About half of child care centers (47%) are non-profits, about one-third (34.5%) are for-profits (30.4% independent and 4.1% franchises or chains), and 15% are government-run.[2] About 6% (7,550) of centers, serving 432,000 children, are sponsored by a church or religious private school.[3] Regarding center size, about one-third (34%) have more than 75 children, 19% have 50-75 children, 27% have 25-50 children, and 8% have fewer than 25 children.[4]

Government Funding: About three-fourths (76%) of centers report receiving government funding (federal, state, and /or local).[5] Among home-based providers, 62% of listed, paid providers receive government funding, as do 18% of unlisted, paid providers.[6]

Children Served: Child care centers serve 7.15 million children ages birth to 5.[7] Paid home-based providers care for 2.6 million children ages birth to 5.[8] In total about 9.8 million children ages birth to 5 are in formal child care settings.

Table 2. Children served, by child care setting and age

Child Care Setting	Age <3	Age 3-5	Total
Center	2,158,000	4,990,000	7,148,000
Home-based, paid, listed	291,000	303,000	594,000
Home-based, paid, unlisted	1,080,000	944,000	2,024,000
TOTAL, formal child care system	**3,529,000**	**6,237,000**	**9,766,000**

Source: National Survey of Early Care and Education, 2019

Child Care Workforce: According to the NSECE, in 2019, child care centers employed 1.82 million staff, with 1.4 million serving children under age 5.[9] Bureau of Labor Statistics data, however, cited a workforce of approximately 1 million child care staff in 2019, across child age and provider setting.[10] This discrepancy in basic data concerning the size of the child care workforce is problematic.

Child Care Supply and Demand

Supply: At the program level, Child Care Aware® of America's recent report[11] found that while the number of center-based programs rebounded to pre-pandemic levels in 2022, they did not grow additionally in 2023. Meanwhile, the number of family child care homes (FCC) continues to decline, though at a slower rate than in previous years. FCC homes have declined approximately 12% since 2019. Moreover, this downward trend predates the pandemic, with FCC homes decreasing at least since 2005.[12]

Examining supply at the level of child care slots or spaces is more complicated. While many assessments of child care supply focus on licensed capacity, it is likely that this overestimates the true supply. In fact, some preliminary research from Virginia indicates that this is the case.[13] Smith and colleagues differentiated licensed capacity, desired capacity (number of children programs want to enroll, given staffing and other considerations), and actual enrollment.[14] They suggested that states should do point-in-time counts to understand how licensed capacity relates to enrollment. Desired capacity could be examined through provider surveys; this might prove to be the most realistic measure of actual supply.

Potential Need vs. Demand and the Child Care Gap

Studies of child care supply gaps typically focus on potential child care need, rather than actual demand, because there is little available data on actual demand.

- Potential Child Care Need: All children under 6 with all available parents in the labor force
- Child Care Demand: Rate at which parents and families actually utilize or look for formal child care

The child care gap is then defined as the difference between potential child care need and child care supply.

Source: Smith, L. K., Bagley, A., & Wolters, B. (2021). Child care in 35 states: What we know and don't know.

Demand: The field has struggled with quantifying actual child care demand. Families' demand can be driven by many factors including need, preferences, access, affordability, available provider quality, etc..[15] A typical approach has been to examine potential child care need, using census data on the number of children below school age who have all available parents in the workforce. However, a survey by the Bipartisan Policy Center (BPC) shows that more than half of families who use informal child care would continue to do so even if formal child care was free and convenient.[16] Other research shows that more than one quarter of parents cite primary reasons other than parental employment for placing their children in child care (i.e., enrichment, to provide parents relief from caretaking)[17] and it's likely that most, if not all, families need some child care support.[18] More work is needed to develop accurate estimates of child care demand.

Gaps: Despite difficulties in quantifying both supply and demand, it is clear that child care supply is inadequate. Many parents report that they struggle to find child care, particularly care they can afford.[19] Availability is especially limited for families who have infants and toddlers, have low incomes, work nontraditional hours, or live in rural areas. A BPC study of 49 states and Washington, DC found a child care supply gap of 30.3%.[20] The gap in rural areas (33.4%) was larger than that in urban areas (29.2%).

Eliminating Gaps—Demand-Side Strategies: Efforts to reduce gaps between supply and demand have focused largely on the demand side, primarily child care subsidies (through the federal Child Care Development Block Grant [CCDBG] and state subsidy programs) that increase low-income parents' ability to pay for care. Under federal rules, to be eligible for subsidies, family income must be less than 85% of the state median income. However, due to underfunding, only 18% of families eligible under federal rules receive CCDBG subsidies.[21] Further, for families to be able to afford child care, eligibility rules would need to be far more generous.

Parental tax credits, such as the Child and Dependent Care Tax Credit (CDCTC) and similar state tax credits, also represent demand-side strategies. However, the impact of the CDCTC is limited,[22] given that the amount of expenses that can be claimed is small compared to the cost of child care. Further, the credit is not refundable, so low-income families without federal tax liability are not eligible. Similarly, the Dependent Care Assistance Plan (DCAP) allows parents to set aside just $5000 per year in pre-tax dollars for child care, an amount less than half the average cost, and fewer than half of employees work at a company that offers a DCAP.[23]

Some states, starting with Michigan, have experimented with a model in which the state, parents, and the parents' employer split child care costs.[24] This "Tri-Share" model has yielded some preliminary positive results, increasing the number of families with access to financial assistance for child care and reducing their child care costs. However, it also raises concerns, including low uptake from businesses, tying child care affordability to staying in a particular job, equity issues around which employers provide this benefit, failing to address child care quality or the child care workforce, and still falling

short of reaching all families who need assistance with paying for child care.

Paid family leave (PFL) might also serve as a demand-side strategy, by reducing parents' need for child care very early in their children's lives. Census data show that 40% of mothers who worked during pregnancy return to work less than three months post-childbirth.[25] At the same time, infant care is the most scarce[26] and most expensive[27] type of child care.[28] The federal Family and Medical Leave Act (FMLA) of 1993 provides eligible workers with unpaid leave for specified family medical and caregiving needs, including the arrival of a child (newborn, adopted, fostered).[29] In addition, several states and DC have PFL laws, with 13 states (CA, CO, CT, DE, ME, MD, MA, MN, NJ, NY, OR, RI, WA) and DC having mandatory PFL and nine states having voluntary PFL (AL, AR, FL, KY, NH, TN, TX, VT, VA).[30] Some private employers also offer PFL and are eligible for the federal Employer Credit for Paid Family and Medical Leave.

However, access to paid leave is lacking across the nation. Only 27% of civilian workers have access to PFL.[31] Moreover, access to employer-provided PFL is not equitably distributed, with the younger, lower-wage employees and those employed by small companies being less likely to have access. Lower-wage workers are also less likely to be able to afford taking unpaid leave under the FMLA.[32]

Eliminating Gaps—Supply-Side Strategies: Recent research has begun to examine supply-side impacts of child care subsidies. The Urban Institute argued that while subsidies have the potential to increase supply, their ability to do so is limited by the fact that subsidies are only a small part of the child care market.[33] Further, raising subsidies alone will not increase supply, because providers face other financial and nonfinancial constraints. However, a recent modeling study in Minnesota found that increasing subsidies produced relatively large increases in child care supply, while having minimal impact on price. Specifically, investing an additional $100 per young child in the population increased the capacity of licensed private providers by 4%, while increasing price by only 0.3%. Note that this model required additional investments per child in the population, whereas existing subsidies through CCDBG serve only a small portion of eligible children,[34] falling far short of an investment in all children. Another model examining the impacts of expanding subsidies to families up to 250% of the national median income, and capping parent payments at 7% of income, predicted that the resulting increased demand for child care would increase both supply and provider wages. In addition, maternal employment would increase.[35]

Preliminary data from new legislation in Vermont that increased subsidy eligibility from 350% to 575% of the federal poverty level found an impact on supply, with 1,000 new slots opening, and more centers and family child care homes opening than closing for the first time since the state started collecting this data.[36]

Other supply-side strategies have been suggested and implemented, including efforts directly targeted to providers: supplementing provider compensation; start-up, operational, and expansion grants;

training in business practices; licensing support; and staffed family child care networks.[37] During the pandemic, in the face of a severe drop in demand, the federal government invested heavily in child care through the American Rescue Plan Act (ARPA). Many states used this funding to launch supply-side interventions that prevented the collapse of the child care system.[38] Research from the Center for the Study of Child Care Employment demonstrated that over the period of ARPA funding, the child care workforce nationwide grew 20%, gradually returning to pre-pandemic levels. Growth since ARPA ended is about 1%.[39]

Lastly, the Employer-Provided Child Tax Credit (45F) (and similar state tax credits, which exist in an increasing number of states[40]) has the potential to sustain or increase child care supply.[41] Employers can receive a nonrefundable tax credit for building or operating on-site child care for employees, contracting with a community child care provider for slots for employees' children, or providing child care resource and referral services. However, the Government Accountability Office (GAO) has identified several problems with the 45F credit, including low awareness among employers and insufficient size to incentivize employer behavior.[42] Perhaps most challenging, the vast majority of businesses in the U. S. are small, with 90% employing fewer than 20 people.[43] Small businesses face challenges in accessing the 45F credit and helping their employees with child care costs. Non profits, who do not have tax liability, are not eligible for the credit. As a result of these challenges, take-up of the 45F credit is extremely low, with less than 1% of businesses claiming it.[44]

The GAO[45] made several recommendations to increase the usefulness of the 45F credit, including: the IRS, child care resource and referral organizations, business associations, and chambers of commerce could all share information on the credit with employers and other constituents; the portion of an employer's child care expenses that can be offset by the tax credit and the maximum allowable credit could be increased; eligibility for the credit could be extended to home-based child care and to employers who do not have federal tax liability; the rules could be changed to allow multiple employers to band together to provide child care services and claim the credit.

It is likely that effective strategies to increase child care supply will need to include both supply- and demand-side policies.[46] Simply increasing the supply of child care will not be adequate; family needs and parental choice must be considered. As mentioned above, BPC's survey data shows that not all parents would use formal care even if it were available to them. These surveys indicate that most parents using informal care are satisfied, and more than half of those would continue to use informal care even if formal care were free and convenient.[47]

Factors Driving Child Care Cost and Quality

Cost: Various models have been developed to estimate the true cost of child care. A recent effort by Prenatal to Five Fiscal Strategies, for example, posits the following as drivers of cost: setting (center vs. FCC home), ratio and group size, number of classrooms, age of children served, staff salaries and benefits, practices that allow family engagement (i.e. teacher conferences), non-personnel expenses (e.g., occupancy) and maintaining an operating reserve.[48] Other models include similar inputs as potential cost drivers.[49] The relationship between some of these factors and cost seems clear (e.g., increasing staff compensation will increase cost, as the BPC determined that staff costs comprise 70-80% of child care program operating budgets).[50] However, the impact of other factors, such as regulations around group size and ratios, is less clear (see below).

Quality: The floor for child care quality is outlined in state regulations and licensing standards, which aim to keep children safe and healthy. These typically focus on structural components of quality, including health practices, physical environment, staff-child ratios, group size, teacher education and training, etc.

As of 2023, 42 states and DC also have a Quality Rating and Improvement System (QRIS) that rates child care providers, in order to inform parents and incentivize quality improvements (often through financial incentives).[51] QRIS ratings go beyond baseline regulations and licensing standards; however, in many states, participation is voluntary and therefore low. Further, Child Trends notes that while QRIS ratings are associated with small differences in quality, the research linking ratings and child outcomes is mixed.[52] Critics have questioned the value of QRIS, arguing that ratings often fail to assess the key aspects of child care quality, particularly the teacher-child interaction, and are overly prescriptive in defining quality.[53] It is likely that process components of quality, focusing on staff-child interactions and the nature of the child's experience in the child care setting (language environment, developmentally-appropriate curriculum and instruction, social relationships, parent engagement, etc.), are most important in contributing to child outcomes.

Role of Regulations in Driving Cost and Quality: A comprehensive review of the impact of regulations on child care found mixed results.[54] Research shows that most providers (70%-80%) voluntarily exceed the minimum standards set in regulations. However, studies also reveal that a substantial number of providers do not comply with regulations. Overall, this research calls into question the impact of regulations.

On the other hand, the same review found that econometric studies have demonstrated impacts of child care regulations. On the negative side, stricter regulations reduce the demand for child care labor and reduce supply, particularly in low-income communities. "Input substitution" also occurs with stricter regulations, whereby providers reduce investments in other factors to comply with the stricter regulations (e.g., hiring more, but less skilled, workers to meet regulations on staff-to-child ratios). On the positive side, stricter regulations have the intended consequences (e.g., higher staff-to-child ratios)

and reduce racial and ethnic gaps in providers' hiring processes. Due to input substitution, stricter regulations do not tend to increase price. The review notes that there are very few studies of the effects of child care regulations on quality and findings are mixed.

Affordability of Child Care

What Can Parents Afford to Pay for Child Care? Many sources cite 7% of family income as an index of affordability, based on the US Department of Health and Human Services' (HHS) benchmark.[55] However, experts have argued that 7% of income could be a large burden for some families, particularly those with low-incomes.[56] In fact, analyses show that families with low incomes pay a substantially higher percentage of their income for child care than do families with higher incomes: those below the poverty line pay an average of 27% of family income, compared to 17% for families at 100-199% of poverty, 12% for families at 200-299% of poverty, and 7% for families with incomes at 300% or more of the poverty line.[57] Further, recent data from Child Care Aware® of America shows that the cost of child care exceeds 7% of median family income in more than 70% of the states and DC.[58] The BPC noted that this 7% benchmark was designed as a recommendation for how much a family receiving child care subsidies should pay as a co-payment, not as an affordability metric for all families.[59]

Parents' Assessments of Affordability: A 2021 BPC poll asked parents to identify the maximum amount they can afford for child care.[60] Two-thirds of respondents reported that the maximum they could afford is about $10,400 annually per child. While this amount is close to the national average cost of care in 2023, the cost of quality care in many states exceeds this amount.[61]

Determining Child Care Affordability: Experts at the BPC have argued that affordability metrics should take factors such as income, household size, regional cost of living, etc., into account. They cite the Economic Policy Institute's family budget calculator[62] as one model for assessing affordability of child care, as it determines the minimum household income needed to afford child care and other expenses. Some have suggested that metrics from other fields, such as housing, could inform the child care affordability debate. However, the 30% rent or mortgage affordability "rule" has a history similar to the HHS 7% benchmark in that it was developed as an index of how much of a public housing tenant's income should be spent on rent.[63] The 30% index was not intended to be a general rule of thumb, yet it was widely adopted by financial advisors and lenders as such. More work is needed to determine a reasonable benchmark for child care affordability.

Impacts of Child Care on Labor Market and Economy

Mothers of Young Children in the Workforce: Although women with children under age 6 represent just 10% of the total workforce,[64] two-thirds of women with children this age are in the workforce.[65] The percentage of working women with children under age 3 is similar (64%).[66] Looking at all working mothers (with children under age 18), the most common occupations are education, health care, and social assistance with 40% of all mothers working in these groups.[67] Child care educators are nearly all

female (97%)[68] and it's likely many are mothers of young children. These professionals earn an average of $30,360 per year and it would take 59% to over 100% of this average annual wage to afford center-based child care for two children.[69]

Supply: Economic research[70] from the US[71] and other countries supports a link between child care availability and maternal employment.[72] Looking across 19 states, the Center for American Progress found a significant positive relationship between licensed child care supply and maternal labor force participation.[73] A recent study by the Council of Economic Advisors found that ARPA funds increased child care provider employment, a proxy for child care supply.[74] Subsequently, labor force participation among mothers of young children increased more than five percentage points (compared to less than three percentage points for mothers of older children and less than one percentage point for women without children). Looking at a change in supply, a study of the expansion of DC's universal preschool program found that it was associated with a 10 percent increase in maternal employment.[75]

Price: Similarly, studies show that the price of child care impacts maternal labor force participation, including both whether to work and the number of hours worked.[76] Some mothers are able to compare the cost of child care with the income they would make outside of the home and actively opt out of the workforce. Other families, such as single parents or those with low incomes, do not have this option. These families often rely on lower- or no-cost child care from family or friends, rather than participate in the formal child care system. A study by the Department of Labor found that a 10% increase in child care prices was associated with a 1 percentage point lower rate of maternal employment.[77] A literature review found that impacts of early education costs on maternal employment vary widely from study to study, but most estimates imply that a 10% price reduction would increase maternal employment by 0.5-2.5%.[78]

Conversely, research on child care subsidies, which make care more affordable, show positive impacts on mothers' labor market participation.[79] Herbst's review of the literature concludes that while studies differ in many respects, their findings are "remarkably consistent" in demonstrating that receipt of child care subsidies increases maternal employment rates.[80] A model examining potential impacts of narrow (up to 85% of national median income) and broad (up to 250% of national median income) expansions of current CCDBG subsidies predicts large increases in maternal employment.[81] The narrow expansion would increase maternal employment overall by two percentage points and full-time employment by almost five percentage points; broad expansion would double these impacts. A study predicting the impacts of expanding child care subsidies to all families in DC found that this would lead to $1.4 billion in economic growth in the first year of the program.[82]

With regard to both supply and price, studies have shown that parents' inability to find affordable child care has significant impacts on both businesses and national and state economies.[83] Parents report negative impacts on their work lives (missing work, leaving the labor force, etc.), resulting in costs to employers and decreased tax revenue.

Summary

This brief background paper demonstrates that considerable research has been done examining the economics of child care. However, it is clear that there is still a lot to learn. The roundtable will explore what we know and don't know about the questions raised here and related issues. Our goal is to provide federal and state policy recommendations that include both near- and long-term solutions to the current child care crises facing the nation.

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