

**Submission to Productivity Commission public inquiry into future options for  
childcare and early childhood learning**

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Dr Wendy Craik AM  
Presiding Commissioner  
Child care and Early Childhood Learning Inquiry  
Productivity Commission  
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(via email: [childcare@pc.gov.au](mailto:childcare@pc.gov.au))

Dear Dr Craik

*Re: Productivity Commission public inquiry into future options for childcare and early childhood learning*

## Introduction

**Chapter 6 of the “*Childcare and Early Childhood Learning - Productivity Commission Issues Paper*”** calls for submissions to express opinions as to which “*aspects of the ECEC are working well and what aspects are problematic*”.

In order to address this question in the submission we have set out in the introduction a summary of the personal experience of the authors of the submission. The submission then addresses in detail the various matters that we believe the Government needs to review to ensure that more equitable childcare arrangements are available for working parents with children.

Affordable flexible childcare is not a female issue; it is an issue that affects both parents and the society at large. Unless it is addressed, it will have a significant long-term impact on Australia’s Gross Domestic Product.

The focus of this submission is income tax reform and the recognition of in home private care as legitimate employment. Our recommendations emphasise facilitating employment and not further welfare payments.

If the Government is serious about getting women to remain in the workforce, and advance into senior management roles, then the Government must face the fact that the cost of childcare for working parents is a legitimate expense inextricably linked with earning assessable income and it needs to make that expense tax deductible.

Further, working parents should have a choice about the provision of childcare; the debate about tax deductibility should not be confined to childcare provided by institutions.

**Louise McBride - Barrister**

I have been an active participant in the childcare debate since 1987. My interest in the subject centred on the retention of women, particularly tertiary educated and skilled women, in the workforce after childbirth.

I am a mother of two children and I have practiced all my working life as a solicitor, attaining partnership in a major law firm while I was pregnant with my second child. I have remained an active participant in the workforce having been the sixth female partner in the firm and the first female partner in the commercial section of that law firm. I was later head hunted to become a partner in an international accounting firm. The accounting firm was to employ me because they had no female tax partners at that time.

In my role as a partner in both organisations, one of my responsibilities was the recruitment and the retention of women.

As a career woman with children and as an employer and mentor of women in the law industry, I experienced and witnessed the struggle young career women have trying to juggle the demands of working and maintaining a career.

I was fortunate enough to have married someone who was already successful in his career so “*he was able to subsidise my work experience*”. A true but pejorative comment made mostly when the strain of having two career people in a marriage became too much. The reality of our life was that until I became a partner the nanny earned more than my entire after tax income. This experience was not unique to me, however I had more resolve to remain in the workforce than most women in similar circumstances because of my mother’s encouragement.

My mother was by all accounts a brilliant medical student, she was training as a pathologist when she became pregnant with me. As was the norm in the 1950s, my mother left medicine, after her contract with the hospital had expired, to bring up her four children. Although she wrote a very successful medical book and worked as a secondary professional to my father (also a doctor) she never completed her specialisation, and in her words she “became out of date”. Just when I was contemplating giving up my career because it was becoming too difficult to juggle both the demands of work and the demands of family and I was out of pocket for all the trouble I was going to, my mother at 56 had to return to practice medicine – not an experience she initially relished.

My mother was fortunate to be able to retrain as a GP and practiced medicine from the age of 56 to 82, when she retired. Her strongly expressed advice to me was to never give up my career, that women needed to have enough experience in their chosen field of expertise before leaving the workforce because if they had to return to it – it was easier to re-enter with experience. My mother was correct - getting back into the workforce is no easy task for a middle-aged and deskilled professional woman. Throughout my career, I have imparted the same advice to the women whom I have mentored or who worked for me.

In my experience the greatest barrier to retaining skilled women in the corporate workplace is access to affordable childcare.

The second hurdle is that government assistance of subsidies and rebates is mostly available when childcare is provided in a childcare centre. Even if a place is available in a childcare centre, getting young children to day care before work can be a

logistical nightmare and another hurdle in an already challenging task of staying in the workforce.

Again, in my experience having sat on both the remuneration and promotion committees of both a top tier accounting firm and top tier law firm, it is a long way to partnership or the top of the corporate ladder for those women who leave work early to collect children from day care centres. These women are seen as less committed to their career than their male colleagues, even if they do work at home later in the evening completing their work. I have had first hand experience of women with children in childcare being overlooked when it came to promotion to partnership and salary increases. In this regard, I have found that 7am - 6pm day care offering of long day care centres is not flexible enough for women trying to climb the corporate ladder; in my experience, it is less stressful for the women to opt out.

In my experience of trying to juggle both family and career, it was easier for me having a nanny who turned up at my house every day than for my colleagues with children in childcare, as they had the added stress at the beginning and end of each day of delivering and collecting children from the childcare centre. Furthermore the nanny was cheaper for me because the hours I worked would have required me to employ additional help after the closure of a childcare centre where my children attended during the day. Finally, in my experience, nannies are not unskilled domestics – the nannies I employed were always highly trained and could command a large salary because of their experience.

In my experience, career women struggle and sacrifice to stay in the workforce when they have young children. They are not heiresses or ladies who lunch. One of my colleagues has drawn down every year against the mortgage on the family home in order to pay for her childcare needs. This situation begs a number of questions. Why should my colleague be disadvantaged when women who don't work who have children get subsidised childcare and financial assistance? We have a system that requires work for the dole but the government is yet to adopt the same approach to childcare? What is equitable about the status quo that provides assistance to women on low incomes and women who don't work, while women who are successful and contribute significantly to Australia's tax revenue are left to provide for themselves?

As I see it, the current policy contributes to highly skilled and highly educated women leaving the workforce. These are exactly the women the Government needs to retain if it really wants to see more women CEOs and Board Members.

### **Sophie Gerber - Director**

Sophie Gerber is the director and owner of Sophie Grace Pty Ltd and Sophie Grace Legal Pty Ltd (together "Sophie Grace"), operating an Australian compliance and legal consultancy. Sophie and her team, including Quynh Truong, Alicia Pevely and Vladimir Kravchenko (who all contributed to this submission) specialise in assisting firms establish and maintain a financial services business in Australia.

Sophie Grace employs young lawyers full-time, with all lawyers being under the age of 35. The majority of lawyers are female with no children at present. Sophie also employs part-time administrative staff. All staff, including Sophie, most likely will one day face the challenges of working with children alongside maintaining a career that took 5 years of study to enter. After spending many years developing and investing in the careers of young lawyers, the prospect of losing talented staff for a potentially extended or indefinite amount of time is very disappointing. Businesses such as Sophie Grace contribute positively to the economy through being Australian owned,



entrepreneurial, honest tax-payers. Having the government tacitly undermining the investment made by such firms is a disappointing result.

The costs of engaging recruitment firms and maternity leave contractors (who require high levels of initial supervision and training) to fill a key role in a small firm are more than a business such as Sophie Grace is able to comfortably absorb. Similarly, the provision of work from home arrangements within small firms become difficult and too expensive when balanced with other legislative requirements such as provision of a safe working environment within the home, technological requirements (e.g. phone and file access). From a practical standpoint, working from home for young mothers effectively means being at home to mind the children and squeezing in some work where possible, a cost which cannot be absorbed easily by small businesses. It similarly can create a bad impression when phone calls are being conducted with clients and other colleagues to the tune of unattended children in the background.

Unlike large organisations which can make the working life easier for staff through the provision of childcare centres which fall within the Fringe Benefits Tax exemptions, Sophie Grace cannot make this provision for staff. Companies like Sophie Grace find it difficult, if not impossible to compete with the offerings of large firms on a purely practical and financial basis, to recruit and retain the best staff.

I also have a young sister of 6 years old who attends after school care. My experience, and that of many people, is that the stress of getting to collect her on time (so as to avoid usurious late fees, sometimes up to \$30) places significant pressure on her collection. Where a parent is not able to make it on time, it additionally places stresses on friends and family who may be called upon.

## Submission summary

We believe the provision of tax deductions for in-home childcare is essential for the Australian community to meet the objectives of the Productivity Commission Inquiry (“**Inquiry**”). Such tax deductions should not be seen as a mutually exclusive substitute to the existing childcare support system but rather as a choice given to parents for whom the current childcare support system is not viable. Also, tax deductions are not welfare payments, they are a deduction for legitimate expenses to facilitate employment. The absence of the measures we propose in this submission creates a major fiscal loss and brain drain in the Australian economy.

Our proposal is outlined below in detail. It follows the structure of the objectives put forward by the Prime Minister in his office’s announcement of 17 November 2013<sup>4</sup>. The four stated objectives of the current Inquiry are “to examine and identify future options for a child care and early childhood learning system that:

1. supports workforce participation, particularly for women;
2. is more flexible to suit the needs of families, including families with non-standard work hours, disadvantaged children, and regional families;

<sup>4</sup> Prime Minister of Australia, the Hon Tony Abbot MP, *Government announces productivity commission inquiry to focus on more flexible, affordable and accessible child care* (2013), <<http://www.pm.gov.au/media/2013-11-17/government-announces-productivity-commission-inquiry-focus-more-flexible-affordable>>.

3. is based on appropriate and fiscally sustainable funding arrangements that better support flexible, affordable and accessible quality child care and early childhood learning; and
4. addresses children's learning and development needs, including the transition to schooling."<sup>6</sup>

## 1. Workforce participation, particularly for women

The present childcare system in Australia is inconsistent with the government objective of increasing workforce participation and the increasing the presence of women in senior roles. It does not provide an incentive or a viable context for most professional women to continue participating in the workforce after childbirth. The only way to alter the present situation is to afford childcare costs the same status as any other work related expenses by making childcare expenses, including those expenses related to in-home care, tax-deductible.

The situation of workforce participation is particularly telling in the case of female workers as women still perform 2.7 times as much childcare tasks and 1.8 times as much household work as men<sup>7</sup>. This imbalance undoubtedly contributes to the lower participation of women in the workforce relative to that of men. In 2011 the male rate of workforce participation was 72% compared to only 59% of that of females and a mere 54% of females with children aged between 0-4 years<sup>8</sup>. In the same year, 88% of the 34% of women with children who did not return to the workforce after giving birth reported that they did not return to work in order to care for their child<sup>9</sup>.

### Problems with the current system of government benefits

It is a stated commitment of the government to increase the number of women in senior roles in the spheres of public and private employment<sup>10</sup>. The way in which the government currently supports working parents - in the form of the Child Care Benefit and Child Care Rebate – is not a sufficient incentive financial for most professional women to remain in the workforce.

The Child Care Benefit is means tested and depends on the yearly family income. The current maximum approved care rate for a non school-aged child in up to 50 hours of care per week is \$3.99 per hour, or \$199.50 per week or \$10,374 a year. The maximum amount is payable when actual family income is under \$41,026 or where the family is on income support. If a family's combined income is more than \$145,642, then the benefit cannot be claimed. With the average national income

<sup>6</sup> Ibid, paragraph 17

<sup>7</sup> Australian Bureau of Statistics, *Trends in Household Work* (2009), <<http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Main+Features40March%202009.>>

<sup>8</sup> Australian Bureau of Statistics, *Australian Social Trends, Data Cube – Work* (2013), <[http://www.abs.gov.au/ausstats/subscriber.nsf/LookupAttach/4102.0Data+Cubes-27.02.135/\\$File/41020\\_work\\_indicators\\_2012.xls.>](http://www.abs.gov.au/ausstats/subscriber.nsf/LookupAttach/4102.0Data+Cubes-27.02.135/$File/41020_work_indicators_2012.xls.>)

<sup>9</sup> Australian Bureau of Statistics, *Australian Social Trends Nov 2013 - Pregnancy and Work Transitions* (2013) <<http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4102.0Main+Features10Nov+2013#p7>>

<sup>10</sup> For example, Department of the Prime Minister and Cabinet <[http://www.dpmc.gov.au/women/priorities/womens\\_leadership/increasing-leadership.cfm>](http://www.dpmc.gov.au/women/priorities/womens_leadership/increasing-leadership.cfm>)

being \$74,724 per year<sup>11</sup>, this means that families where each partner earns slightly more than the average national income are not entitled to the benefit at all<sup>12</sup> and the vast majority of families are not entitled to receive the full benefit. Clearly, most professional women would not be able to access this Child Care Benefit. Assuming that both parents in a family are earning the same amounts, if their salaries are \$73,821 a year or above then they are no longer eligible for the benefit as their combined income would be that of \$145,642 or above. This means that if the yearly salary of both of these parents is just \$1,903 above \$73,821 then such families are not eligible for the benefit.

Annexure A to this report is a table with childcare centres and their costs for the suburbs from six of the greater Sydney areas: Baulkham Hills, Ashfield, Parramatta, Hurstville, Bondi Junction and Mosman. We compiled this table using the information provided on <http://www.mychild.gov.au/> about the available childcare centres in those suburbs. The average daily cost of day care for the six suburbs is \$99.65 and the highest daily fee is \$154. When you compare these costs and the average cost of a nanny for a regular 9 hour working of \$160 dollars a day, it becomes clear that the Child Care Benefit is of little support to anyone who is employed full time.

The situation is even worse for the large number of people whose working day is longer than 8 hours or who work hours that fall outside of the 9am to 5pm paradigm.

The Child Care Benefit is also available to registered childcare providers. Registered childcare is care provided by grandparents or other relatives, friends or nannies who are registered as carers with the Department of Human Services. The maximum amount payable per week is \$33.30 (\$0.666 per hour). This would cover about one hour of care per week, the expenses of a trip to the movies or a frugal day out! At this rate, it is almost offensive for parents of young children to claim this to provide it to their aged parents to look after their children.

The Child Care Rebate covers 50 per cent of the out-of-pocket expenses and is capped at \$7,500 a year. These expenses constitute the total childcare fees paid, minus the amount of any Child Care Benefit. However, the Child Care Rebate is available for 'eligible' parents rather than restricted to tax-paying employers and only applies to 'approved' childcare.

The requirement of being an 'eligible' parent means that the Child Care Rebate is not easy to get. Anecdotally, the time spent liaising with the childcare centre and the authorities in order to become registered and eligible is time-consuming and difficult. To become eligible, a parent needs to prove they work excessively long and irregular hours have multiple of children or a child with special needs. Further, they must be prepared to subject themselves two times a year to an audit by an agency just to make sure that the above conditions have not changed.

Likewise, fact that the Child Care Rebate can only be claimed via 'approved' childcare has highly limiting implications for in-home care.

Firstly, there is a limited number of 'approved' in-home childcare facilities which means that only a limited number of carers are available to parents wishing to claim the Child Care Rebate for in-home care. For example, there are only 20 in-home

<sup>11</sup> Australian Bureau of Statistics, *Increasing Leadership and Representation Opportunities* (November 2013) <<http://www.abs.gov.au/ausstats/abs@.nsf/Products/6302.0~Nov+2013~Main+Features~Australia?OpenDocument>>

<sup>12</sup>

childcare facilities in the whole of NSW and some of them have no vacancies, which leaves the parents living in the areas where centres have reached capacity without the in-home option<sup>13</sup>.

Secondly as the government outsources the administration of the Child Care Rebates to registered in-home care employment agencies the maximum real amount a parent is able to receive for in-home care via the Child Care Rebate is far lower than the \$7,500 per year per child. Presently, the approved agencies charge a fee of \$5 on average for each hour a nanny registered with the agency works. This means that if a nanny is employed for 55 hours a week 52 weeks a year the fees that need to be paid to the nanny's employment agency amount to \$14,300 a year, leaving parents who are eligible for a Child Care Rebate of \$15,000 with a mere \$700 of support.

However, even if these administrative fees did not take up such a large percentage of the available Child Care Rebate, the Child Care Rebate is still a fraction of in-home childcare costs. A nanny employed by a parent on a full-time basis typically works 50-55 hours a week and earns \$65,000 to \$71,500 a year. With the 9 per cent superannuation a nanny's salary averages between \$70,850-\$77,935. A female executive has to be in the top 1.7 per cent of all female wage earners and earn \$104,000 a year, or \$77,570 after tax, just to pay for a nanny. With the high costs of childcare in metropolitan areas such as Sydney or Melbourne the rebate is not sufficient for families dependent on formal care living in those areas.

Further, the Child Care Rebate does not directly promote workforce participation, (you don't have to work to claim it) and does not recognise childcare as an essential cost of working.

The current Child Care Rebate and Child Care Benefit are obviously better suited to the circumstances of non-working women and low-income earners. There is little to no encouragement from the government given to mid to high-income earners. Effectively, government stops all aid to parents who both earn \$73,821 or above. Given the high costs of childcare, a simple economic analysis of a professional female parent's wage shows that the stress of juggling career and family life is not justified. Marginal tax rates, the lack or relative difficulty of obtaining welfare payments and the cost of childcare are always cited as the major reasons women choose to participate in the workforce on a part-time basis, or not at all, after having children.

Limiting government assistance only to those families that are perceived to need a helping hand arbitrarily encourages lower-income earners back into the workforce and higher earners to stay at home – a result definitely not desirable for the Australian community.

The *Henry Review of Tax* report noted the current system of childcare welfare justified the disproportionate amount of assistance to unemployed and unskilled female workers on the basis that it facilitated workplace participation<sup>14</sup>. Whilst we recognise that welfare should be disproportionate to assist low-income families to break out of the cycle of poverty and foster an egalitarian society, we stress that not

<sup>13</sup> [mychild.gov.au](http://mychild.gov.au) <<http://ifp.mychild.gov.au/mvc/SearchResults/ShowChildCareResults>>

<sup>14</sup> Ken Henry, Jeff Harmer, John Piggot, Heather Ridout, Greg Smith, *Australia's Future Tax System* (2009),

65<[http://taxreview.treasury.gov.au/content/downloads/final\\_report\\_part\\_1/00\\_AFTS\\_final\\_report\\_consolidated.pdf](http://taxreview.treasury.gov.au/content/downloads/final_report_part_1/00_AFTS_final_report_consolidated.pdf)>

giving adequate financial support to highly trained and skilled females will not keep those women in the workforce or change existing patterns of behaviour that discourage them from remaining in the workforce.

There is no reason why the existing benefits cannot coexist with a tax deduction for in home-care limited to employed parents.

### Consequences of non-participation of women in the workforce

The negative implications of middle-ranking women leaving the workforce to look after children at home are extremely severe for the Australian economy and society at large.

Firstly, tertiary-educated women dropping out of the workforce results in a massive brain drain for the Australian economy, especially given that 57% of university students are women<sup>15</sup>. This also leads to a major investment loss for the community, as the women who do not participate in the workforce do not repay their HECS debts. The problem is particularly telling for middle to high-income earning women because if they stay in the workforce, they are not only obliged to repay their HECS debts but have to do so at faster rates, repaying the investment made by the government and the community at large in their education. There is also a long-term cost to Australian employers from training then losing their skilled staff and executives.

Secondly, women who drop out of the workforce stop paying taxes, stop contributing to superannuation for their retirement, rapidly lose professional skills and become dependent on their husbands' salaries and government assistance in the form of the Child Care Rebate and Child Care Benefit. Similarly to HECS debt, these issues are particularly grave in the case of middle to high-ranking women. Their contribution to the revenue is significantly larger than that of other women. For example, in 2009/2010 individuals earning more than \$80,000 a year paid 57.5 per cent, or \$68 billion, of the \$120 billion in tax collected from individuals<sup>16</sup>. Not actively encouraging such women to stay in the workforce, goes against a number of government policies, including its oft stated objective to have individuals fund their retirement through increasing their superannuation balance or even against the obvious objective of increasing the budget revenue. Whilst it is highly detrimental to the Australian economy to see the women who earn above \$80,000 leave the workforce, the fact that these women receive little to no childcare assistance from government means that there is little financial incentive for them to remain in the workforce when they have children. Additionally, it is unfair to women who pay 37 per cent or more of their income above \$80,000 on tax, and receive no support from the government in return for their contribution to the economy.

Thirdly, the need to care for children directly contributes to the low numbers of women in senior management roles. Most professionals rise from middle to senior management between the ages of 30-45. This is also the age when women's

<sup>15</sup> Australian Bureau of Statistics, *Australian Social Trends, July 2013 – Hitting the Books: Characteristics of higher education students* (2013)

<<http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Main+Features20July+2013#p2>>

<sup>16</sup> Australian Government, the Treasury, *Pocket Guide to the Australian Tax System* (2013)

<<http://www.treasury.gov.au/Policy-Topics/Taxation/Pocket-Guide-to-the-Australian-Tax-System/Pocket-Guide-to-the-Australian-Tax-System/Part-2>>



participation rates in the workforce are the lowest<sup>17</sup> Considering that the median age of mothers in Australia is 30.7 years<sup>18</sup> and that the workforce participation is notably lower for women with dependant children<sup>19</sup> it is easy to understand why women are unable to progress to more senior roles. Leaving the workforce to care for children means that women are unable to gain the necessary experience, respect from their peers and seniority within their field to be selected as chief executive officers and board members. To increase the number of women in senior roles the government needs to give women in middle-ranking roles a realistic financial incentive to remain in the workforce when they have children. A childcare system that arbitrarily discriminates against high-income earners is not going to achieve this goal.

According to the Australian Bureau of Statistics, in 2012, 123,244 marriages were registered and 49,917 divorces granted in Australia<sup>20</sup>. The women, many of whom dropped out of the workforce to look after the children whilst married, find that when they return to the workforce post-divorce in order to support themselves and often the children, they are required take a position lower than they would have retained had they not taken leave. In many cases these women become reliant on government assistance as their salary is not high enough to support themselves and their children because of their lack of current skills and workplace continuity. Considering that 48.4% of all divorces involve children<sup>21</sup> and the high rate of women leaving the workforce to care for children, a very significant number of women end up in this vulnerable post-divorce situation because they have not stayed in the workforce. This creates an unnecessary and avoidable impact on the welfare system, and indirectly the education system. The only way to remedy this is to encourage women to remain in the workforce throughout their lives.

### Proposed solution

The government needs to provide women with children with a choice of either subsidised childcare or a tax deduction including for when they are employing someone privately to take care of their children.

We propose that alongside the existing government welfare, the government allows taxpayers to instead elect to making their expenditure on childcare (including in-home childcare) tax-deductible. This would not be a welfare measure but a measure to facilitate employment of both women and childcare workers. This is the only realistic way of providing an incentive for middle to high-ranking women to remain in the workforce and it has significant benefits for the Australian economy and society. As we outline below, such an approach would offer parents the required flexibility, provide a sustainable fiscal model and cater to the learning and development needs of children.

<sup>17</sup>Australian Bureau of Statistics, *Gender Indicators, Australia, Jan 2013 – Labour Force* (2013) <<http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4125.0main+features1110Jan%202013>>

<sup>18</sup>Australian Bureau of Statistics, *Births, Australia, 2012* (2012) <<http://www.abs.gov.au/ausstats/abs@.nsf/Products/3301.0~2012~Main+Features~Births?OpenDocument>>

<sup>19</sup>Australian Bureau of Statistics, *Gender Indicators, Australia, Jan 2013* (2013) <<http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4125.0main+features1110Jan%202013>>

<sup>20</sup>Australian Bureau of Statistics 'How long can we wait before tying the knot?' (Media Release, 209/2013, 27 November 2013)

<sup>21</sup>Australian Bureau of Statistics, *Marriages and Divorces, Australia, 2012 – Divorces* (2013) <<http://www.abs.gov.au/ausstats/abs@.nsf/Products/3310.0~2012~Chapter~Divorces?OpenDocument>>

This approach is also favoured by the 2006 Senate Inquiry *Balancing Work and Family* report.<sup>22</sup>

## **2. Flexibility to suit the needs of families, including families with non-standard work hours, disadvantaged children and regional families**

Childcare centres are not a viable option for many parents pursuing a professional career in Australia's 21st-century corporate environment. As outlined above, childcare centres are presently the only viable option available to the vast majority of parents. The best way to address this problem would be for the government to make in-home care a tax-deductible expense in the same way other employment-related expenses are tax deductible.

The Prime Minister's office acknowledges that "our child care system should be responsive to the needs of today's families and today's economy, not the five-day 9am-5pm working week of last century"<sup>23</sup>. Most professional people today, especially those in or aspiring to executive positions, are required to work hours outside of the 9am-5pm paradigm. This occurs, for example, when a breakfast meeting is called at work, when an out-of-town client insists on meeting outside of working hours or when the workload requires a person to stay at work late. The majority of childcare centres operate from 8am to 6pm and as a result dropping off or picking a child up at a centre becomes a practical impossibility for many professionals.

Those who do shape their work around the operating hours of childcare centres face adverse consequences at work. Professionals who leave work early to collect children or who start work later in order to drop children off at a childcare centre are perceived as less dedicated than their childless colleagues. This is even more pronounced with the extra stress of late fees for turning up more than 1 minute after the centre closes and the generally unreliable nature of public transport and traffic in major cities. For many parents who are able to structure their life around the hours when their chosen childcare centre operates, getting small children to the centre in the morning and then arriving at the office composed and tidy presents an unnecessary additional burden on top of the already arduous work life. Often the chosen childcare centre is not in close proximity to the parent's work. It is not unusual for a parent to travel an hour across metropolitan cities to collect a child from childcare.

The problem does not disappear once a child reaches school age. Instead it persists possibly to a greater extent as children attend after school care (usually provides a 7am to 6pm school day) and extra-curricular activities. Separate arrangements for school holidays, where competition is intense for vacation care places. These vacation care places usually need to be paid upfront, in advance of when a parent is able to request leave from work or determine the availability of other friends or family members to supervise their children. We discuss the particular implications for teenage children below.

The availability of 24-hour care is not a viable alternative. The realities of late and inconsistent working hours, particularly for those engaged in shift work, mean that a child left in an overnight facility would be picked up by their parent at the hour the

<sup>22</sup> Standing Committee on Family and Human Services, House of Representatives, *Balancing Work and Family* (2006) 266

<sup>23</sup> Prime Minister of Australia Honourable Tony Abbot MP 'Government announces productivity commission inquiry to focus on more flexible, affordable and accessible child care' (Media Release, 17 November 2013)



parent finishes work, which in some cases can be in the middle of the night. Research shows that for healthy development, children require regular sleeping patterns<sup>24</sup>; instead 24-hour childcare centres force children into a lifestyle of haphazardness and stress.

The problems are exacerbated when one considers that 40% of parents in Australia use public transport to get to and from work<sup>25</sup>. The overcrowded public transport in metropolitan areas, on busy commutes before and after work is certainly not a healthy environment for pre-school children to be in.

Another impracticality of childcare centres is that the waiting lists in some areas are up to 24 months. As a result of this, parents are required to choose a particular centre well in advance and for the long term. It becomes very difficult to change a childcare centre once a child has been successfully enrolled into one or to sacrifice a good wait-list position. These limitations are extremely impractical given that the modern professional's working conditions often change. For example, a move to a different employer or into a different role may render new working conditions inconsistent with the services provided by the chosen childcare centre.

#### Deductibility of in-home care

The only feasible way to solve these impracticalities and increase the participation of women in the workforce – a move that would bring major benefits to the economy as outlined above – is to make childcare, including in-home childcare tax deductible.

As outlined above, for many parents, remaining in the workforce is not achievable by placing their child in a childcare centre. What they require instead is to have someone they can rely on take care of their children, in the hours that reflect their working commitments. The argument that hiring a nanny is a luxury does not hold basis in fact as for many people it is the only viable way to remain in the workforce. In-home care allows parents to raise a child without the logistical challenges of wrestling with childcare centres.

In the case of parents with more than one child, in-home care is also the more cost-effective option, as it is cheaper to hire one nanny for a day than pay for two or three children to attend a childcare centre. For example, with the average cost of day care being above \$90 in the greater Sydney area (please see Annexure A), hiring a nanny for two children at an average of \$160 for a day is cheaper than sending the two children to day care centres. At the same time having in-home care provides the child with a regular, safe and consistent life in the familiar home environment that is more akin to being cared for by one of the child's parents.

### **3. Based on appropriate and fiscally sustainable funding arrangements that better support flexible, affordable and accessible quality child care and early childhood learning**

The current childcare system can and needs to be dramatically improved both in terms of fiscal sustainability and in terms of the flexibility, affordability and accessibility of childcare options that are offered to parents. In our opinion, the recognition of in-home childcare as legitimate option together with a childcare tax

<sup>24</sup> <http://www.ucl.ac.uk/news/news-articles/1310/141013-bedtimes-linked-to-behavioral-problems-in-children>

<sup>25</sup> <http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Chapter10102008>

deduction would provide the necessary improvements. This tax deduction would not be a welfare measure but a measure to facilitate employment. It would recognise as legitimate an industry that already exists.

#### Harmful inconsistency in taxation policy

As stated above our approach is favoured by the 2006 Senate Inquiry *Balancing Work and Family* report. The report acknowledges that a tax deduction for childcare coupled with current childcare welfare is superior to the present system and should be offered as a choice to working parents<sup>26</sup>.

The 2006 Senate Inquiry *Balancing Work and Family* identified that “there is a logical inconsistency in the Government’s policy position on tax deductibility for child care”<sup>30</sup>. The report highlighted that the current exclusion of childcare costs from tax deductibility is a result of the interpretation of the *Income Taxation Act 1997* by the courts that is based on dated social norms<sup>31</sup>.

In addition, the report agreed with an earlier study that provided the following arguments in support of childcare costs being tax deductible:

“... such a system, by decreasing the net cost of going out of work, would encourage more women to earn taxable income, thereby increasing tax revenue. It also argued that welfare payments would be reduced and employment created as a result of increased demand for child care places, and that facilitating women’s return to the workforce after the birth of their children would result in a better return from public investment in the education and training of women.”<sup>32</sup>

Finally, the report noted that making childcare tax-deductible “would align government expenditure in this area more closely with workforce participation outcomes.”<sup>33</sup>

We provide the relevant section of the report at Annexure B.

We further note that the exclusion of childcare related expenses as tax deductions results in inconsistencies within Australia’s tax law. In 2009/2010 individuals claimed \$17.1 billion in work-related deductions, mostly for cars, uniforms and self-education expenses. If typists, utes and uniforms are legitimate expenses in earning income, why is childcare not? There is also no logic or practical benefit in the exclusion of a nanny’s wage from tax deductibility when the wages of secretaries or even off-shore services that are incurred in gaining a professional income are tax deductible.

There is a common law argument that the cost of childcare is a precursor to earning assessable income. Childcare costs have been treated as akin to travel expenses or the cost of clothing and therefore not incurred “in” the course of earning assessable income, which precludes childcare costs from being tax deductible.

<sup>26</sup> [http://www.aph.gov.au/parliamentary\\_business/committees/house\\_of\\_representatives\\_committees?url=fhs/workandfamily/report/reportfinal.pdf](http://www.aph.gov.au/parliamentary_business/committees/house_of_representatives_committees?url=fhs/workandfamily/report/reportfinal.pdf), pages 266

<sup>30</sup> *ibid*, page 254

<sup>31</sup> *ibid*, 256-261

<sup>32</sup> Cass B and Brennan B, ‘Taxing women: The politics of gender in the tax/transfer system’, eJournal of tax research (2003), University of New South Wales, vol 1, no 1, p 48. as cited at [file:///Users/Adrian/Downloads/http---www.aphref.aph.gov.au-house-committee-fhs-workandfamily-report-reportfinal%20\(2\).pdf](file:///Users/Adrian/Downloads/http---www.aphref.aph.gov.au-house-committee-fhs-workandfamily-report-reportfinal%20(2).pdf), page 254

<sup>33</sup> [http://www.aph.gov.au/parliamentary\\_business/committees/house\\_of\\_representatives\\_committees?url=fhs/workandfamily/report/reportfinal.pdf](http://www.aph.gov.au/parliamentary_business/committees/house_of_representatives_committees?url=fhs/workandfamily/report/reportfinal.pdf), pages 261

The courts have had no difficulty finding the necessary link between the salary paid to a secretary and the increased productivity and therefore increased income of a taxpayer, allowing the taxpayer to deduct the secretary's salary<sup>34</sup>. However when it comes to childcare costs, the courts have held that these costs are not "*incidental or relevant to the taxpayers activities of earning assessable income*"<sup>35</sup>. This argument has no logic nor reflects the realities of today's life: a parent with young children cannot work at all (unless they work from home) without childcare arrangements in place but can work quite effectively without a secretary, albeit possibly less productively. The Tax Act should not discriminate between types of employment when the employment can be demonstrated to have a necessary nexus with the earning of assessable income.

In the age of the Internet and digital dictation, the salary of the mailroom staff or the secretary are less relevant to the earning of assessable income than they once were. Arguably such expenses no longer satisfy "the essential character" test required by s.8-1 Income Tax Assessment Act 1997 (1997 Act). On the other hand, the increase in the number of parents working with young children has made childcare expenses more relevant and essential in the derivation of assessable income.

There is no cogent reason why the taxation legislation should draw an arbitrary line between a nanny's salary and a secretary's salary if there is a nexus with the employer/parent deriving assessable income. The salary of a nanny is no less of an expense incurred in "gaining or producing" assessable income than a secretary.

An employer, no matter how enlightened, would not allow a member of staff to bring a two year old to work every day of the year. Even if the employee could demonstrate they were able to work productively with the distraction of having their two-year-old child in the office, the other employees would complain about being disturbed. The reality is that parents with children cannot go to work unless arrangements are in place for the children to be cared for during office hours.

From a purely economic stance, there is no national interest in deductions being allowed for the payment made to a non-resident typist who types the digital dictation because that is an expense incurred in the course of earning assessable income, whilst tax deductions for the salary paid to the resident nanny are being barred to taxpayers.

Additionally, the unaffordability of nannies and the bureaucratic difficulties associated with accessing the Child Care Rebate for in-home care, outlined above, create a thriving black economy. Parents who have no other choice but to hire a nanny are forced to hire one outside the taxation system to save on paying taxes. As a result, the current system contributes to a black economy the size of which even according to conservative calculations is \$500 million a year<sup>36</sup>; surely this could not have been the government's intention. Recognising the provision of services by nannies providing in-home private care and making it a tax deductible expense to the parent/employer would go a long way to cleaning up the black economy, which is booming in this sector as well as the accompanying Centrelink fraud.

<sup>34</sup> Wells v Commissioner of Taxation 2000 ATC 2077

<sup>35</sup> Lodge v Commissioner of Taxation of the Commonwealth of Australia (1972) 128 CLR 171; Martin v FC of T 1983 83 ATC 4722; Douglas John Hyde v Commissioner of Taxation [1988] FCA ; Jayatilake v Federal Commissioner of Taxation (1919) 101 ALR 11

<sup>36</sup> [www.aphref.aph.gov.au-house-committee-fhs-workandfamily-report-reportfinal%20\(3\).pdf](http://www.aphref.aph.gov.au-house-committee-fhs-workandfamily-report-reportfinal%20(3).pdf) at pages 216-217

The Australian Taxation Office is aware that for every dollar in the black economy there is a dollar of social security fraud, but while there is no incentive to put nannies on the books, the leakage in revenue will continue to occur.

A further inconsistency becomes apparent when one considers that childcare centres are able to claim a tax deduction for the salary of their employees. The same should be afforded to working parents in employing a nanny, especially given the necessity of hiring one to remain in the workforce.

#### Fringe benefits tax (FBT)

Another flaw in the current tax system in relation to the provision of childcare is in the way exemptions to the FBT currently operate.

Presently, employees do not pay income tax on the portion of salary they sacrificed in return for the provision of childcare by their employer. Provided that the childcare is on business premises of the employer, the childcare is exempt from the FBT. In effect this means that employees, who have access to such employer-based childcare, tax deduct the money they expend on childcare.

Whilst the government intended that the exemption to the FBT would encourage Australian employers to aid their employees with childcare and concurrently increase women's workforce participation, the results of the exemption are lamentable. Because the FBT laws require that to qualify for the FBT exemption childcare provided by employers needs to be provided on their business premises, only the very large businesses are able to afford their employees such child care services.

The problem is even more pronounced as even the largest private companies are unwilling to provide these services due to the high costs – upwards of \$2 million – of setting up a childcare facility, the logistic and administrative inconveniences and the high risk rates involved<sup>37</sup>. For example, BHP Billiton cited that lack of expertise and potential community resentment due to the elitist nature of employer-provided childcare as factors that outweigh the benefits of providing childcare to employees<sup>38</sup>. Presently, we are only aware of five private sector employers who offer childcare benefits in Australia<sup>39</sup>. Also, people who are geographically removed from the child care services provided by their employer, cannot take advantage of the exemption.

The *Balancing Work and Family* report notes that the above factors result in gross injustice in who can take advantage of the exemption as only an "elite number of Australian employees are permitted to deduct the cost of child fees from their pre-tax income"<sup>40</sup>.

The issue becomes even more pronounced when one considers that 70% of people in Australia are employed by small and medium businesses<sup>41</sup> that do not provide, and have no means of providing, such child care as fringe benefits.

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<sup>37</sup> *ibid*, pages 234-241

<sup>38</sup> *ibid*, 241

<sup>39</sup> *ibid*, page 236

<sup>40</sup> *ibid*

<sup>41</sup> [http://www.abs.gov.au/websitedbs/d3310114.nsf/4a256353001af3ed4b2562bb00121564/d291d673c4c5aab4ca257a330014dda2/\\$FILE/RBA%20Small%20Business%20An%20economic%20Overview%202012.pdf](http://www.abs.gov.au/websitedbs/d3310114.nsf/4a256353001af3ed4b2562bb00121564/d291d673c4c5aab4ca257a330014dda2/$FILE/RBA%20Small%20Business%20An%20economic%20Overview%202012.pdf)

### Benefits of making in-home care tax-deductable

The financial benefits to the Australian economy of the inclusion of in-home childcare as a tax deduction are numerous.

If parents, particularly women, are able to offset their expenditure on in-home childcare, more of them will have the opportunity to remain in the workforce. This would eliminate the current losses suffered by the Treasury and the Australian community at large that we outline under the paragraph “Consequences of women not participating in the workforce” above. The *Game-changers: Economic reform priorities for Australia* released by the Grattan Institute in June 2012 estimates that if just an extra six per cent of women were retained in the workforce, Australia’s gross domestic product would increase by approximately \$25 billion<sup>42</sup>. Obviously, an economic gain of this level would easily offset the potential costs related to including in-home childcare as a tax deduction.

The Australian economy would also gain from the elimination of the childcare black-market that currently exists as parents will no longer have an incentive to resort to paying nannies ‘under the table’ if their expenditure on in-home care becomes tax deductible. This will provide additional benefits to the economy and revenue for the Treasury as nannies who are legally employed would pay tax and contribute to their superannuation.

In addition, making in-home care tax-deductible would achieve the objective of providing the flexible, accessible and affordable childcare that the government sets for the current Inquiry.

Finally, the criticism that a tax deduction is more valuable to women in higher income brackets and prejudices women on low incomes ignores the fact that women on low incomes currently receive significant Government assistance while women on higher incomes are left to fund their childcare needs out of their after tax income.

### Mechanisms for implementing tax-deductibility

Another argument in favour of making in-home childcare tax deductible is that it could be achieved with relative ease. There is no need for the parliament to pass new legislation. The 1997 Act already allows a deduction.

Section 8-1 of the 1997 Act provides:

- (1) You can deduct from you assessable income any loss or outgoing to the extent that:
  - (a) it is incurred in gaining or producing your assessable income; or
  - (b) [...]
- (2) However, you cannot deduct a loss or outgoing under this section to the extent that:
  - (a) [...]
  - (b) it is a loss or outgoing of a private or domestic nature;

It would be very easy for the government to direct the Commissioner of Taxation to allow tax deductions for child care expenses when the necessary nexus between child care and earning an assessable income is demonstrated.

<sup>42</sup> [http://grattan.edu.au/static/files/assets/bc719f82/Game\\_Changers\\_Web.pdf](http://grattan.edu.au/static/files/assets/bc719f82/Game_Changers_Web.pdf)

In practice, when taking advantage of tax-deductible childcare, we suggest that a parent should be required to obtain the hired nanny's tax file number and bank account. The tax deduction claimed by the parent would need to match the taxable income declared by the nanny. This would achieve transparency in terms of compliance with the Australian taxation system on the part of both the parent and the nanny.

By analogy with the deductions of tax in respect of the wages of secretaries not being capped, we suggest there should be no cap on the amount, which can be claimed for employing in-home childcare. This would guarantee healthy competition within the industry as parents could choose how much to pay a nanny based on the nanny's experience and qualifications.

To our knowledge there exist only two studies that have attempted to cost tax deductibility of childcare. The first is the evaluation by Dr Neil Warren of the Taxation Institute of Australia's proposal to the tax treatment of Childcare expenses in 1991, provided in Annexure C. The second is the report prepared by Econtech Pty Ltd for the House of Representatives Standing Committee on Family and Human Services in 2006<sup>43</sup>. Both Studies showed that the cost of providing a tax deduction for childcare was not significantly more than the current arrangements and would increase the revenue by increasing the income tax collected. The increase in revenue is likely to have been understated because of size of the black economy and the linked Centrelink fraud associated with private childcare arrangements.

#### Problems with child-care centres

The major argument against in-home childcare is the availability of childcare centres. However, in addition to unsuitability of childcare centres for many working parents identified above, there exist a number of other problems with the current system of childcare centres that the government should consider as part of the present Inquiry.

Firstly, Childcare centres receive 60% of the cost of each child from the Government yet still charge exorbitant amounts.

Secondly, Council subsidised childcare centres receive a rent subsidies yet charge as much as the private centres.

Finally, there are childcare centres that receive all the subsidies of not for profit organisations yet make substantial profit.

#### **4. Children's learning and development needs, including the transition to schooling**

There exists a significant pool of data that suggests that pre-school children's learning and development needs are better met through in-home care than institutional care. The Australian government should look into the formally recognised systems of in-home care that exist in countries such as New Zealand and the United Kingdom to provide a similar option of childcare to parents in Australia.

The 2008 NSW Department of Community Services report provides the findings of a number of independent studies that suggest that institutionalised care "rated significantly lower than childminders, relatives or nannies on measures of quality,

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<sup>43</sup> [www.aphref.aph.gov.au-house-committee-fhs-workandfamily-report-appendix.pdf](http://www.aphref.aph.gov.au-house-committee-fhs-workandfamily-report-appendix.pdf)



even including safety and health measures, and this applied irrespective of the cost of nurseries”<sup>44</sup>.

One of the widely recognised factors behind the quality of childcare is a high staff to child ratio<sup>45</sup>. This is because in large groups children have to compete for carer time, space and toys and the carers take on a predominantly supervisory role<sup>46</sup>. The provision of childcare on in-home basis means that the ratio of staff to child is very high. Even if a family has a number of children to be looked after by one nanny, this ratio is likely to be considerably higher than in a child care centre, translating into better quality childcare.

Another benefit of in-home care is that it does not create an artificial world for children like childcare institutions do but rather is more reflective of an authentic community based world<sup>47</sup>. Childcare provided at home is ‘relaxed’ and ‘enables an educator to build an intimate relationship with the children and their families in a model not dissimilar to extended family’<sup>48</sup>. Likewise, in-home care allows parents to choose the nanny they employ based on skill and trust, which guarantees a more personal relationship between all parties involved and is something that is not possible in an institutional setting.

One of the major criticisms levelled at in-home childcare in Australia is that nannies are unqualified and therefore the learning and development needs of children are not met by in-home childcare. This argument is made mostly by childcare centres who have a vested interest in the debate as their profits are dependent on attendance levels and they see a rise in in-home child-care as a threat to their business model. There is no reason why a private nanny should have lower qualifications than a carer employed in a day care centre. Australia should adopt a model of education programs for nannies such as those that exist in the UK and New Zealand.

Whilst official qualifications for nannies are not a legal requirement the governments of both the United Kingdom<sup>49</sup> and New Zealand<sup>50</sup> recognise that most parents expect a nanny to be qualified. Educational institutions in the United Kingdom and New Zealand<sup>51</sup> offer future nannies qualifications as high as bachelor degrees. The programs, as for example that at the Norland College<sup>52</sup>, are comprehensive and contain both theory and practical experience. In New Zealand, nannies are also required to meet the goals and learning outcomes for children through the delivery of the outcomes set by the Ministry of Education<sup>53</sup>. Such a system provides children with the benefits of home-based childcare whilst meeting children’s learning and developmental needs that are set by the government.

One of the authors of this submission, Louise McBride, employed Norland Nannies. She found that they were highly trained and suitable to her circumstances, as she

<sup>44</sup> [http://www.community.nsw.gov.au/docswr/assets/main/documents/research\\_qualitychildcare.pdf](http://www.community.nsw.gov.au/docswr/assets/main/documents/research_qualitychildcare.pdf), p11 and <http://taskforce.ece.govt.nz/wp-content/uploads/2010/11/ECE-Literature-Review.pdf>, p8

<sup>45</sup> <http://taskforce.ece.govt.nz/wp-content/uploads/2010/11/ECE-Literature-Review.pdf>, p52

<sup>46</sup> *ibid*, pp57-58

<sup>47</sup> [http://www.nzabe.ac.nz/conferences/2001/pdf/05\\_saturday\\_pm/lynette\\_wrigh-progpaper.pdf](http://www.nzabe.ac.nz/conferences/2001/pdf/05_saturday_pm/lynette_wrigh-progpaper.pdf), pp7-8

<sup>48</sup> <http://www.educate.ece.govt.nz/~media/Educate/Files/Reference%20Downloads/InfantsAndToddlers/HomeBasedECE.pdf>, page 1

<sup>49</sup> <http://www.nidirect.gov.uk/nannies-qualifications-and-skills>

<sup>50</sup> <http://www.careers.govt.nz/jobs/education/nannychild-carer/how-to-enter-the-job>

<sup>51</sup> <http://www.careers.govt.nz/qualifications/view/CA2335/6004>

<sup>52</sup> [http://www.norland.co.uk/courses/view/ba\\_hons1#2014\\_course\\_map\\_and\\_modules](http://www.norland.co.uk/courses/view/ba_hons1#2014_course_map_and_modules)

<sup>53</sup> <http://www.educate.ece.govt.nz/~media/Educate/Files/Reference%20Downloads/InfantsAndToddlers/HomeBasedECE.pdf>, page 2



needed to be able to go to work with the knowledge that her children were in capable hands and did not have to worry about their wellbeing during working hours.

The COAG Reform Council *Education in Australia 2012: Five years of performance* report found that pre-primary education is linked to better results at school<sup>54</sup> and recommended that preschool attendance must rise to 15 hours per week for children in Australia<sup>55</sup>. At the same time, the report does not suggest that preschool learning should be conducted through childcare centres. The report defined suitable pre-primary education as: “a structured, play-based learning program, delivered by a degree qualified teacher, primarily aimed at children in the year before they commence full-time schooling. This is irrespective of the type of institution that provides it, or whether it is government funded, or privately provided”. We suggest that a qualified nanny with a degree in preschool education can provide a child with a much better pre-primary education to a child due to the reasons outlined above.

A major alternative to nannies for parents in Australia has been grandparent childcare. However, grandparent childcare is not widely available to parents of young children and is becoming increasingly less so as the retirement age in Australia keeps increasing and people stay employed into their 70s. Also, childcare is a stressful activity and there are studies that suggest that a large proportion of grandparents who do fulfil childcare roles wish they did not have this stressful commitment<sup>56</sup>. The availability of nannies would not only aid to fill the void for parents of young children who do not have access to grandparent childcare but also alleviate the stress for a lot of grandparents who currently fulfil the roles of child carers.

### Teenage children

Finally, in-home childcare is vital for parents with teenage children, who are not afforded after-school care. Teenagers are in no lesser need of supervision than younger children yet at present there do not exist any childcare services directed at them.

Teenagers have a heightened risk to succumbing to bad influences. Some of the dangers that many teenagers face in the absence of supervision are pornography, introduction to drugs, unhealthy nutrition and decreased academic performance due to lack of supervision.

For example, many of today’s teenagers, when unsupervised, loiter in the afterschool hours in shopping malls, on streets or at the beach instead of doing their homework in a safe environment.

It is very important for working parents to know that somebody is picking their children up from school and supervising them in the after-school hours whilst they are still at work. Currently only in-home childcare can provide this service.

### **Conclusion**

We recommend that in-home childcare should be developed by the Australian government and provided to parents who are in need of it with subsidies made in the form of tax-deductions.

<sup>54</sup> <file:///Users/Adrian/Downloads/COAG%20reform%20council.pdf>, page 19

<sup>55</sup> *ibid* 8

<sup>56</sup> [http://www.uws.edu.au/\\_\\_data/assets/pdf\\_file/0009/156339/Jenkins.pdf](http://www.uws.edu.au/__data/assets/pdf_file/0009/156339/Jenkins.pdf)

If you have any questions or would like to discuss this matter further, we would be pleased to hear from you.

Yours Sincerely,

Louise McBride, Sophie Gerber and Vladimir Kravchenko

# Annexure A

Suburb	Name	Average cost per day
Mosman	Giraffe Early Learning Centre	\$125.00
	Goodstart Early Learning	\$115.92
	Heritage House Beauty Point Child Care And Learning Centre Service	\$99.20
	Mosman Kinderland -\$83	\$83.00
	Mosman Occasional Childcare Centre and Long Day Care (MOCC)	\$90.00
	Only About Children Mosman	\$132.00
	Sally's Place	\$154.00
	<b>Average cost per day in Mosman</b>	<b>\$114.16</b>
Hurstville	CASS Hurstville Child Care Centre	\$79.00
	Goodstart Early Learning Hurstville - Forest Road	\$86.96
	Goodstart Early Learning Hurstville - Millet Street	\$93.46
	Hurstville Possums Child Care Centre	\$80.00
	Hurstville Preschool and Occasional Care	\$57.00
	Hurstville Teddy Bear Child Care	\$83.00
	Kiddyland Childcare Centre	\$84.00
	Kidz On The Avenue	\$82.50
	Teddy Bear Early Learning Centre	\$87.00
	<b>Average cost per day Hurstville</b>	<b>\$96.84</b>
Bondi Junction	Goodstart Early Learning Bondi Junction - Oxford Street North	\$123.98
	Goodstart Early Learning Bondi Junction - Oxford Street South	\$123.98
	Goodstart Early Learning Bondi Junction - Oxford Street West	\$128.58
	The Grace Child Care Centre	\$100.00
	Waverley Early Education Centre	\$71.60
	Wee Care 2 Child Care Centre	\$112.00
	Wee Care Kindergarten	\$112.00
	<b>Average cost per day in Bondi Junction</b>	<b>\$110.31</b>
Parramatta	Westfield Kids World	\$80.00
	Reggio Emilia Early Learning Centre Parramatta CBD	\$91.50
	Goodstart Early Learning Parramatta	\$89.54
	<b>Average cost per day in Paramatta</b>	<b>\$95.87</b>
Ashfield	Ashfield Little Bunnies Day Care Centre	\$83.00
	Ashfield Baptist Long Day Care	\$85.40
	Goodstart Early Learning Ashfield	\$104.34
	The Infants Home Learning & Development Centre - Robinson House	\$92.75
	The Infants Home Child and Family Services - Johnson House	\$92.00
	The Infants Home Child and Family Services - Robinson House	\$92.75
	<b>Average cost per day in Ashfield</b>	<b>\$91.71</b>

<b>Baulkham Hills</b>	Balcombe Heights Child Care Centre	\$84.80
	Dashing Ducks Pre-School	\$86.20
	Early Learning Centre Baulkham Hills	\$87.00
	Giggles Child Care Centre Baulkham Hills	\$94.00
	Hillsong Child Care Centre	\$96.63
	Little Angels Early Learning Centre	\$91.00
	Norwest Child Care Centre	\$83.20
	<b>Average cost per day in Baulkham Hills</b>	<b>\$88.98</b>
	<b>Total average:</b>	<b>\$99.65</b>

## Annexure B

## Choice and flexibility in child care

- 6.1 Child care issues have dominated this inquiry. Over two-thirds of the submissions received make comment on the accessibility and affordability of child care in Australia, and its impact on women's ability to participate in paid work at an optimum level. Continuing increases in women's workforce participation, the intensity of modern working lifestyles and pressures of cost and supply in the child care market are highlighting child care as a flashpoint in balancing parenting with paid work.
- 6.2 As noted in the previous chapter, difficulties in accessing child care not only push families to make stressful compromises, but directly affect labour market participation. Single parents are particularly affected, given the simple fact that one parent cannot be in two places at once. Women are also particularly affected, as child care, whether provided by the mother or by someone else, is still often conceptualised as a mother's responsibility, particularly if she is a part time or secondary earner relative to a full time breadwinner.<sup>1</sup>
- 6.3 This chapter is about developing a child care system that provides parents with more choice and flexibility in the types of child care that are available to them, and real support for those choices from government.

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1 Smyth C, Rawsthorne M and Siminski P, Social Policy Research Centre, University of New South Wales, *Women's lifework: Labour market transition experiences of women, final report* (2006), SPRC report 7/06, p 55.

## Use of child care in Australia

### Types of care

- 6.4 A survey conducted in 2005 by the Australian Bureau of Statistics found that in any given school week, 35 per cent of Australian children aged 0-4 received formal child care; that is, regulated care that takes place away from the child's home.<sup>2</sup>
- 6.5 Informal care, which includes care by family members, friends, neighbours, babysitters and in-home (nanny) care, was used by 38.4 per cent of children aged 0-4, either alone or in combination with formal care.<sup>3</sup>
- 6.6 The use of formal care varies with age. As figure 6.1 shows, the use of formal care for very young children is low, but by the age of two, 46.3 per cent of children are in formal care; and by the age of three, 53.4 per cent. From age four, when many children have started preschool, the percentage of children in formal care begins to decline. Seventeen per cent of 6-8 year olds attended formal care, down to eight per cent for 9-12 year olds.<sup>4</sup>
- 6.7 The use of informal care peaks between the ages of nought and two, possibly reflecting parents' preferences for infants and very young children to be cared for in the home; if not by themselves, by an in-home carer, grandparent, friend or relative. Informal care use varies less with age than formal care. A significant number of children aged 5-12 are still receiving informal care after formal care use has tapered off.

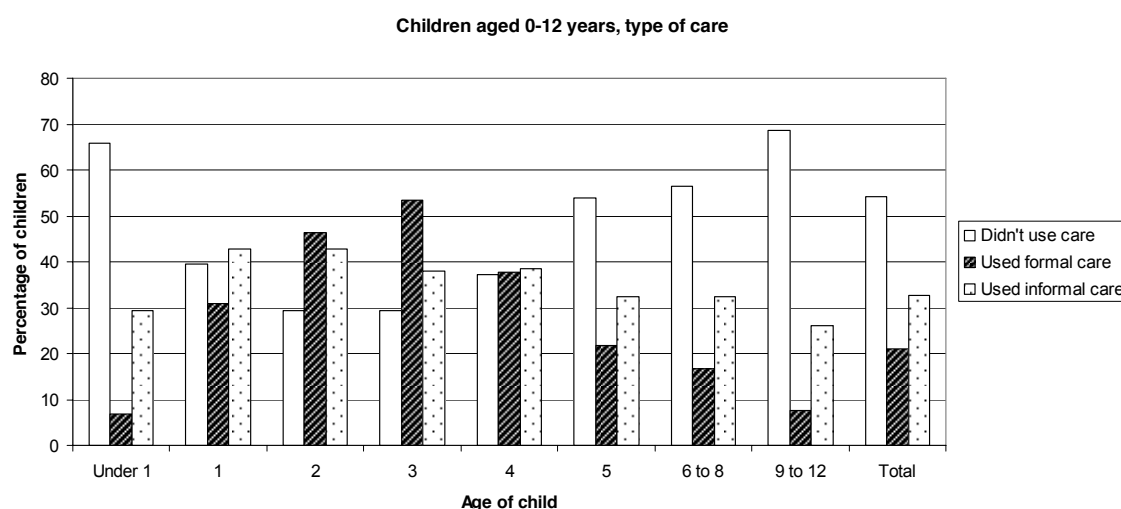
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2 Australian Bureau of Statistics, *Child care, Australia, Jun 2005* (2006), Cat No 4402.0, p 42.

3 Australian Bureau of Statistics, *Child care, Australia, Jun 2005* (2006), Cat No 4402.0, p 42.

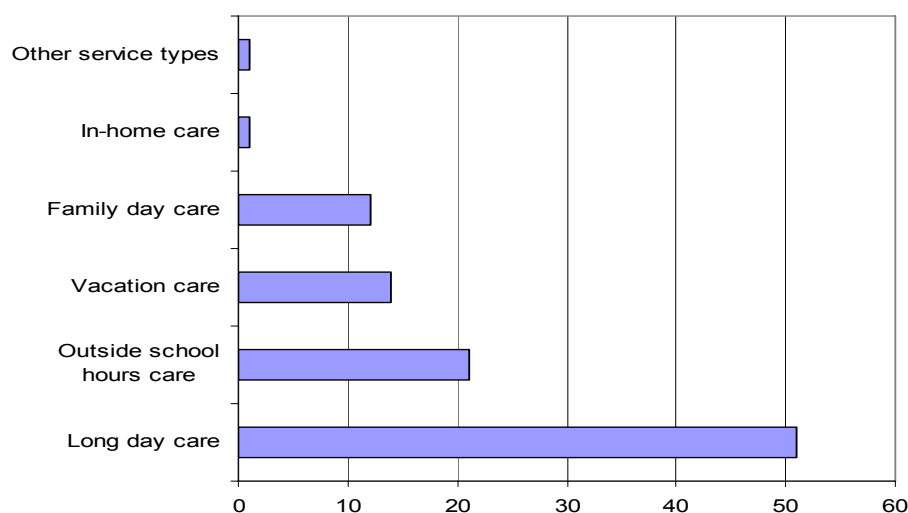
4 Australian Bureau of Statistics, *Child care, Australia, Jun 2005* (2006), Cat No 4402.0, pp 4, 14.



**Figure 6.1 Use of formal and informal child care in Australia, 2005**

Source: Australian Bureau of Statistics, *Child care, Australia, June 2005 (2006)*, Cat No 4402.0, p 14.

6.8 Amongst those children receiving formal child care, the majority are in long day care, as figure 6.2 illustrates:

**Figure 6.2 Children by formal child care service type, 2004 (%)**

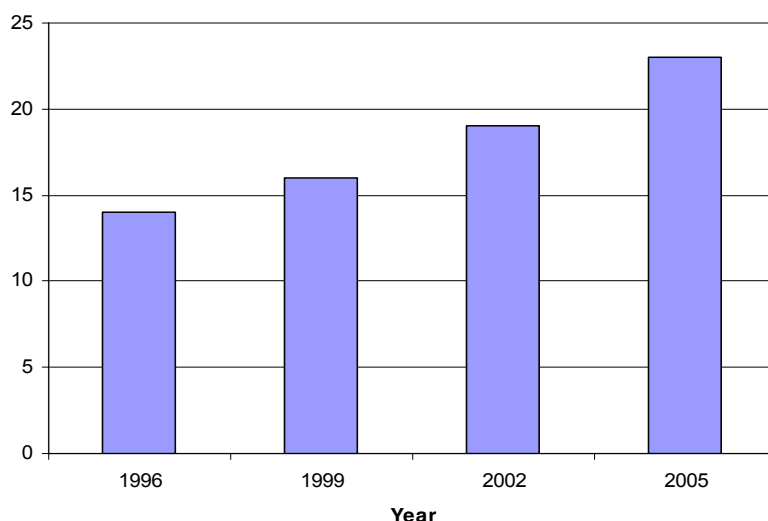
Source: Department of Family and Community Services, *2004 Census of child care services (2005)*, p 13. This data covers children in government-funded care only, and does not include children being cared for informally by family members or friends, or through a cash arrangement with an unregistered in-home carer. The in-home care category refers to care provided under the Australian Government's In-Home Care program.

6.9 Regular survey data is revealing steady increases in the use of formal care. This may reflect increasing women's workforce participation; the increased workforce participation of mature workers who can longer care

for grandchildren; family isolation from support networks; and changing social attitudes towards the use of child care.

- 6.10 As figure 6.3 shows, the proportion of children using formal care, either alone or in combination with informal care, has increased nine percentage points since 1996, from 14 to 23 per cent.<sup>5</sup> The figures from the 2004 census of child care services, published by the Department of Family and Community Services, suggest an even larger increase. The census reports that since 1999, the number of children in formal care had increased by an estimated 30 per cent.<sup>6</sup> These increases may have been even more significant if not for strong unmet demand for child care places in many areas of Australia.

**Figure 6.3 Proportion of Australian children aged 0-11 who used formal care 1996-2005 (%)**



Source: Australian Bureau of Statistics, *Child care, Australia, June 2005 (2006)*, Cat No. 4402.0, p 3. Formal care refers to regulated care that takes place away from the child's home, for example long day care, before and/or after school care and family day care.

- 6.11 Increases in the number of children in care are corroborated by increases in the number of child care services in Australia. The 2004 census of child care services found that the number of child care services had increased seven per cent in only two years. The strongest increases were in the long day care sector, at eight per cent, and in in-home care services, at 44 per

5 Australian Bureau of Statistics, *Child care, Australia, June 2005 (2006)*, Cat No 4402.0, p 3.

6 Department of Family and Community Services, *2004 Census of child care services (2005)*, p 13. The differences in statistical estimates may be accounted for in definitional slippage between formal and informal care (ABS); and Australian Government approved care and other care (FACS).

cent. The dramatic increase in in-home care services was partly due to the fact that the program was still in an implementation phase.<sup>7</sup>

## Work-related child care

6.12 Unsurprisingly, child care use is more likely when both parents in a family are employed, or when a sole parent is employed.<sup>8</sup> Work-related reasons are the most common for parents using formal child care in Australia.<sup>9</sup> As table 6.1 shows, this relationship is strongest for outside school hours care, vacation care and long day care, with over 90 per cent of care hours being work-related. Across the different types of formal care, an average 83 per cent of care hours are work-related.

**Table 6.1 Percentage of care that is work-related (as % of hours of care)**

Long day care	90%
Family day care	88%
Outside school hours care	97%
Occasional care	49%
Vacation care	93%

Source: Department of Family and Community Services, *2004 Census of child care services (2005)*, p 15.

## Child care costs

6.13 There is little current data on average child care costs in Australia, especially given that child care costs are increasing at a rate far in excess of CPI.<sup>10</sup> The Australian Bureau of Statistics conducted a Child Care Survey in 2005, but the data collected details only the cost of care net of Child Care Benefit, rather than the actual fees charged by child care providers.<sup>11</sup> The most recent comprehensive statistical data to do this comes from the 2004 census of child care services conducted by the Department of Family and Community Services.

6.14 Table 6.2 details the average fees reported to the Department by child care providers in 2004:

7 Department of Family and Community Services, *2004 Census of child care services (2005)*, pp 7, 9.

8 Australian Bureau of Statistics, *Child care, Australia, June 2005 (2006)*, Cat No 4402.0, p 9.

9 Australian Bureau of Statistics, *Child care, Australia, June 2005 (2006)*, Cat No 4402.0, p 5.

10 Taskforce on Care Costs, *2006 Interim review: Where are we now? (2006)*, p 7.

11 Australian Bureau of Statistics, *Child care, Australia, June 2005 (2006)*, Cat No 4402.0, p 6.

**Table 6.2 Average fees for child care services, 2004**

Average weekly fees		Average hourly fees	
Private long day care	\$208	Occasional care	\$5.35
Community long day care	\$211	In-home care	\$11.84
Family day care	\$185		
Vacation care	\$139		

Source: Department of Family and Community Services, *2004 Census of child care services* (2005), p 11. Given the data subsequently published from the census by the Productivity Commission, it would appear that average weekly fees refer to the cost of 50 hours of care. Productivity Commission, *Report on Government services 2006* (2006), vol II, p 14.22. Such a figure is not available for other types of care as they have different fee structures.

- 6.15 The census also reported that outside school hours care services charged on average \$6.68 per session for before school care, and \$10.28 per session for after school care. Before school care providers offered an average session of one hour and 53 minutes, while after school care providers offered an average session of three hours and two minutes.<sup>12</sup>
- 6.16 Child care costs appear to reflect local characteristics of supply and demand, as well as state requirements that may influence fees through differences in staffing ratios, licensing, wages, and whether fees are charged for additional supplies such as nappies and meals.<sup>13</sup> The 2004 census of child care services, for example, found that while the average weekly fee for a long day care centre in Queensland was \$195, it was \$229 in the Australian Capital Territory.
- 6.17 Anecdotal evidence provided to the committee confirms that long day care fees vary greatly across Australia, between states and between regional and metropolitan areas. While fees in regional areas and some states can be \$40 or \$50 per day, fees reported to the committee by mothers living in Sydney and Melbourne ranged between \$70 and \$120 per day. One Sydney mother made the extraordinary admission that she had sent one of her children to a top private school a year early, because it was cheaper than child care.<sup>14</sup>
- 6.18 Fees are highest for nought to two year olds, due to higher staffing ratios and more intensive caring requirements. The 2004 census of child care services found that while the average weekly cost of long day care was

12 Department of Family and Community Services, *2004 Census of child care services* (2005), pp 114, 119.

13 Productivity Commission, *Report on Government services 2006* (2006), vol II, p 14.23.

14 Clark K, transcript, 22 September 2005, p 44.

\$208, this rose to \$210 for a two year old, and \$218 for a one year old.<sup>15</sup>

More recently, the Benevolent Society, who operate two child care centres in Sydney's eastern suburbs, told the committee that, 'We now find that we need to set our fees for children under two years of age at \$75 - \$80 per day just to break even'.<sup>16</sup>

- 6.19 Calculations by the National Centre for Social and Economic Modelling (NATSEM) on the Australian Bureau of Statistics' 2002 child care survey reveal that there is not a strong relationship between parental income and child care usage.<sup>17</sup> In fact, child care usage is represented fairly evenly across all income scales. At the lower end of the income scale, this reflects the targeted assistance provided by the Child Care Benefit. At the higher end of the income scale, there is a likelihood that families will have two parents working and thus have a greater propensity to use child care. Nevertheless, increasing care costs since 2002 may be putting pressure on families' ability to access care.

## Informal care arrangements

- 6.20 In 2005, 32.6 per cent of children aged 0-12 and 38.4 per cent of children aged 0-4 received regular informal care, either alone or in combination with formal care.<sup>18</sup> Informal care, under the Australian Bureau of Statistics' definition, includes care by family members, friends, neighbours, babysitters and in-home (nanny) carers. It is grandparents who are the main informal carers, providing care for 20 per cent of children aged 0-12. A further five percent of children receive care from a sibling or another relative in any given reference week.<sup>19</sup>
- 6.21 Many grandparents in Australia selflessly provide hours of child care every week, 'taking on the role sometimes lovingly, but not necessarily willingly'.<sup>20</sup> They make it possible for their adult children to work without incurring child care costs.
- 6.22 Grandparent care is not an option for all families. Grandparents may well be living thousands of kilometres away. Parents who do not have the

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15 Department of Family and Community Services, *2004 Census of child care services* (2005), pp 28, 29.

16 Benevolent Society, sub 80, p 2.

17 National Centre for Social and Economic Modelling, *Who cares? The cost of caring in Australia in 2002 to 2005* (2006), AMP.NATSEM Income and Wealth Report, issue 13, p 7. These figures predate the introduction of the Child Care Tax Rebate.

18 Australian Bureau of Statistics, *Child care, Australia, June 2005* (2006), Cat No 4402.0, pp 14, 42.

19 Australian Bureau of Statistics, *Child care, Australia, June 2005* (2006), Cat No 4402.0, p 3.

20 Quinlan F, Catholic Welfare Australia, transcript, 19 April 2005, p 36.

physical and emotional support of extended family in their local area feel this absence keenly.<sup>21</sup>

- 6.23 Even when grandparents are nearby, grandparent care is not necessarily a solution. Increased longevity and the need to increase superannuation savings mean that some grandparents are still working themselves, up to and beyond what has hitherto been regarded as retirement age. The number of women aged over 65 in paid employment increased by 85 per cent between 1984-85 and 2004-05. The number of men aged over 65 in paid employment increased by 20.5 per cent; one of only two male age cohorts that increased their participation over the last twenty years. The other was for men aged 55 to 64.<sup>22</sup>
- 6.24 Even in the shorter term, there have been increases to mature age workforce participation, possibly fuelled by changes to superannuation law. In their report commissioned by the committee, Access Economics notes that participation rates for older workers are rising at a faster rate than anticipated in the intergenerational report of 2002.<sup>23</sup>
- 6.25 The committee received a number of comments from parents trying to balance their urgent need for child care with a sensitivity for the needs of grandparents:

For the last 18 months prior to this year, there were just no vacancies, despite being on the waiting list, and we were forced to rely primarily on my mother and friends in order to get by. Bear in mind that both my parents have failing health and my mother also works a full-time night job in her own right on the days I am not working.<sup>24</sup>

I used to be able to rely upon my parents a lot. My father has now passed away... I know my mother has got a plateful [dealing with other family members], so I just do not feel it is my place to impinge on her any more than I have to. I have a nephew and his wife that can sometimes help out with babysitting.<sup>25</sup>

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21 Smyth C, Rawsthorne M and Siminski P, Social Policy Research Centre, University of New South Wales, *Women's lifework: Labour market transition experiences of women, final report* (2006), SPRC Report 7/06, p 54; see also Bentley S, sub 43; McLachlan E, sub 194.

22 Australia Bureau of Statistics, *Year Book Australia, 2006* (2006), Cat No 1301.0, p 153.

23 Access Economics, Appendix D, p 5.

24 Watson K, transcript, 21 June 2006, p 2.

25 Richards P, transcript, 30 June 2006, p 20.

Although we are now nearer my husband's parents, they are still an hour away and both work full-time. So they can provide us little support for child care.<sup>26</sup>

I think a lot of people juggle with their parents, 'Can the grandparents look after them?' or whatever. I did not want to burden my mum with that because she has already raised a family. I know a lot of people rely on grandparents, and if the grandparents are not available then day care can sometimes be more expensive than what you are earning. Everyone has that struggle... So, definitely, having someone regularly to be a carer for your child, because it is paid work, means that it is a lot easier – asking someone that you are employing to work rather than trying to get your parents, friends or whatever to rearrange their life.<sup>27</sup>

- 6.26 Other sources of informal care are also increasingly difficult to find. As a Perth mother observed:

Our support networks are often thinner than they used to be. We don't tend to live as near family as we used. Grandparents may be busy doing their own things, possibly still working themselves, to take grandchildren for extended periods. We don't know our neighbours like we used to, particularly if we are still working as we'll never see them.<sup>28</sup>

- 6.27 The committee acknowledges the enormous contribution of grandparents in raising and caring for children, usually with little or no financial compensation. Measures such as the Grandparent Child Care Benefit are positive recognition of this contribution.
- 6.28 Indications are, however, that neither parents nor government policy can continue to rely on grandparents as a source of low or no-cost care. The government has a policy of encouraging mature aged workers to remain in the workforce, and has put several initiatives in place to achieve this, such as the Pension Bonus Scheme and changes to superannuation announced in the 2006-07 Budget. Relying on grandparents to provide care while their adult children work is in conflict with this policy.
- 6.29 Some parents feel more comfortable leaving their children with a family member or friend rather than a 'stranger' in a child care centre. Others, like one of the mothers quoted above, prefer to secure care within a

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26 Langham J, sub 171, p 2.

27 Romer J, transcript, 18 October 2006, pp 10, 11.

28 Davies K, sub 4, p 2.



business agreement where roles and responsibilities are clearly defined. Informal arrangements do have the advantages of being cheap and flexible. Realistically, however, the use of child care provided by carers who are not family members or friends will continue to increase. The availability and accessibility of child care will continue to play a significant role in Australian families' decisions about work and family.

## Child care and the economy

### Facilitating economic activity

- 6.30 Government expenditure on child care is often characterised as a 'soft' welfare measure. The committee is of the view, however, that child care should be recognised as a measure that supports a range of essential economic activities. This is true both now and increasingly as the ageing population presses workforce participation and national productivity downwards. As economic commentator Ross Gittins writes in *The Sydney Morning Herald*, child care is the key to keeping 'an ever-growing proportion of well-educated married women' in the workforce: 'Be clear: fixing child care is as much about economics narrowly defined as it is about social concerns'.<sup>29</sup>
- 6.31 Several government-sponsored studies in the last 15 years have examined the economic benefits of child care. In 1994, the Australian National Audit Office, in an 'efficiency audit' of Commonwealth child care services, reported that work-related child care was revenue-neutral:
- The costs to the Commonwealth of workforce-related care are substantial, but the break-even point where tax revenue and social security savings equal this cost in all cases comes well below average earnings.<sup>30</sup>
- 6.32 Similarly, a 1998 study by the Centre for Economic Policy Research at the Australian National University found that:

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29 Gittins R, 'Costello's failed experiment: reform without pain', *The Sydney Morning Herald*, 15 May 2006, p 19.

30 Australian National Audit Office, *Mind the children: Management of children's services* (1994), Efficiency Audit, Audit Report no 42, 1993-94, p 42; cited in Senate Community Affairs Reference Committee, *Report on Child Care Funding* (1998), p 9.

Child care has a net cost to the budget far less than the gross cost... and could very likely save taxpayers more than it costs.<sup>31</sup>

By attracting more women into the labour force, the Children's Services Program [government funding for child care] helps to decrease interruption to careers, which has beneficial effects for society as well as for the individual. With less depreciation of work-related skills and a greater commitment to the labour force as a result of the program, the economy will tend to create better jobs than it would do in the absence of the program. Also, the increase in female labour supply resulting from the program will generate more jobs in the longer term.<sup>32</sup>

6.33 Most recently, a research paper published by the Department of Families and Community Services in 2004 made a preliminary assessment of the actual value of these returns to the government. It estimated that in 2001-02, paid work facilitated by government-funded child care use generated \$1.6 billion in income tax, breaking even with the \$1.6 billion spent by the Government on child care.<sup>33</sup>

6.34 The government also saves money, however, on foregone income from Family Tax Benefit and Parenting Payment. Taking this into account, the paper found that:

Every dollar spent on child care returns \$1.86 directly to the Government's bottom line, in the form of increased taxation and reduced government outlays.<sup>34</sup>

6.35 These findings are consistent with international studies on the economic value of child care:

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31 Centre for Economic Policy Research at the Australian National University, for the Department of Community Services and Health, *Government spending on work-related child care: Some economic issues* (1988), p 1.

32 Centre for Economic Policy Research at the Australian National University, for the Department of Community Services and Health, *Government spending on work-related child care: Some economic issues* (1988), p 1.

33 Martin J, Department of Family and Community Services, 'More than just play dough: A preliminary assessment of the contribution of child care to the Australian economy', *Australian Social Policy* (2004), p 9, viewed on 10 March 2006 at [http://www.facs.gov.au/research/austsocpolicy\\_2004/australian\\_social\\_policy\\_2004.pdf](http://www.facs.gov.au/research/austsocpolicy_2004/australian_social_policy_2004.pdf).

34 Martin J, Department of Family and Community Services, 'More than just play dough: A preliminary assessment of the contribution of child care to the Australian economy', *Australian Social Policy* (2004), p 9, viewed on 10 March 2006 at [http://www.facs.gov.au/research/austsocpolicy\\_2004/australian\\_social\\_policy\\_2004.pdf](http://www.facs.gov.au/research/austsocpolicy_2004/australian_social_policy_2004.pdf).

Returns to the government budget, per dollar spent, have variously been estimated at \$1.56 in Texas; \$1.50 to \$3.00 for the United States in total... and \$2.00 in Canada.<sup>35</sup>

- 6.36 The actual returns to government, however, will be even greater, as these figures represent only the impact on the government's bottom line. The more diffuse effects of increased economic activity and other flow-on effects multiply the benefits many times over. These include:
- increased productivity;
  - increased household expenditure;
  - increased superannuation for carers and others remaining in the workforce;
  - reduction in the child care cash economy, and an increase in income tax paid by child care workers; and
  - skill retention and decreased business staff turnover costs.<sup>36</sup>
- 6.37 The value of diffuse benefits is, of course, difficult to measure accurately. The Department of Family and Community Services paper estimates the total economic benefits of child care to be worth \$8.11 per dollar spent. On current government child care expenditure of \$2.3 billion dollars per annum, this estimate suggests a return of \$18.6 billion to the economy.<sup>37</sup>
- 6.38 As Jay Martin writes, 'The value of the [child care] sector is not only what it produces, but also what it supports others to produce.'<sup>38</sup> He argues that child care should be considered among the essential infrastructure of an industrial Western economy:

In 2002 in Australia, around half of all children in the 0 to 11 age group used care, a total of around 1.5 million children (Australian Bureau of Statistics (ABS) 2003). The skills and experience of the

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35 Martin J, Department of Family and Community Services, 'More than just play dough: A preliminary assessment of the contribution of child care to the Australian economy', *Australian Social Policy* (2004), p 9, viewed on 10 March 2006 at [http://www.facs.gov.au/research/austsocpolicy\\_2004/australian\\_social\\_policy\\_2004.pdf](http://www.facs.gov.au/research/austsocpolicy_2004/australian_social_policy_2004.pdf).

36 Taskforce on Care Costs, *Where to now? 2006 Final report* (2006), pp 4-5, 33.

37 In the 2006-07 Federal Budget, the Minister for Families, Community Services and Indigenous Affairs, the Hon Mal Brough MP, announced a record \$9.6 billion investment in child care over four years. '2006-07 Budget - A more responsive, quality child care system', media release, 9 May 2006.

38 Martin J, Department of Family and Community Services, 'More than just play dough: A preliminary assessment of the contribution of child care to the Australian economy', *Australian Social Policy* (2004), p 3, viewed on 10 March 2006 at [http://www.facs.gov.au/research/austsocpolicy\\_2004/australian\\_social\\_policy\\_2004.pdf](http://www.facs.gov.au/research/austsocpolicy_2004/australian_social_policy_2004.pdf).

parents of these children obviously represent a considerable economic and social resource to the community, much of which would be unavailable to employers for substantial periods of time if child care was not available.

Therefore, one of the major contributions that child care makes is to enable the 'nation's pool of talented and skilled parents to engage in the formal economy', as MCubed [a consultancy] noted in 2002. This places it among the essential infrastructure of a society, such as transportation, telecommunications or education, without which a range of economic activities would not be possible.<sup>39</sup>

- 6.39 A 2003 OECD paper on the labour force participation of women also supports the view of child care as a facilitator of economic activity. For low income families, particularly, government child care assistance can operate as a financial 'leg-up' into the labour market and path to increased future earnings for parents:

Credit market imperfections (such as adverse selection and moral hazard) may prevent women in low-income families from borrowing against future earnings to finance child care and break away from welfare dependence (Walker, 1996). The implicit assumption is that employment facilitates the accumulation of human capital and work experience which will generate future earnings sufficiently high to repay the initial loan. Thus, child care subsidies could be expected to result in lower future welfare spending (Robins, 1991).<sup>40</sup>

## Long-term socio-economic outcomes

- 6.40 Beyond returns to the bottom line in each budget cycle, government investment in child care also contributes to important long-term socio-economic outcomes. The OECD paper cited above notes additional justifications for government expenditure on child care, including child development, social integration, and gender equity.<sup>41</sup> Increasing evidence

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39 Martin J, Department of Family and Community Services, 'More than just play dough: A preliminary assessment of the contribution of child care to the Australian economy', *Australian Social Policy* (2004), p 3, viewed on 10 March 2006 at [http://www.facs.gov.au/research/austsocpolicy\\_2004/australian\\_social\\_policy\\_2004.pdf](http://www.facs.gov.au/research/austsocpolicy_2004/australian_social_policy_2004.pdf).

40 Jaumotte F, 'Labour force participation of women: Empirical evidence on the role of policy and other determinants in OECD countries' (2003), *OECD Economic Studies*, no 37, p 60.

41 Jaumotte F, 'Labour force participation of women: Empirical evidence on the role of policy and other determinants in OECD countries' (2003), *OECD Economic Studies*, no 37, p 60.

in early childhood development is supportive of the gains achieved by quality child care for future social health and wellbeing:

Child care contributes to the economy by acting as an early intervention in children's lives. Quality child care, which is of great benefit to disadvantaged and at-risk children, decreases health, welfare and legal cost outlays by Government and decreases the chance of these occurring later in life.<sup>42</sup>

Alternatively, as a 1988 report into government funded child care put it, 'Well-brought up children make good citizens – less crime, better voters, larger tax base.'<sup>43</sup>

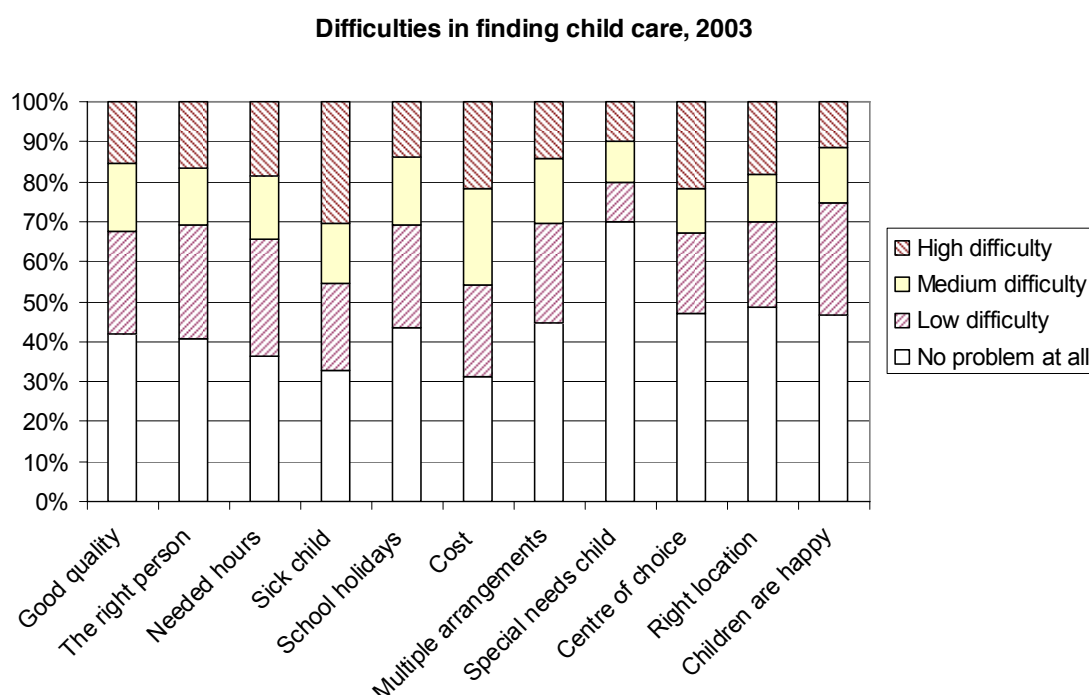
## Problems in accessing care

- 6.41 Unfortunately, given the economic importance of child care provision, some Australian families are experiencing problems in accessing affordable care. In part, this is the result of present child care policy and its total lack of flexibility. For most families, the approved care category, which is the only category for which any meaningful assistance is provided, offers only group care in a centre-based environment. It provides one solution to fit all when clearly families' wants and needs are different.
- 6.42 As figure 6.4 illustrates, these wants and needs are diverse. Some of the criteria that parents consider are subjective, for example, whether a parent feels that their child could be happy in an arrangement. Others are not discretionary. School holidays and sick children are particular hot spots, and parents have little influence over the number of hours and days they are offered by a child care centre.

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42 Martin J, Department of Family and Community Services, 'More than just play dough: A preliminary assessment of the contribution of child care to the Australian economy', *Australian Social Policy* (2004), p 5, viewed on 10 March 2006 at [http://www.facs.gov.au/research/austsocpolicy\\_2004/australian\\_social\\_policy\\_2004.pdf](http://www.facs.gov.au/research/austsocpolicy_2004/australian_social_policy_2004.pdf).

43 Centre for Economic Policy Research at the Australian National University, for the Department of Community Services and Health, *Government spending on work-related child care: Some economic issues* (1988), p 10.

**Figure 6.4 Difficulties in finding child care, 2003**

Source: The Melbourne Institute of Applied Economic and Social Research, The University of Melbourne, *Families, incomes and jobs: A statistical report of the Household Income and Labour Dynamics Survey (HILDA) (2006)*, p 11. Household Estimates for special needs children for difficulty categories are not reliable.

- 6.43 For some parents, problems in accessing care mean that they may have to choose an imperfect option which creates stress for the family, although it allows parents to take on paid work. For other parents, the impossibility of accommodating work and family obligations within existing child care options means that they cannot work at all.

## Parents' working hours and working patterns

- 6.44 Parents who do shiftwork, work on weekends, work at night, or who regularly work overtime have immense difficulties in accessing child care.
- 6.45 The 2004 census of child care services produced by the Department of Families and Community Services reported that long day care centres opened for an average 10 hours and 48 minutes per day, generally between 8 am and 6 pm. Of 3,812 long day care services surveyed, only 21 opened on weekends, and of these eight opened on both Saturday and Sunday. There were only two centres operating for 24 hours a day.<sup>44</sup>

44 Department of Family and Community Services, *2004 Census of child care services* (2005), pp 10-11.

Occasional care tends to have shorter opening hours than long day care; an average of 8 hours and 20 minutes per day. Outside school hours care typically provides three hours of care per day.<sup>45</sup>

- 6.46 Family day care is more flexible, although its carers are more likely to lack child care qualifications.<sup>46</sup> The main use of family day care schemes occurred during the hours of 8 am and 6 pm, but seven per cent of children in family day care received care between the hours of 6 pm and 8 am.<sup>47</sup> While nothing precludes family day care providers from offering overnight or after hours care, this can in practice be difficult to find. A Sydney mother told the committee:

There are issues with family day care. Invariably they do not suit many working parents typically needing eight hour days. I spoke with someone from [the local council] family day care only yesterday and, unfortunately, there really are no spaces for children of women who require longer day care situations. Her words to me were, 'Look, if you were more flexible with hours, we'd obviously have a better chance of placing you'. I asked what the times were, and she said, 'Generally eight or eight-thirty to about four'. That does not suit my needs.<sup>48</sup>

- 6.47 For parents working business hours, their only care option is often long day care, and the standard 6 pm closing time of most centres can be difficult to accommodate within a business culture that expects them to remain at work if a meeting runs overtime, or if an urgent task materialises. The practice of charging fines by the minute for late pick-ups means that many parents are, in one mother's words, 'zooming across town' in peak hour traffic to make the closing time.<sup>49</sup> The Women Lawyers Association of New South Wales said that:

The opening and closing hours of child care centres are often inflexible and do not coincide with the sometimes long hours that lawyers work. Late fees are imposed for every hour that a lawyer is, for example, caught up with a client or in city traffic and delayed from picking up their children.<sup>50</sup>

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45 Department of Family and Community Services, *2004 Census of child care services* (2005), pp 10-11.

46 Department of Family and Community Services, *2004 Census of child care services* (2005), p 10.

47 Department of Family and Community Services, *2004 Census of child care services* (2005), p 10.

48 Watson K, transcript, 21 June 2006, p 8.

49 McNee R, sub 127, p 2.

50 Women Lawyers' Association of New South Wales, sub 99, p 3.

- 6.48 If parents working business hours have problems finding suitable care, then it is even more difficult for those working non-standard hours. A single mother from Coffs Harbour told the committee:

There are a lot of problems, especially with after school care. For instance, you may have a job that starts at seven o'clock in the morning and finishes at four o'clock in the afternoon, but there is no care before eight o'clock in the morning... When it comes to working and being offered a job to start at seven o'clock in the morning, I cannot take it because I do not even have the option to put my children into care. It makes it very hard.<sup>51</sup>

- 6.49 Casual or sporadic workers may not be able to use long day care because they do not always know in advance when or for how long they will be working. A 2001 survey cited by the National Council of Single Mothers and their Children found that 'child care usually had to be booked in advance, creating difficulties for women who worked casual hours and were unsure of their child care needs'.<sup>52</sup> The Australian Council of Trade Unions said that in a child care 'phone-in' they conducted in 2004, parents complained that child care centres were inflexible. 'Fees were charged on public holidays which is hard for casual workers who do not receive any pay for public holidays'.<sup>53</sup> Similarly, the YWCA reported that its clients often struggled to find flexible child care, which was 'essential for casual or temporary staff with irregular hours or for students whose class timetable changes from term to term'.<sup>54</sup>

- 6.50 Salary packaging provider McMillan Shakespeare observed that:

The greatest demand for child care is actually casual child care... [but] it does not exist. The home care proposition that you put is one that would overcome that. If you could call up an agency and say, 'Come in and look after my child for this day because I have a meeting, but my mother and father happen to be caravanning up in Cairns' – for example – 'or unavailable because they have doctors' appointments,' there are no conflicts. If we had a system that allowed that flexibility you talk about, Madam Chair, that would help overcome that problem as well. Casual care is in big demand. There is no-one in the market place that is providing any support for that market.<sup>55</sup>

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51 Griffin S, Uniting Care Burnside, transcript, 13 March 2006, p 19.

52 National Council of Single Mothers and their Children, sub 108, p 8.

53 Australian Council of Trade Unions, sub 104, p 16.

54 YWCA of Australia, sub 113, p 5.

55 Podesta A, transcript, 1 November 2006, p 10.



- 6.51 An example of a worker affected by such inflexibilities is that of a single father of four from Perth, Paul Richards, who gave evidence to the committee. Mr Richards was an electrical maintenance contractor who was offered a \$100,000 position in regional Western Australia. The job was on a fly-in, fly-out arrangement, however, with two weeks on and two off. Although he wanted to work, and his family needed the money, he was unable to take up the position. While he did, eventually, locate overnight care, the lack of government assistance with in-home care meant that he was unable to afford the up-front costs of the care.<sup>56</sup>
- 6.52 Another example is that of a mother of three, Jenny de Lacy, who wrote to the committee of her difficulties in finding care to match her irregular work as a contractor in education. These had in fact led her to quit her job and find alternative employment for the sake of her family arrangements:
- Recently we decided I would return to more regular work, as contracting work is hard on the family, and ad hoc child care almost impossible for us to find. We have no family support for child care, and working as a contractor is not predictable, so child care had to be permanent even if the work was not.<sup>57</sup>
- 6.53 In many cases, for parents working casual or irregular hours, it is only informal care provided by grandparents, relatives and family friends that enables them to earn an income. A professional mother told the committee that, 'Flexibility is not part of child care. If you are required to work additional hours, travel interstate or go to breakfast meetings, these can only occur with the support of other family members'.<sup>58</sup>
- 6.54 Such arrangements rely on goodwill, however, and as noted earlier, grandparents and other family members may be less and less able to provide such care in the future. A single mother of five wrote that while she worked doing night fill in supermarkets, one of her sons cared for the younger children overnight. This informal arrangement was about to be disrupted and there was no alternative child care available to her:

I will soon have to quit my part time employment (night fill in the supermarket) as my 16 year old son will be moving out to live with his father. This is mainly due to having better living conditions due to more money in the household and the fact that he finds the responsibility of looking after his siblings (on the

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56 Richards P, sub 170, p 1.

57 De Lacy J, p 172, p 1.

58 Waldock J, The Association of Professional Engineers, Scientists and Managers Australia, transcript, 3 August 2005, p 27.

nights I am working, if I need to go to appointments, studying or shopping), tedious and tiring. I will have no-one to look after the children.<sup>59</sup>

6.55 Amongst couple families there is evidence that some manage the dearth of out-of-hours child care by working alternate 'shifts' across day and night. This means that one parent is always at home with the children, but it can have negative consequences for parents' health and their own relationship, as they may seldom see each other except to 'hand over'. Mr John Hart, Chief Executive Officer of Restaurant and Catering Australia, told the committee that because 'after-hours places are as scarce as hens' teeth', these arrangements were quite common in his industry, where 56 per cent of business was transacted after 7 pm.<sup>60</sup>

6.56 The Working Women's Centre of South Australia said:

Women report that they take on night shifts thinking that child care will be easier to manage if their partners can look after the children at nights. They describe relationships where they rarely spend time together and worry about the impact of this on their children.<sup>61</sup>

## Waiting lists for child care places

6.57 The qualities of child care make it difficult for access to be nationally consistent. Child care supply is heavily localised, as there is a limit to the travelling times which parents can reasonably undertake on a daily basis.

6.58 In the long day care sector, which cares for the majority of children in formal care, some centres do have vacancies. As noted in chapter five, the Australian Government has claimed that there are up to 120,000 child care vacancies in Australia, depending on the day of the week.<sup>62</sup>

6.59 There are pockets of intense shortages in long day care, however. Earlier this year, the Melbourne bayside municipality of Port Phillip had 1,935 children on the waiting list for care.<sup>63</sup> In evidence the committee has heard of waiting lists of 18 months or more in some metropolitan areas, particularly inner metropolitan areas. The committee heard that some mothers put their names down on waiting lists virtually 'at conception' of

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59 Bentley S, sub 43, p 2.

60 Hart J, transcript, 3 February 2006, p 28.

61 Working Women's Centre of South Australia, sub 74, p 6.

62 Hon M Brough MP, Minister for Families, Community Services and Indigenous Affairs, 'Childcare places and the Childcare Access Hotline', media release, 27 September 2006.

63 Clausen L, 'Putting a price on our children', *Time*, 13 March 2006, p 43.

their children. There were many comments on the frustrations of finding child care:

The waiting lists for child care are enormous... When I found out I was pregnant I called my obstetrician, my private hospital and my child care provider before I even told my family, because the child care centre needs to know before anybody else does.<sup>64</sup>

It has taken our family over three years to access a reasonable level of long day-care positions... You will note from the attachment to my written submission a record of 50 registered child care centres and family day care providers that I have kept regarding the availability of positions last year.<sup>65</sup>

When our children were born, the key issue for my wife and I was the difficulty in accessing child care. It was a very stressful time, involving a huge number of phone calls and waiting lists.<sup>66</sup>

When I was returning to work after each baby, access to child care was a problem. We were on the waiting list for many child care centres and eventually were offered a place. I found having an impending date of return to work with no child care yet in place an extremely stressful situation.<sup>67</sup>

Our situation is not unique. We have heard of people who put their child's name on a waiting list only to be told that there are six A4 pages of names before them, or that the child may get a place by the time it is of school age, or simply not to bother putting a name down as there is no chance of getting a place.<sup>68</sup>

We were on about 12 different waiting lists for about 14 months. The only reason we got child care in the end was that I was diagnosed with postnatal depression and given a priority placement.<sup>69</sup>

## Child care affordability

6.60 Alongside issues of availability, affordability was an issue consistently raised in submissions. The 2006 Household Income and Labour Dynamics Survey found that 45 per cent of parents report medium or high

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64 Somerville J, transcript, 13 March 2006, p 27.

65 Watson K, transcript, 21 June 2006, p2.

66 Fulton P, transcript, 11 April 2006, p 24.

67 Name withheld, sub 95, p 1.

68 Hawker C and Kleiman A, sub 42, p 4.

69 Hawker C, transcript, 13 March 2006, p 31.

difficulties in finding affordable care.<sup>70</sup> The Taskforce on Care Costs found in their 2006 survey that 37 per cent of employees with caring responsibilities now feel that the cost of care is too high relative to their income, up from 31 per cent in 2004.<sup>71</sup>

6.61 High child care costs are not merely a perception. They are real. The Taskforce reported that since 2004, child care costs have seen annual increases of 12.4 per cent, whilst the annual average Consumer Price Index increases have been 2.5 per cent.<sup>72</sup>

6.62 Some parents who gave evidence to the committee suggested that in light of such fees, government assistance with child care was not generous and the current system was unfair. Some families were receiving Child Care Benefit of \$0.457 per hour when their annual child care costs could be almost \$20,000. One mother commented:

While it would be nice to receive some assistance in caring for our children while I return part time to the workforce, I recognise that I am in a well-paid profession and probably do not need the same level of assistance that many others do... I believe that child care assistance payments of some form should be made to people who are below a certain salary bracket. However I do believe that in addition all people who use child care so that they can return to the workforce should be able to claim their child care expenses as a tax rebate/deduction.

I appreciate that the government does give some non-means tested assistance to child care. Currently that is approximately \$3 per day. When the centre charges \$80 per day, the \$3 per day is laughable.<sup>73</sup>

6.63 Over most of the period of taking evidence, parents had not yet been able to claim the 30 per cent Child Care Tax Rebate, although it was positively anticipated.

6.64 This issue of government assistance with child care costs and the most appropriate mechanisms for that assistance will be discussed further in chapter seven.

70 Melbourne Institute of Applied Economic and Social Research, The University of Melbourne, *Families, incomes and jobs: A statistical report of the Household Income and Labour Dynamics Survey (HILDA)* (2006), p 11.

71 Taskforce on Care Costs, *Where to now? 2006 Final report* (2006), p 11.

72 Taskforce on Care Costs, *2006 Interim review: Where are we now?* (2006), p 7.

73 Somerville J, sub 61, p 3.

## Difficulties related to the age of children

- 6.65 Some parents' difficulties in accessing child care lie in finding age-appropriate care for children. Care for children aged two and under is a particular problem. The Benevolent Society stated:

There is a significant shortage of child care spaces for children under two years of age. Many centres find this age group hard to cater to and they are more expensive rooms to run due to the staffing ratios... Both of The Benevolent Society's child care centres run rooms for children from six weeks of age. Our waiting lists for care of under twos means that for a possibility of securing a place, women need to get on the waiting list while pregnant and may still have to wait at least 18 months before that chance of securing a place.<sup>74</sup>

- 6.66 At the other side of the scale, the care of teenagers has emerged as a hidden issue for many parents. Workforce Participation Minister Sharman Stone recently said that in a series of nationwide consultations, care for teenagers had emerged as one of the biggest concerns for parents.<sup>75</sup> The Minister acknowledged that this concern was affecting parents' decisions about taking on paid work. A single mother of teenagers who had turned down a job offer told *The Australian*:

Thirteen is not a good age to be alone, it is vulnerable time for kids. I want to work, but... I was worried about the non-supervision hours.<sup>76</sup>

- 6.67 A 2006 study of women's labour market transitions, conducted by the Social Policy Research Centre at the University of New South Wales, found that the care of teenage children was a source of concern for the mothers interviewed. 'During the teenage years the conflict between "labour force participation" and "parental responsibility" discourses come most starkly into conflict'.<sup>77</sup>
- 6.68 The study found that government policy reflected an assumption that children were old enough to look after themselves after they started high school, but that on the other hand, parents were still held responsible for

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74 Benevolent Society, sub 80, p 4.

75 Karvelas P, 'Teens new childcare hole', *The Australian*, 19 April 2006, p 2.

76 Karvelas P, 'Teens new childcare hole', *The Australian*, 19 April 2006, p 2.

77 Smyth C, Rawsthorne M and Siminski P, Social Policy Research Centre, University of New South Wales, *Women's lifework: Labour market transition experiences of women, final report* (2006), SPRC report 7/06, p 55.

anti-social and criminal behaviours by teenagers. Sole parents had the greatest concern about unsupervised teenagers.<sup>78</sup>

- 6.69 A single mother from Coffs Harbour told the committee that the gap in provision for young people in this age group that made it difficult for parents to work and be assured of their security:

The other side of [child care problems] is with children who go into high school. They are 11 or 12 when they start year 7. Once they get out of year six and hit high school, they are no longer eligible for outside of school hours or vacation care. Under the Department of Community Services, a child is not able to be left at home until the age of 14. So it is very contradictory...<sup>79</sup>

- 6.70 Many teenagers, of course, are antagonistic to the idea of formal care, particularly if they will be joining a group of younger children, and most child care providers do not cater for children over the age of 12. In 2004, less than 0.05 per cent of all children in outside school hours care were aged 13. There were no children aged 14 or over.<sup>80</sup>

## Preferences for child care

- 6.71 In the real world, parents' actual choices do not purely reflect their preferences; they are circumscribed by the services that are available in their local area and the cost of those services.
- 6.72 Committee members, after hearing of difficulties such as those outlined above, often asked witnesses to indulge in a 'blue sky' perspective for a moment and describe what sort of child care they would have in a perfect world. Unsurprisingly, the diversity of Australian families is represented in a range of preferences for care types. There are probably as many 'ideal' child care arrangements as there are families.

## Children's development

- 6.73 Parents consider their children's social and cognitive development when making child care choices. Many parents who gave evidence to the

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78 Smyth C, Rawsthorne M and Siminski P, Social Policy Research Centre, University of New South Wales, *Women's lifework: Labour market transition experiences of women - Final report* (2006), SPRC report 7/06, p 55.

79 Griffin S, Uniting Care Burnside, transcript, 13 March 2006, p 19.

80 Department of Family and Community Services, *2004 Census of child care services* (2005), p 126.

committee sent their children to day care for the opportunity to socialise with other children. A Sydney mother working part time said:

We chose a centre rather than an individual nanny as such...  
[because] I personally think the social interaction for children is very important.<sup>81</sup>

- 6.74 The witness and her husband were also attracted by the structured learning opportunities on offer in formal group care:

At kindy [my daughter] gets exposed to Japanese and health classes, they have language and music classes. I could not do all that at home and I think it would be a rare individual nanny who would offer all of that to a child.<sup>82</sup>

- 6.75 On the other hand, some parents choose in-home carers because of the intensive one-on-one language development opportunities afforded to children who get a carer's constant attention. A manager of a nanny agency in Sydney, Marina McHutchison, said:

Most of the good professional nannies I have met all talk underwater. It is constant. It promotes language skills with the children because they are constantly talking.<sup>83</sup>

- 6.76 Children's developmental needs vary not only from child to child but between children of different ages. There was a preference to have very young children cared for in an in-home situation, through a nanny, family day carer, or by a family member or friend in their own home where possible. This is reflected in the higher numbers of nought to two year olds in family day care and in-home care than in any other form of care, even without including those infants and toddlers being cared for within the in-home care cash economy.<sup>84</sup>

- 6.77 As children reach the ages of three and four this preference turns to group care situations where they can begin to make friends. Given the trend towards smaller family sizes, many children do not have as many siblings as they may once have had, and group care gives them a chance to interact with others in preparation for primary school.

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81 Somerville J, transcript 13 March 2006, p 38.

82 Somerville J, transcript 13 March 2006, p 39.

83 McHutchison M, The Australian Consortium of Nannies, transcript, 22 September 2005, p 57.

84 Department of Family and Community Services, *2004 Census of child care services* (2005), p 13.

## Children's care needs

- 6.78 For parents of children with particular health or care needs, formal group care, such as long day care or outside school hours care, may not be an option. For example, the committee heard that parents choose to use in-home carers if their children are vulnerable to multiple coughs and colds after being exposed to a large number of children in a day care centre.<sup>85</sup>
- 6.79 A Sydney mother who gave evidence to the committee told how her search for child care places had been made especially difficult by the fact that one of her sons suffered from anaphylaxis, a severe food allergy. Many of the long day care centres she contacted in her local area could not provide a peanut-free environment.<sup>86</sup>
- 6.80 The committee also heard evidence from parents of children who had Attention Deficit Hyperactivity Disorder (ADHD), autism, behavioural problems and moderate to profound disabilities.<sup>87</sup> Where these children exhibit challenging behaviour or have complex care needs, a long day care or after school care program may not be a solution for the child, the provider, or the parent, who may be frequently called back from work to attend to problems. In many cases care providers will simply not accept children with behavioural problems or disabilities.
- 6.81 A Brisbane mother told the committee that the lack of adequate child care for her three year old autistic son was the reason why she was not considering returning to the workforce, noting, 'The current day care system does not meet the needs of children with ASD [autism]'.<sup>88</sup> Respite care and specialist care programs exist, although these can be difficult to find and access. Care of children with disabilities is a problem and will be further considered in chapter eight.

## Reliability and security

- 6.82 For some parents, the reliability of their care arrangements was also a primary concern. For busy parents, the threat of being thrown into panic over the sudden collapse of child care arrangements was too much. Agencies that provide in-home carers to families may often be able to provide a replacement carer at short notice if a carer is sick or on leave. Individual in-home carers or family day care providers may not, however,

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85 Gibietis P, Nanny Sharing Connections, transcript, 22 September 2005, p 9.

86 Watson K, transcript, 21 June 2006, p 6.

87 See, for example, Griffin S, transcript, 13 March 2006, p 20; Richards P, transcript, 30 June 2006, p 17; Stapledon A, sub 179, p 1; Engwirda F, sub 221, p 2.

88 Engwirda F, sub 221, p 2.



be able to offer this back-up, and for this reason some parents prefer the security of an established long day care centre or outside school hours care.

As to child care and the choices you make, it is an extremely complex decision. I am speaking for myself here. I was not particularly interested in the at-home child care solution. I saw that there were risks involved in it to do with the reliability of it... The advantage of a crèche system or an out-of-hours school program is that, because it is run for a number of families, you know that there will be staff there. If your individual at-home carer is unwell or is called away because of their own family requirements, you are left trying to juggle it.<sup>89</sup>

We looked at child care and nannying. We thought that a child care centre would better suit our needs because there is the support of a centre and a lot of other carers. I didn't want to be in the situation where I am reliant on one person only to look after my children, and there is some benefit – from my perspective – when there are other people around.<sup>90</sup>

- 6.83 Some parents, such as the Sydney mother quoted above, also feel that there is increased safety in the numbers of staff working at a child care centre, while others prefer to have control by selecting their children's carer and monitoring the situation themselves. Clearly, choice is needed.

## In-home care sector

- 6.84 One kind of care which can accommodate the varied working patterns and care requirements of many families is in-home care, in which a carer comes to care for children in their own home. Government assistance for child care is heavily focussed on group care settings outside of the child's home, as in long day care, preschool, outside school hours care, vacation care and occasional care. Family day care, which is funded through registered and approved models, involves a small group of children being cared for in the home of the carer.
- 6.85 The Australian Government's recently established In-Home Care program is the only form of care in the child's home that is funded at approved care

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89 Waldock J, Association of Professional Engineers, Scientists and Managers Australia, transcript, 3 August 2005, p 31.

90 Burchsmith E, transcript, 13 March 2006, p 30.

rates of Child Care Benefit, and the only one that is eligible for the Child Care Tax Rebate. Access to the program is heavily restricted, however. By and large, the in-home care industry in Australia is happening in the black economy.

## **Australian Government's In-Home Care program**

- 6.86 The Australian Government established an in-home care program in 2001. Under this model, care is provided in the home of the child by an approved carer, and parents can claim Child Care Benefit at the approved care rate as well as the Child Care Tax Rebate. The program supports a highly flexible form of care: the 2004 census of child care services reported that 18 per cent of children in in-home care were being cared for between the hours of 8 pm and 6 am, a higher proportion than any other type of care.<sup>91</sup>
- 6.87 Ms Susan Rogan, operator of a nanny agency and an approved in-home care provider, offered the following as advantages of in-home care:
- increased flexibility results in decreased pressure on families;
  - child care can be accessed when children are unwell;
  - one-to-one care is less stressful for children; and
  - care is provided in a familiar environment by a familiar carer.<sup>92</sup>
- 6.88 The program is limited, however, to families whose child care needs cannot be met by an existing service. Families that may be eligible for in-home care include:
- families where the parent/s or child has an illness or disability;
  - families in remote or rural areas;
  - parents working shift work or non-standard hours;
  - parents who have had a multiple birth (three or more), and/or have three or more children under school age; and
  - breastfeeding mothers working from home.<sup>93</sup>

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91 Department of Family and Community Services, *2004 Census of child care services* (2005), p 10.

92 Susan Rogan Family Care, sub 159, p 2.

93 Department of Families, Community Services and Indigenous Affairs website, viewed on 5 October 2006 at [http://www.facsia.gov.au/internet/facsinternet.nsf/childcare/families-in\\_home\\_care.htm](http://www.facsia.gov.au/internet/facsinternet.nsf/childcare/families-in_home_care.htm).

- 6.89 Take-up of in-home care places has been steady, although the program remains modest in size. The 2004 census of child care services reported that 68 in-home schemes were in operation, providing carers to 3,240 children, up from 45 schemes and 1,500 children in 2002.<sup>94</sup>
- 6.90 In-home care places are capped by the Australian Government pending finalisation of a review into the program. Since its commencement in January 2001, 7,700 in-home care places have been allocated. In the 2005-06 Budget a further 1,000 places were allocated over four years, to better support those affected by Welfare to Work.<sup>95</sup> It appears unlikely that 7,700 places will enable all families in the situations above to access in-home care.<sup>96</sup> In any case, evidence taken by the committee suggests that most families are not aware that the program exists.<sup>97</sup>
- 6.91 Ms Kay Ganley, Chief Executive Officer of the Charlton Brown Group, made some positive comments about the program. Charlton Brown are a child care training organisation, nanny agency and an approved provider of in-home care services in four states:

We would like to congratulate the federal government on this initiative of in-home care provision. Prior to this, there was no subsidy available to families who could not access centre based or family day care because they lived in remote or rural areas, because they were shift workers or because they had an ill child. We have demand from people in very unfortunate circumstances, such as where children have cancer et cetera and they cannot access care. There are also children or young people with disabilities who are in care or in integrated situations but for after school hours they need a break and need individual care.<sup>98</sup>

## **In-home (nanny) care industry**

- 6.92 The committee took evidence on an extensive in-home care industry in Australia, which is only captured in small part by the Australian Government's In-Home Care program. A 'nanny day' roundtable on 22 September 2005 brought together parents, nannies, approved in-home

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94 Department of Family and Community Services, *2004 Census of child care services* (2005), pp 7, 9.

95 Department of Families, Community Services and Indigenous Affairs, correspondence, 23 November 2006.

96 Australian Bureau of Statistics, *Australian demographic statistics* (2006), Cat No 3101.0, p 18.

97 Nannies day roundtable, transcript, 22 September 2005, p 26.

98 Ganley K, transcript, 22 July 2005, p 37.

care providers, and nanny agency directors to discuss the state of the industry and how to bring it forward.

6.93 In considering how this sector can be given recognition and reformed so as to be more widely available to families who need in-home support, the committee has found it more useful to refer to 'in-home carers'.

6.94 The work of nannies is very similar to the work done by approved in-home care providers under the Australian Government program for families in special circumstances. In fact, most approved in-home care providers are nanny agencies. Outside of the auspices of government-funded in-home care places, however, parents who use in-home carers receive no or minimal assistance. If their carer registers with the Family Assistance Office, they receive Child Care Benefit at a flat minimum rate, currently \$0.497 per hour per child.<sup>99</sup> Nannies may be unwilling to register if they are paid in cash, as the Family Assistance Office will therefore have evidence of an income-earning relationship. From the parents' point of view, a maximum of \$24.85 per week may not be sufficient incentive for them to push their carer to register, given that the assistance also involves substantial paperwork.

6.95 There is a common perception that in-home carers are only employed by wealthy families, but the committee has not found this to be the case. Those who participated in the roundtable told the committee:

In 2005, employing a nanny is no longer for the privileged and wealthy of Australia to take leisurely lunches and play tennis.<sup>100</sup>

I have worked for different people, from those on the rich 200 list right down to policemen and ambulance people.<sup>101</sup>

6.96 For some families, particularly for those with three or more children, it can actually be more cost-effective to hire an in-home carer than to put all their children into long day care. A Sydney mother told the committee:

I am the mother of three children of preschool age. This year I was ecstatic to secure a part time job in a fantastic company – it is a great feeling to be using my skills and contributing to society (and finally being paid for it). With such young children my only child care option was to hire a nanny – this was actually cheaper than putting all three children into long day care. You seem to fall for

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99 Centrelink website, viewed on 11 May 2006 at [http://www.centrelink.gov.au/internet/internet.nsf/payments/qual\\_how\\_ccb.htm](http://www.centrelink.gov.au/internet/internet.nsf/payments/qual_how_ccb.htm).

100 Elite Nanny Service, supplementary sub 157, p 2.

101 Slattery L, transcript, 22 September 2005, p 45.

the general view that if you can afford a nanny you must be really well off. This is absolutely not the case with many families I know.<sup>102</sup>

- 6.97 Other parents hire in-home carers simply because they cannot access long day care; they need to return to work and cannot wait the 18 to 24 months it may take to get a place. A nanny agency operator reported that, 'This agency receives calls daily from distressed parents unable to access approved child care places seeking information about nanny care'.<sup>103</sup> Another nanny agency operator, who was also a mother, said that:

The government is taking away choice from families who are considering their child care options. Employing a nanny may be the only option as child care places are unavailable... I have employed a nanny since my child was six months old given that no suitable place in child care was available.<sup>104</sup>

- 6.98 Other workers employ in-home carers because their job requirements mean they can't use long day care or after school care. For all the reasons outlined in the sections above, shift workers, weekend workers, and those who do regular overtime need child care outside of standard centre opening hours. Nannies and agency directors reported that there was a lot of interest in in-home care from flight attendants, police officers and emergency services workers.<sup>105</sup> A Sydney businesswoman told the committee the reasons why she employed an in-home carer:

As a business woman running a small business I do not have the luxury of a 9 to 5 position and as such have few alternatives in the way of care for my child. Even if a suitable child care place was available in relatively close proximity to our home or my work, the hours that I work in order to maintain my business and the people I employ do not fit into the narrow constraints imposed by the child care centres.<sup>106</sup>

## **Black market in in-home care**

- 6.99 A cash economy in child care has been active in this country for many years, although there are varied estimates on its size. The Australian Taxation Office suggests that the nanny industry in Australia could be

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102 McDonald E, sub 154, p 1.

103 Susan Rogan Family Care, sub 159, p 2.

104 Elite Nanny Service, sub 147, p 2.

105 Nanny day roundtable, transcript, 22 September 2005, pp 5-6, 13, 43, 46.

106 Elite Nanny Service, supplementary sub 157, p 2.

worth about \$400 million to \$500 million a year, but they have no evidence of the compliance rate in the industry.<sup>107</sup> This does not include cash paid to babysitters, housekeepers, cleaners and unregistered carers. Furthermore, it only includes the cost of goods and services themselves, and not the income tax that the government would otherwise be collecting.

- 6.100 In 1998, the Australian Taxation Office's Cash Economy Task Force found that personal and household services (for example, child care, appliance repairs and installations, gardening, car repairs etc) appeared to be amongst the fastest growing sectors in the cash economy.<sup>108</sup>
- 6.101 It is not known what size this sector has grown to now, but there is some statistical data suggestive of the value of the black economy in child care. The Australian Bureau of Statistics found in 2005 that six per cent of children aged 0-12, or over 200,000 children, were being cared for in an informal and unregulated arrangement by a person unrelated to the family. This would include friends, neighbours and babysitters, but the committee would also expect it to include the nanny industry.<sup>109</sup>
- 6.102 In their 2006 survey of 1,000 Australians with caring responsibilities, the Taskforce on Care Costs found that 17 to 26 per cent of workers who pay for their caring arrangements do so on an informal basis; that is, by paying cash to family members, friends or unregistered carers such as nannies.<sup>110</sup> If the transactions currently generated by the formal child care industry in Australia represent only 75 or 80 per cent of the market, the remainder is significant. Given the greater likelihood that cash will be changing hands in an informal business relationship rather than between family members, the size and value of the black economy in child care may in fact be in the billions of dollars.
- 6.103 Parents and nannies testified to the committee that the black market is 'alive and kicking':<sup>111</sup>

If I put an ad in the paper [for my agency] the phone does not ring as much as if I just put my mobile number. When you answer the phone, people say, 'Are you an agency?' You say, 'Yes', and they bang down the phone. If you can get them to talk they say, 'I want

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107 Konza M, transcript, 21 June 2006, p 12.

108 Australian Taxation Office, *Improving tax compliance in the cash economy* (1998), p 16.

109 Australian Bureau of Statistics, *Child care, Australia, June 2005* (2006), Cat No 4402.0, p 3.

110 Taskforce on Care Costs, *Where to now? 2006 Final report* (2006), p 33.

111 Watson K, transcript, 21 June 2006, p 4.

cash'. I can't tell you how many people say that to me on the phone.<sup>112</sup>

The black market is huge and we need to hit that on the head and stop it as much as we can.<sup>113</sup>

The 'black market' that is spoken of has grown due to a desperate need to obtain any child care.<sup>114</sup>

6.104 The committee heard of registered nannies who had an agreement with their family that only part of their income would be declared, and the rest would be paid in cash, pushing up their hourly rate.<sup>115</sup> The committee was also told of arrangements where working mothers were paying cash to non-working mothers to mind their children. These mothers were not only earning a cash income, but claiming family tax benefits for staying at home. If they put their own children in care, they were not only taking up child care places ahead of working mothers but claiming Child Care Benefit as well.<sup>116</sup>

6.105 Where there is no incentive for registering an in-home carer, where the cost of child care is a financial stress, and where parents can avoid paying superannuation and sick leave, the black economy will thrive. Many will continue to negotiate cash payments to their carer. The Women Lawyers Association of New South Wales told the committee that based on the results of a recent survey:

Many colleagues have found the cost of full time nannies prohibitive and have been forced to make arrangements to employ friends or family members on a cash basis as an alternative. In my observation, the prohibitive cost and unavailability of child care appears to be sparking a flourishing tax-free industry.<sup>117</sup>

6.106 Parents who made submissions to the inquiry also identified a link between low government assistance for in-home care (a maximum of \$24.85 per week for registered nannies) and the black economy in child care:

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112 Clark C, My Little Friend Nanny Agency, transcript, 22 September 2006, p 82.

113 Kerr C, Charlton Brown Group, transcript, 22 September 2005, p 7.

114 Name withheld, sub 193, p 2.

115 Douglas D, Mothercraft and Nannies Pty Ltd, transcript, 22 September 2005, p 15.

116 Name withheld, sub 193, p 2.

117 Carr B, transcript 13 March 2006, p 56.

By offering so little support to families who use nannies, many families just pay their nannies cash, so it costs them less. That just encourages a black market.<sup>118</sup>

- 6.107 As a result, many in-home carers in this country are being employed on the black market. This is not the best outcome for parents, who often get a less committed carer. Parents are also, of course, committing an illegal act by employing someone on a cash basis. The black market is also not the best outcome for the carers. As heard by the committee at the nanny day roundtable, the lack of a legitimate employment record means that nannies have problems getting car loans and mortgages. Also of concern was the fact that carers working for cash accumulate no superannuation, and many are worried about how to provide for their future.<sup>119</sup>

### **Encouraging a professional in-home care sector**

- 6.108 Long day care is an established model of child care provision and remains the preference of many parents, particularly those who have secured a place in a centre which their children enjoy. As the committee has seen, however, the personal circumstances of many families are not accommodated by the child care industry. Family day care offers a more flexible alternative to centre-based care, but it is still not delivering the flexibility that families need. Places in either sort of care are in extremely high demand in some areas and parents may have to wait 18 months for a place, which even then may not be for the hours or days requested.

- 6.109 Susan Rogan, operator of a nanny agency and an approved in-home care provider, told the committee that:

It appears that care 'out of home' is the preferred option of funding and training bodies, although many families would prefer child care at home.<sup>120</sup>

- 6.110 The committee agrees with this statement. While it supports the continuation of the current long day care model, it also believes that a greater range of child care options are needed to service workers in a flexible and responsive domestic economy. Those who do not wish to use long day care, or the many families who simply cannot, should not be penalised for their choice by receiving lesser government assistance.

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118 MacDonald E, sub 154, p 1.

119 Nanny day roundtable, transcript, 22 September 2005, pp 3-13.

120 Susan Rogan Family Care, sub 159, p 2.



- 6.111 In Australia, in-home care seems to suffer from a stigma that is not found in other countries where nannies, au pairs and other forms of in-home care are an accepted part of the child care landscape. In Italy, 27 per cent of children aged 0-3 receive in-home care.<sup>121</sup> In France, parents of children aged 0-3 receive government assistance for carers (*garde à domicile*) who will come into the home and care for infants and toddlers.<sup>122</sup> The Netherlands also has an in-home care program.<sup>123</sup>
- 6.112 The United Kingdom set up a Home Childcarers Scheme in April 2003 'to help widen the availability of tax credit support by ensuring that parents can access approved forms of child care to use within their own homes'.<sup>124</sup> Nannies, or 'home childminders', must be registered and must have completed induction-level training at a minimum. They must also have first aid qualifications and have passed a police record check. The program aims to raise the standard of home-based care and allows parents employing a registered carer to access the child care element of the Working Tax Credit and other forms of government child care assistance where eligible.<sup>125</sup>
- 6.113 The United Kingdom system also incorporates:
- mothers' helps, who work alongside the mother in the home and assist with child care and housework;
  - maternity nurses, who are live-in nurses specially trained to take care of new babies for up to three months after the birth;
  - childminders, who are similar to our family day carers; and
  - au pairs.<sup>126</sup>
- 6.114 The committee received a number of comments from parents who were puzzled and unhappy that the Australian government did not offer similar assistance, except within the very limited In-Home Care program:

121 OECD, *Starting strong II: Early childhood education and care* (2006), p 363.

122 OECD, *Starting strong II: Early childhood education and care* (2006), pp 325-27.

123 OECD, *Starting strong II: Early childhood education and care* (2006), p 386.

124 Department for Education and Skills, and Department for Work and Pensions (United Kingdom), Sure Start website, viewed on 6 November 2006 at <http://www.surestart.gov.uk/aboutsurestart/parents/childcareapprovalscheme/>.

125 Department for Education and Skills, and Department for Work and Pensions (United Kingdom), SureStart website, viewed on 6 November 2006 at <http://www.surestart.gov.uk/aboutsurestart/parents/childcareapprovalscheme/>.

126 Department for Education and Skills, and Department for Work and Pensions (United Kingdom), SureStart website, viewed on 6 November 2006 at <http://www.surestart.gov.uk/aboutsurestart/parents/needananny/whatisananny/>.

I don't see why families that use nannies should not be able to benefit from all the rebates that are offered to other forms of child care. The amount we receive back under the 'registered carer' category is pathetic.<sup>127</sup>

I have had to cancel my arrangement with the nanny agency as it is ludicrous to work and give it all away in tax and child care costs. Why aren't the subsidies for in-home care as good as the child care centres?<sup>128</sup>

- 6.115 In-home care subsidies have been the subject of political debate in Australia for several years now. While the Government has repeatedly rejected calls to increase assistance for in-home care, the Prime Minister himself has expressed sympathy for supporting choices more equally. As reported in *The Australian* in 2005:

Mr Howard has previously resisted subsidising nanny care, arguing nannies were mostly employed by the rich. But yesterday he acknowledged the growth in the use of nannies by working parents, saying, 'I think the proposition that if it's good enough to pay somebody X dollars a week to defray the cost of formal child care, then why isn't it good enough to pay the same amount of money to another couple in a similar situation where the care occurs at home? I think there is some argument for that'.<sup>129</sup>

- 6.116 The development of a professional and accessible in-home care sector would not only benefit parents, but could also benefit the child care industry as a whole, which is struggling to meet demand in some areas. A recent OECD paper on women's workforce participation noted that home-based child care arrangements could be seen to increase the responsiveness of child care supply because they had low start-up and maintenance capital arrangements.<sup>130</sup> Extending in-home care assistance to families with children in all circumstances may therefore solve some of the problems with long day care waiting lists, particularly for children aged 0-2, for whom parents may prefer a home-based care environment in any case.<sup>131</sup>

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127 McDonald E, sub 154, p 1.

128 De Lacy J, sub 172, p 1.

129 Overington C and Karvelas P, 'Howard reversal on nanny rebate', *The Australian*, 22 October 2005, p 1.

130 Jaumotte F, 'Labour force participation of women: Empirical evidence on the role of policy and other determinants in OECD countries' (2003), *OECD Economic Studies*, no 37, p 92.

131 Ganley K, Charlton Brown Group, transcript, 22 July 2005, p 38.

- 6.117 Kathy Clark, of My Little Friend Nanny Agency, said that many parents chose to employ a nanny because in-home care made such a dramatic difference to their ability to balance work and family. The extra support and not having to coordinate two trips to a child care centre every day had a positive influence on their relationships with their children and their spouse:

A lot of my clients say to me that, if they have got to get to work by eight o'clock, they have to get up, get the babies dressed, pack their bags, get them in the car, drive to the child care centre, put the children in the child care centre, unpack the children's bags, get the children settled, then get back in the car and drive to work.

Then, if they are in the middle of a meeting they have to say, 'I've got to go. It's 10 to six. I've got to be at the child care centre.'

However, if you have a nanny and you are in the middle of an important meeting you just SMS the nanny and say, 'I'm running half an hour late.' When the mother walks in the door at the end of the day, the children are bathed and fed, the house is relatively tidy and the washing has been done. Mum walks in, she sits down and she spends quality time with her children... has a conversation with her husband – and then tries to be the mother, the lover and everything else.

But that is the difference for a lot of my clients. They say to me, 'Otherwise, I drive in traffic and pick my kids up at six o'clock. They are screaming tired; they are dirty. I've got nothing for dinner. I've got to go to the shop and pick something up and then come home. By the time I've fed the kids it's 7.30 or eight o'clock. I've got to bath the kids and put them to bed. By that stage I'm exhausted and I start screaming at my husband. My life is a tragedy!' That is my life when I do not have a nanny. I can tell you: that is me.<sup>132</sup>

- 6.118 Kay Ganley, of nanny agency and training organisation Charlton Brown, told the committee that a professional in-home care sector would be complementary to, and not competitive with, the choices that families currently have:

One of the arguments that we would have is that families require different care at different times...I will give you an example: we have a family where the mum is a nurse and she has four children, including one set of twins, under school age. You could imagine

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132 Clark K, transcript, 22 September 2005, p 46.

how difficult it is for her to try to get the four children prepared, into the car and into child care, and then get herself off to work and then back to pick them all up and put them in the car.

Whereas, thinking of work-life family balance, having a carer looking after those children at home allows her to go to work without being worried about time constraints. The children are well cared for. As the children grow older and she would like them to go to child care or to family day care, there should be a transition. It should not be one against the other; it should not be competitive within the services. The services should be cooperative and provide the care that the family needs.<sup>133</sup>

- 6.119 The committee considers that a system of nanny registration is required, affording in-home care the same recognition that other forms of child care receive, and linking registration to more generous assistance for parents. This could potentially be achieved through an expansion of the existing In-Home Care program.
- 6.120 Subject to further industry consultation, the committee proposes that such a system be based on the following criteria:
- a minimum Certificate II qualification in child care, or an equivalent recognition of prior learning;
  - a current working with children police record check; and
  - a current first aid certification.
- 6.121 Where in-home carers are employed by an agency, taxation arrangements would take place through the agency, and parents would pay their fees to the agency. Where parents employ in-home carers directly, the carer would need to provide a tax file number, and parents would withhold and remit to the Australian Taxation Office a small withholding tax.
- 6.122 At the nanny day roundtable held by the committee, nannies, parents and agency operators were positive about such a registration system linked to government assistance for parents. It would not only provide cost relief to families but provide them with a real incentive to use only registered in-home carers who were legitimately employed with superannuation and sick pay entitlements. The in-home care industry would have more legitimacy, and by providing nannies with a more sustainable career path, it would have a better chance of attracting and retaining workers to the profession. Professional in-home carers, as recognised by government,

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133 Ganley K, Charlton Brown Group, transcript, 22 July 2005, p 38.

- would receive better and safer working conditions through payment of superannuation and workers compensation entitlements.
- 6.123 While opinions differed on what the minimum qualification requirements should be and whether additional duty of care conditions should be included, there was broad acceptance that if in-home carers were to gain from increased professionalism there was also a responsibility on the part of the industry to achieve and maintain a standard.
- 6.124 As the committee has heard, there are many experienced and wonderful in-home carers currently working with no qualifications, and there needs to be recognition of prior learning to take account of this. Transitional arrangements would be appropriate, which would allow in-home carers to register provided they were in the process of gaining a minimum qualification.
- 6.125 Nannies and training providers would also need to collaborate on the development of an appropriate course. Current Certificate courses in Children's Services cater to workers going into centre-based care, and feedback from the nanny industry is that they do not provide adequate training for workers going into a home environment.
- 6.126 Charlton Brown in Brisbane has developed a specialist in-home care qualification; the committee understands that they are the only organisation in Australia to do so.<sup>134</sup> The Certificate II in Community Services (Nanny Award) is tailored to training in-home carers, and includes 15 hours per week of experience in a family's home with a baby and a toddler. It also includes first aid, self-defence, defensive driving, lifesaving, emergency procedures and food preparation. Additionally, New Zealand has a National Nanny Certificate which could act as a model.
- 6.127 A minimum in-home care qualification would need, in any case, to be offered via flexible delivery, with the option of part-time or online study, so that carers do not have to stop working and give up their income in order to meet the new requirements.
- 6.128 The nannies who gave evidence to the committee felt that being part of a professional in-home care sector, recognised by government as a legitimate and vital part of child care services, would benefit their industry. It was felt that linking registration to tax relief for parents would increase the professionalism of interaction between nannies and parents:

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134 Ganley K, telephone conversation, 2 November 2006.

If you know you can get tax relief for employing a nanny... then you are also going to find out what your obligations are and how to meet those obligations. In a long term situation it is going to improve the status of nannies as being regarded as professionals and treated correctly.<sup>135</sup>

I think if nannies became tax deductible as employees, the standard and quality of girl would improve.<sup>136</sup>

- 6.129 Clearly too, such arrangements would dramatically reduce the incentives for employing in-home carers on the black market. Nanny agency operator Marina McHutchison gave evidence referring to the Child Care Cash Rebate (which preceded the Child Care Benefit) which was not means-tested and was paid for in-home care:

When I spoke to the Cash Economy Task Force about seven years ago, I asked if there was an increase of nannies on the books. They said that they were surprised that there was a dramatic increase of nannies in the taxation bookwork. What it did for our industry was that it made the parents sit up and take notice of the nannies. Instead of being paid cash, suddenly the nannies were on the books, which meant that they were getting holiday pay, sick leave and superannuation. So there was recognition there. Then, when means testing was brought in suddenly all the payment went back under the table. So there is proven history that if parents are given some sort of subsidy then they do come onto the books.<sup>137</sup>

## Recommendation 11

- 6.130 **In-home (nanny) care be categorised as approved care, and thus attract payments and tax concessions extended to users of approved care, where providers are registered with the Family Assistance Office, and:**
- **have or are at an advanced stage of attaining a minimum Certificate II qualification in child care, or an equivalent recognition of prior learning; and**
  - **have a current 'working with children' police record check; and**
  - **have a current first aid certification.**

135 Scrimizzi G, transcript, 22 September 2005, p 19.

136 Clark C, transcript, 22 September 2005, p 4.

137 McHutchison M, The Australian Consortium of Nannies, transcript, 22 September 2005, p 16.

## Au pairs

- 6.131 Au pairs are working holidaymakers between 18 and 26 years who receive board and an allowance in return for child care and supporting family activities. Au pairs currently receive between \$250 and \$300 per week, in addition to accommodation and board, for up to 45 hours per week of child care.<sup>138</sup> There are a number of specialist placement agencies in Australia who make the connection between parents and au pairs for a placement fee. Many nanny agencies will also have au pairs on their books. Suzanne Adelman, of nanny agency Mum's Best Friend, said that, 'Au pairs is an industry in Sydney which is certainly booming'.<sup>139</sup>
- 6.132 Most au pairs in Australia enter the country on a working holiday visa which permits them a 12 month stay but limits work with each employer to three months. This is inappropriate for child care workers for obvious reasons: families put a lot of time and effort into selecting an au pair, and it may take some time for a carer to get to know the family's routine and specific requirements.<sup>140</sup> The current system encourages illegal activity, as au pairs are likely to stay on with a family on a cash basis.
- 6.133 When an arrangement does work, however, it can deliver the benefits of in-home care to a family, together with an element of cultural exchange for both children and au pair. A small businesswoman from Sydney told the committee:
- A live-in au pair makes life easier and makes the family flow better. When I got home from work with an au pair, dinner was starting to be prepared or they could go shopping during the day with the baby, or have the washing on the line. The daily things that a stay-at-home mum would do the au pair does for you. I did not feel as stressed, I guess you could say, when I had an au pair. I was stressed financially, but I was not as stressed physically and emotionally.<sup>141</sup>
- The in-home care support was so important to this mother's life and her ability to continue to manage a retail business that she refinanced her mortgage three times in order to pay for it.<sup>142</sup>
- 6.134 Unlike many other countries, such as Germany, Switzerland, Belgium, the USA and Canada, Australia's au pair industry is unregulated. Participants

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138 Storm D, sub 167, p 1.

139 Adelman S, transcript, 22 September 2005, p 5.

140 Adelman S, transcript, 22 September 2005, p 5.

141 Romer J, transcript, 18 October 2006, pp 9-10.

142 Romer J, transcript, 18 October 2006, p 11.

at the nanny day roundtable felt that this leads to undesirable outcomes for some working travellers who are usually young, unfamiliar with Australian employment standards and may not have resources to manage a compromising situation:

I feel that having no guidelines within that particular market of child care leads to a lot working travellers and students here in Australia being taken advantage of and, unfortunately, leads to bad feeling. That is no good for industry, no good for child care, and no good generally. I would like to see that industry become more regulated.<sup>143</sup>

Overseas, in London and in America, there are regulated au pair industries and I believe that Australia should look into that.<sup>144</sup>

6.135 In the USA there has been an au pair program since 1986. Au pairs are admitted under a special category of visa for a placement of 12 to 24 months with a family. Applicants must:

- be between 18 and 26 years old;
- have 200 hours of child care or babysitting experience;
- have completed high school;
- have a drivers licence,
- have a clean criminal record;
- and be interviewed in person for a mature and appropriate attitude.<sup>145</sup>

Host families are also interviewed personally and must sign a contract detailing the family schedule, care requirements, pay and holidays as under regulations.

6.136 Another model for consideration could be Canada's. Canada has a Live-In Caregiver program, which allows professionals in child care, aged care and disability care into the country under a special class of visa. Applicants must have six months of full-time training in a classroom setting or twelve months of full-time paid employment in their chosen area of care.<sup>146</sup>

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143 Adelman S, transcript, 22 September 2005, p 5.

144 Slattery L, transcript, 22 September 2005, p 5.

145 Storm D, sub 167, p 3.

146 Citizenship and Immigration Canada website, viewed on 6 November 2006 at <http://www.cic.gc.ca/english/pub/caregiver/caregiver-2.html#1>.



- 6.137 The committee received a small number of submissions suggesting that Australia consider such programs as models for one of our own. It notes a recent OECD report which suggests that a more responsive supply of affordable child care could be encouraged by 'less restrictive immigration policies'.<sup>147</sup> Given current pressures on the long day care system and shortages of child care workers, a special visa category for au pairs would create some elasticity in local child care markets. By imposing some degree of regulation on the system and setting standards for things such as maximum working hours and workers compensation, this would also prevent the exploitation of young women travellers in Australia.
- 6.138 The committee considers that it would not be appropriate to make au pair expenses eligible for Child Care Benefit. Au pairs are employed under a unique pay structure which does not translate well into a level of assistance paid per hour: they are paid only a small allowance in recognition of the fact they receive accommodation and meals.

### **Recommendation 12**

- 6.139 **The Government investigate the introduction of a national au pair program that would allow child care workers to live-in and work for a host family for 12 continuous months under a special category of visa.**

## **Supporting all child care choices**

### **Inconsistencies in approved and registered care**

- 6.140 The inconsistencies between government assistance for registered care, in the case of nannies, and approved care, in the case of long day care centres, drew the committee's attention to other inconsistencies in this classification that effectively attributes greater or lesser values to different types of care.
- 6.141 Child Care Benefit for approved care (most long day care, family day care, before and after school care, vacation care, some occasional care and some in-home care providers) is means-tested, ranging from \$0.497 to \$2.96 per child per hour depending on family income. All families using approved

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147 Jaumotte F, 'Labour force participation of women: Empirical evidence on the role of policy and other determinants in OECD countries' (2003), *OECD Economic Studies*, no 37, p 92.

care are, however, eligible for the 30 per cent Child Care Tax Rebate for out-of-pocket child care costs, to a maximum value of \$4,000.

6.142 Registered care, on the other hand, is care provided by family day care, some private preschools and kindergartens, some outside school hours care services and some occasional care centres. It also includes care by grandparents, relatives, friends or nannies that are registered with the Family Assistance Office. Families using registered care are entitled to only the minimum rate of Child Care Benefit, currently \$0.497 per hour per child.<sup>148</sup> They are not eligible for the Child Care Tax Rebate.

6.143 These inconsistencies have not escaped the notice of parents, for whom there may be thousands of dollars in Child Care Benefit and Child Care Tax Rebate at stake. A mother wrote to the committee about preschools:

The preschool my son attends on the days I work is registered rather than approved, and, therefore, I will not be assisted by the Federal Government's 30 per cent Child Care Tax Rebate.

The premise of the rebate was surely to provide taxation relief to young families where all guardians were undertaking work, study or training, making child care an essential expense. What then should it matter whether this be an approved or registered child care provider? It should be sufficient that they be licensed to provide child care services. The taxpayer's choice of supplier should not affect eligibility for the rebate.

This legislation, as it stands, is going to lead to the inequitable treatment of Australian taxpayers. The Child Care Tax Rebate was meant to help working families with the cost of child care. Some families don't deserve that more than others because of the *type* of child care provider they choose.<sup>149</sup>

6.144 The committee agrees that if the government offers child care assistance (and there are strong social and economic imperatives for doing so) parents should have more choice about how they expend that assistance. Providing that all subsidised care meets minimum qualification and registration standards, there is no reason to distort market behaviour by giving parents a greater subsidy for a form of care which may not suit their work and lifestyle needs, nor the needs of the child. As we have seen, there are many parents who cannot use long day care or after school care because they need care outside of the opening hours, or because the

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148 Centrelink website, viewed on 11 May 2006 at [http://www.centrelink.gov.au/internet/internet.nsf/payments/qual\\_how\\_ccb.htm](http://www.centrelink.gov.au/internet/internet.nsf/payments/qual_how_ccb.htm).

149 Selas J, sub 185, p 1.

inflexible payment model for child care places is not appropriate to casual or sporadic working patterns.

6.145 There is a precedent for offering government assistance for a more flexible range of child care options. As noted above, the Child Care Cash Rebate, introduced in 1994, was innovative both in its break from means-tested child care assistance (it was paid to all working parents) and in its flexibility. The 1996 Economic Planning Advisory Commission report on child care found that the advantage of the Child Care Cash Rebate was that it was 'payable for a wide range of child care services, delivered in a variety of settings'. This included in-home care.<sup>150</sup>

6.146 The Economic Planning Advisory Commission concluded that a funding distinction between different forms of care was illogical and unreasonably distorted parents' choices about the care they used for their children:

The Task Force considers that both equity and efficiency considerations would require that all forms of paid child care provided outside the family should achieve equivalent treatment in terms of funding. The Task Force recommends that all forms of paid child care, including occasional care, vacation care, nanny care and informal care, which meet required quality standards should be equally eligible for financial assistance.<sup>151</sup>

6.147 The Taskforce on Care Costs, a group of business and non-government organisations, recently made a similar recommendation to government:

The extension of [the current child care assistance] to fully cover registered care will place approved care and registered care on a level playing field and provide real choice to carers with dependents. It is anticipated that the extension of benefits to registered care will improve the quality of care outside the approved care sector and will also reduce the cash economy, with significant secondary benefits.<sup>152</sup>

6.148 In light of the above, the committee makes the following recommendations.

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150 Economic Planning Advisory Commission, *Child Care Task Force interim report: Future child care provision in Australia* (1996), pp 101-102.

151 Economic Planning Advisory Commission, *Child Care Task Force interim report: Future child care provision in Australia* (1996), p 111.

152 Taskforce on Care Costs, *Where to now? 2006 Final report* (2006), p 43.

**Recommendation 13**

- 6.149      **Paid care currently categorised as registered, including family day care, occasional care, outside school hours care, private preschools and in-home care; excluding care provided by grandparents, relatives or friends; be re-categorised as approved care, and thus attract payments and tax concessions extended to users of approved care.**

**Recommendation 14**

- 6.150      **The registered care category and associated rates of Child Care Benefit continue to apply for work-related care that is provided by grandparents, relatives or friends who are registered with the Family Assistance Office.**



## Tax relief for child care

### Salary sacrifice

- 7.1 As outlined in chapter three, employer-sponsored child care is exempt from fringe benefits tax (FBT), where provided on business premises. This means that employers can give staff the option of salary sacrificing child care fees, by which employees forgo part of their salary and employers pay the child care fees. Employees do not pay income tax on the portion of salary they have sacrificed, so they gain what amounts to a tax deduction in every pay packet.
- 7.2 Without the exemption under the *Fringe Benefits Tax Assessment Act 1986*, employers offering this would incur a fringe benefits tax penalty of 46.5 per cent of the value of the benefits provided. Regardless of whether this liability would be borne by the employer or transferred to staff by means of an employee contribution, it would mean that salary sacrificing would not be worthwhile.
- 7.3 The intention of the exemption, therefore, was to encourage employers to participate in solutions to their employees' child care needs. This would assist not only employees but contribute to the government's objectives for increased women's workforce participation.
- 7.4 In fact, the committee has found that the business premises limitation of the exemption, combined with continuing uncertainty about the Australian Taxation Office's rulings on the exemption legislation, is discouraging employers from getting involved.

## Who is salary sacrificing for child care?

- 7.5 The exact number of employees salary sacrificing for child care is not known, and nor is the value of this practice as a tax expenditure by government. This is because exempt benefits do not have to be reported to the Australian Taxation Office. As the Office told the committee:
- In-house child care benefits – that is the exempt benefits – provided under salary sacrificing arrangements or otherwise are exempt fringe benefits that are not required to be reported in the payment summary or disclosed in the FBT returns. We would have no information on that.<sup>1</sup>
- 7.6 The Australian Taxation Office also disclosed that due to the self-assessment of fringe benefits by employers, it was possible that there were employers offering salary sacrificing for child care that was not exempt and not reporting the fringe benefits tax liability. Commissioner of Taxation, Michael D’Ascenzo, said that, ‘There is no requirement in the law or in our practices for people who salary sacrifice to indicate to the Tax Office that they are salary sacrificing’.<sup>2</sup>
- 7.7 In modelling commissioned by the committee, consultants Econtech calculated that the cost to revenue of the fringe benefits tax exemption for child care fees is approximately \$14.08 million per year.<sup>3</sup> This figure was based on evidence gathered by the committee on private companies and Australian Government departments currently offering salary sacrifice; evidence presented in submissions and public hearings; and available workplace surveys from recent years.
- 7.8 Available data suggests that there are very few employers offering salary sacrificing for child care. The impracticalities of the exemption for most businesses, together with the inhibiting effect of Australian Taxation Office rulings, are evidenced by low levels of take up around Australia. A review in 2000 found that there were only 65 employer-sponsored child care centres nationwide.<sup>4</sup>

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1 Chooi A, transcript, 29 November 2006, p 10.

2 D’Ascenzo M, transcript, 29 November 2006, p 4.

3 Econtech, Appendix E, p i.

4 Department of Family and Community Services and Department of Employment and Workplace Relations, *Australia’s background report (2002) for the OECD Review of family-friendly policies: The reconciliation of work and family life*, p 49.

- 7.9 Deloitte and 37 other top 200 companies made a submission to the Federal Treasurer on the subject of this exemption in 2005. Deloitte said:

Numerous surveys indicate that there are very few child care facilities located on the employer's business premises... From our own survey in 2005 of 599 employers with a total workforce of over 300,000 employees, less than ten employers provided a facility that qualified for this exemption.<sup>5</sup>

- 7.10 Similarly, salary packaging provider McMillan Shakespeare told the committee that across their 1000 employer clients there was a very small number who were able to take advantage of the exemption:

I guess as a provider of salary packaging services to a wide range of employers across the country, from the Kimberley to far north and far south of the country, with 160,000 people packaging [for a range of benefits], it is pretty damning to say that fewer than 1,000 people are currently participating in salary packaging arrangements [for child care] out of the 160,000 that we have. Of the 1,000 employers, obviously very few are able to offer that as a benefit.<sup>6</sup>

- 7.11 In its submission, the South Australian Government claims that there is only one employer large enough to sustain an onsite child care centre in the entire state, so that the fringe benefits tax exemption in practice offers no assistance to close to 100 per cent of South Australian workers.<sup>7</sup> Meanwhile, Westpac Bank claimed to have opened the first corporate child care centre in Brisbane only in August 2006.<sup>8</sup>

- 7.12 There are, as the committee has discovered, a minority of employees in major banks, universities and Australian Government departments who are able to salary sacrifice for child care. Employers offering salary sacrificing for child care in Australia include those detailed below in figures 7.1 - 7.3:

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5 Deloitte et al., 'Submission to the Federal Treasurer: Exemption of child care from fringe benefits tax' (2005), synopsis, pp 2, 4.

6 Podesta A, transcript, 1 November 2006, p 2.

7 South Australian Government, sub 155, p 14.

8 'Westpac opens the first corporate child care centre in Brisbane', media release, 25 August 2006.



**Figure 7.1 Private sector employers offering salary sacrificing for child care**

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ANZ Bank  
Westpac Banking Corporation  
National Australia Bank  
Shell Australia

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*Source: Correspondence with employers, various, 2006.*

**Figure 7.2 Universities offering salary sacrificing for child care**

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Monash University  
Griffith University  
Curtin University  
University of Western Australia  
University of Wollongong  
University of Adelaide  
University of Western Sydney  
University of New England  
Flinders University  
Queensland University of Technology

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*Source: Correspondence with employers, various, 2006.*

**Figure 7.3 Australian Government agencies offering salary sacrificing for child care**


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Department of Foreign Affairs and Trade  
 Department of Finance and Administration  
 Department of the Treasury  
 Department of Defence  
 Attorney-General's Department  
 Department of Employment and Workplace Relations  
 Department of Agriculture, Fisheries and Forestry  
 Department of Industry, Tourism and Resources  
 Department of Immigration and Multicultural Affairs  
 Australian Taxation Office  
 Australian Sports Commission  
 Commonwealth Science and Industrial Research Organisation  
 Australian Bureau of Statistics  
 Australian Fisheries Management Authority  
 Biosecurity Australia  
 Land and Water Australia  
 Dairy Adjustment Authority  
 Office of Parliamentary Counsel  
 Office of the Privacy Commissioner  
 Australian Sports Commission  
 Australian National Museum  
 Special Broadcasting Service (SBS)  
 Australian Broadcasting Corporation (ABC)  
 Telstra  
 Australian Communications & Media Authority  
 Australian Sports Anti-Doping Authority  
 Commonwealth Grants Commission  
 Austrade  
 Private Health Insurance Administration Council  
 Tourism Australia  
 Australian National Audit Office  
 Office of the Governor-General  
 Australian Securities and Investment Commission  
 Australian Office of Financial Management

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Source: Correspondence with agencies, various, 2006.

- 7.13 It should be noted that not all employees of these agencies and companies will have access to salary sacrificing for child care, if their work location is not in proximity to a child care facility that meets the requirements of the fringe benefits tax exemption. Staff members in outlying campuses and branch offices in regional and outer metropolitan areas are unlikely to be able to take up salary sacrificing

for child care, because there will not be a sufficient concentration of staff for employers to establish a child care centre.

- 7.14 Australian Government departments are advantaged in respect of the exemption by section 4(1) of the *Fringe Benefits Tax (Application to the Commonwealth) Act 1986*, which says that a department should be regarded as if it were a company, and each other department or authority of the Commonwealth should be regarded as a related company.
- 7.15 This means that if employees of one department salary sacrifice for child care on the premises of another government department, that will qualify as the 'business premises' of a related company and hence qualify for exemption from fringe benefits tax. For example, the Department of Finance and Administration has advised that its staff can salary sacrifice for child care fees at a centre located in the Treasury building. The Australian Tax Office has advised that its staff can do the same at a centre owned by the Australian Bureau of Statistics.<sup>9</sup>
- 7.16 Employees of Australian companies, universities and public sector agencies that do offer salary sacrificing for child care fees are fortunate to work for an employer with both the initiative and capacity to establish a child care centre on business premises. However, the available information suggests that they are a privileged few in relation to Australia's total workforce.
- 7.17 Lenore Taylor writes in the *Australian Financial Review*:
- When one woman at our Canberra mothers' group confided she could salary sacrifice for child care it was like the famous scene from *When Harry Met Sally*. En masse. We all wanted what she was having.<sup>10</sup>

## Business premises limitation

- 7.18 Under section 47(2) of the *Fringe Benefits Tax Assessment Act 1986*, where:
- the recreational facility or child care facility, as the case maybe, is located on business premises of:
- (i) the employer; or

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9 Department of Finance and Administration, transcript, 11 October 2006, p 1; Australian Taxation Office, correspondence, 14 August 2006.

10 Taylor L, 'A sacrifice worth making', *Australian Financial Review*, 19 August 2006, p 30.

(ii) if the employer is a company, of the employer or of a company that is related to the employer;

the benefit is an exempt benefit.

7.19 The Commissioner of Taxation and the courts have assessed 'business premises of the employer' by way of a two-part test. Firstly, business premises must be the site of business operations; and secondly, in order to be *of the person*, there must be a relationship of ownership or control between the employer and the premises.

7.20 The first test has been interpreted broadly by the Commissioner and the courts, who have held that child care provision is a part of business operations. The site of a child care facility may therefore be business premises.<sup>11</sup> Justice Merkel of the Federal Court found that:

Once it is accepted that the provision of benefits to employees in the form of child care at business premises of an employer is an important factor in recruiting, retaining and otherwise rewarding employees and, as such, is part of the business operations of the employer, it does not seem to be relevant whether the child care facilities are located at the premises where the employer carries out other business operations, or are located at premises of the employer which have been procured solely for the purpose of the provision of a child care facility thereon.<sup>12</sup>

7.21 If, for example, an employer takes a commercial lease on a site several blocks away from the office, in order to operate a child care facility there, that may qualify for the exemption. Another example, provided in the Commissioner of Taxation's public ruling, is of a mining company, whose staff are located in a company town 30 kilometres from the site of mining operations. Should that mining company construct a child care centre in the town, for the use of employees, that would be considered fringe benefits tax exempt.<sup>13</sup>

7.22 The second part of the test, whether the premises are *of the person*, has been more contentious. In both of the examples above, the employer has sufficient control of the premises and of the child care operations to satisfy the requirement for possession. In another of the

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11 Federal Commissioner of Taxation's private ruling, cited by Merkel J, *Esso Australia Ltd v FC of T* 1998 ATC 4953.

12 *Esso Australia Ltd v FC of T* 1998 ATC 4953.

13 Federal Commissioner of Taxation, public ruling TR 2000/4, 'Fringe benefits tax: meaning of "business premises"'.

Commissioner of Taxation's examples, however, a professional child care provider establishes a centre in the CBD of a major city, and enters in arrangements with surrounding employers to provide child care to their children. Even if these employers enter into a series of subleases for undivided shares of the premises, they still cannot demonstrate sufficient control of the premises or of the management of the child care operation.<sup>14</sup>

- 7.23 For most employers, the expense and increased legal liability incurred in doing that will be too onerous. Deloitte has asserted:

The cost of an [on site child care facility] and the associated administration costs will usually outweigh the benefits for most employers... The administration and risks associated with government regulations and industry accreditations in operating and managing a child care facility are significant.<sup>15</sup>

- 7.24 Establishing an in-house child care facility also exposes employers to considerable risk should business needs change. McMillan Shakespeare told the committee:

We have some cases where employers have set up such establishments and then they find it is a white elephant a number of years later because the demographics change and they have been caught.<sup>16</sup>

- 7.25 Aegis Consulting confirms the cost of an employer establishing a child care centre in the Sydney CBD can be upwards of \$2 million; the Department of Finance and Administration advised that it had cost \$2 million to establish their child care in Canberra's Parliamentary Triangle.<sup>17</sup> Deloitte claims that an on-site centre might take ten years to become financially sustainable for an employer.<sup>18</sup>

- 7.26 It is difficult for employers to justify taking on such a risk when it does not relate to a company's core business.<sup>19</sup> BHP Billiton told the

14 Federal Commissioner of Taxation, public ruling TR 2000/4, 'Fringe benefits tax: meaning of "business premises"'.

15 Deloitte et al., 'Submission to the Federal Treasurer: Exemption of child care from fringe benefits tax' (2005), synopsis, p 3.

16 Podesta A, transcript, 1 November 2006, p 3.

17 Aegis Consulting, sub 107, p 8; and Department of Finance and Administration, Hutson J, transcript, 11 October 2006, p 5.

18 Deloitte et al., 'Submission to Federal Treasurer: Exemption of child care from fringe benefits tax', 11 November 2005, p 11.

19 Deloitte et al., 'Submission to the Federal Treasurer: Exemption of child care from fringe benefits tax' (2005), synopsis, p 3.

committee that they wanted to assist employees with child care, and were even willing to provide seed funding for a child care venture near one of their mining operations in Western Australia. They felt, however, that they did not have the necessary expertise or inclination to operate a child care centre. 'The BHP Billitons of this world do not know how to run child care', said the company in evidence.<sup>20</sup> Additionally, where the company was installing major mining operations adjoining small regional towns, it was unwilling to create a climate of community resentment by reserving 'soft' infrastructure and services such as child care for BHP Billiton employees.

- 7.27 The committee considers this a reasonable attitude, particularly when there are already professional providers with child care expertise, not to mention facilities in which they are already operating child care services.
- 7.28 The Department of Defence's dilemma is another case in point. Defence own 19 child care centres which are available for employee use; shortly before giving evidence to the committee they had acquired a further 30 centres through a lease licence arrangement with ABC Learning Ltd. A significant number of Defence children are already enrolled, and the Department has applied for a private ruling on whether the parents of these children would be able to salary sacrifice for the child care fees. At the time of giving evidence, the Department of Defence felt that given the restrictions of the business premises test, it was unlikely to be successful.<sup>21</sup>
- 7.29 Centrelink told the committee that they were negotiating with tenderers but were yet to apply for a private ruling which would cover their 38,000 employees across Australia. At the time of writing, however, it was not clear what the terms of the application would be and whether it would be successful.<sup>22</sup>

## Small and medium-sized workplaces

- 7.30 If the establishment of a child care centre is daunting for a company of BHP Billiton's size, the exemption certainly discriminates against small and medium-sized businesses. These typically have smaller workforces, have lesser financial resources, and are less likely to pay for professional legal advice for a matter outside their core business.

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20 Murray F, transcript, 30 June 2006, p 49.

21 Stodulka J, Defence Community Organisation, transcript, 21 August 2006, pp 23-24.

22 Cotterill P, 13 September 2006, transcript, private briefing, pp 3-4.

7.31 In a survey conducted by Aegis Consulting, employers said that they felt it was uneconomical to establish a child care centre unless there were at least 1,000 employees in any one location and at least 40 children using the facility.<sup>23</sup> Three and a half million Australians, however, are employed by small businesses with less than 20 workers, representing 49 per cent of all private sector employment.<sup>24</sup> As at June 2004, 32.8 per cent of all small businesses employed between one and four people.<sup>25</sup> Under current fringe benefits tax legislation and the Commissioner of Taxation's rulings, a number of such businesses cannot combine together in order to operate a child care cooperative for the benefit of their workers.<sup>26</sup>

7.32 Aegis told the committee, 'At the moment there is what we would consider an anomaly in the tax system that discriminates against small and medium sized employers'.<sup>27</sup> Under questioning about the fringe benefits tax exemption for child care, the Australian Taxation Office agreed that, in a practical sense, this was so:

Legally, all taxpayers are able to enter into the same arrangements as described in our public ruling and get such an exemption. But we are aware that it is not very practical for small business.<sup>28</sup>

7.33 The committee received a number of comments on this subject:

As a PAYE employee without access to employer supplied child care, there is no possible mechanism for me to pay child care fees from pre-tax income. If my employer was a university or a large bank or another employer with child care facilities on-site, this would be possible, saving me 32 per cent of child care costs...Why are these avenues open to only select people within society?<sup>29</sup>

It is unfortunate that salary sacrifice is available to a select few. It is impossible for a small business to erect and maintain

23 Aegis Consulting, sub 107, p 8.

24 Australian Bureau of Statistics, *Small business in Australia, 2001* (2002), Cat No 1321.0, p 1.

25 Australian Bureau of Statistics, *Characteristics of small business, Australia, 2004* (2005), Cat No 8127.0, p 31.

26 Federal Commissioner of Taxation, public ruling TR 2000/4, 'Fringe benefits tax: meaning of "business premises"'; see also Konza M, Australian Taxation Office, transcript, 21 June 2006, p 19.

27 Beri V, transcript, 22 July 2005, p 19.

28 Konza M, transcript, 21 June 2006, p 17.

29 Fulton P, sub 38, p 1.

a child care facility whilst the Australian Government and other large groups, e.g. banks, are able to fully sustain their own work based child care centre.<sup>30</sup>

## Regional and rural workplaces

7.34 For the same lack of economies of scale, regional and rural workplaces are unlikely to benefit from the fringe benefits tax exemption for child care. In many rural centres, it is difficult to sustain a single public access child care centre, let alone to establish another for the employees of one company.

7.35 Businesses with a national distribution of staff are finding that they are unable to offer regional employees the same conditions as their metropolitan counterparts. It is not feasible for them to enter in leasing and operating arrangements for child care centres in every town where they have branches. ANZ Bank gave evidence on their suite of family-friendly provisions, including five child care centres, to be followed with a further six leased through an agreement with ABC Learning:

Whilst many of our ANZ families have utilised child care provided through ANZ's partnership with ABC, it is impractical for a company that operates in so many communities across Australia to ensure these centres are accessible to every employee.

ANZ locates centres in areas where there is likely to be a high demand from ANZ families which tends to be CBD locations. This excludes many of our staff outside CBD locations and staff based in regional Australia.

We receive regular feedback from staff requesting the ability to salary sacrifice child care other than that provided by ABC, however due to current fringe benefits tax arrangements salary sacrificing outside of our ABC partnership arrangement is not tax effective for either ANZ or for our staff.

These tax restrictions prevent ANZ from providing support to defray the cost of child care for staff in non-metropolitan areas. The removal of FBT on all child care would enhance

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30 Childcare Queensland, sub 198, p 6.



ANZ's ability to assist our people with their caring responsibilities.<sup>31</sup>

## Are workplaces places for children?

- 7.36 A further problem with the exemption is that many business premises and related areas are inappropriate places to have a child care facility. As Justice Merkel of the Federal Court noted:

Common sense would dictate that in many instances basic requirements for child care facilities may be such that it is inappropriate for the facilities to be located upon the same premises where the other business operations of an employer are conducted.<sup>32</sup>

- 7.37 Deloitte argued that:

Business premises are generally not designed to house child care facilities creating significant set-up and investment costs for employers... A CBD location brings its own concerns. [They include] the difficulty in accommodating drop-off zones for parents as well as the difficulties involved in meeting noise, health and safety, fire and pollution regulations.<sup>33</sup>

- 7.38 ABC Learning gave evidence to the committee that:

We are seeing a lot more child care centres in business parks. We have corporate care services, where we provide centres at the workplace... One of the difficulties we have is that, in many instances, it is unlikely that councils will approve centres in locations that are quite industrial. Also, state regulations have a requirement that centres not be provided in hazardous environments. So where there is storage of chemicals and petroleum products, or concrete batch plants and so on, that will often rule out placing a child care centre in that area.<sup>34</sup>

- 7.39 As another example, the Western Australia Police Service told the committee that police stations were not appropriate places for

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31 ANZ Bank, sub 133, p 6.

32 *Esso Australia Ltd v FC of T* 1998 ATC 4953.

33 Deloitte et al., 'Submission to the Federal Treasurer: Exemption of child care from fringe benefits tax' (2005), synopsis, p 3.

34 Kemp M, transcript, 22 July 2005, p 11.

children, and that the business premises limitation was having an impact on which child care options they were able to consider.<sup>35</sup> The inflexible requirements of the legislation, as interpreted by the Australian Taxation Office, are holding back many employers on the basis of the nature of their business and the working environment of their staff.

- 7.40 Child Care Associations Australia, the national peak body representing primarily private long day care centres, reported that the child care market in the Australian Capital Territory was being distorted by the limitations to the exemption. This was because parents could not exercise choice over where they put their children without losing a financial benefit:

Within the ACT this [business premises limitation] creates distortions in the local market with parents making their choices about child care not on the basis of centre of choice, but the centre offering the most affordable care available. Individual parents in the ACT have found the choices distressing emotionally as they are not necessarily in the best interests of their child. It can also influence the employment decisions made by parents.<sup>36</sup>

## **Reforming the business premises limitation**

- 7.41 Evidence received by the committee indicates that the business premises limitation is distorting the intended outcome of the exemption and imposing penalties on those whom it was designed to benefit.
- 7.42 The Australian economy is already suffering from skills shortages, which are likely to be exacerbated by demographic changes. Therefore, the provision of child care should be a legitimate way for businesses to attract and retain staff, should they choose to do so.
- 7.43 The committee is also concerned that the Australian Taxation Office's interpretation of the legislation is not giving employers certainty about whether they might qualify for the exemption, and that the Office's jurisdiction is potentially straying into policy grounds. It notes that the Inspector-General of Taxation expressed similar concerns in his 2005-06 Annual Report:

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35 Harrison-Ward J, transcript, 30 June 2006, p 46.

36 Child Care Associations Australia, sub 130, p 8.

I am concerned about how the Tax Office approaches interpretation and administration of the law in some significant cases and the potential for this issue to be systemic... I notice that the Tax Office from time to time seems to blur the gap between tax policy and administration... I have noted signs that the Tax Office is willing to interpret and administer the law in line with its view of policy even if the letter of the law does not adequately support it.<sup>37</sup>

- 7.44 Considerable financial and legal resources are being expended in order to meet the business premises rule. Evidence was taken from multiple witnesses who had applied for, or were in the process of applying for, a private ruling from the Taxation Office on their specific circumstances. Despite expenditure of time and money by employers who have a genuine wish to offer child care to their staff, private rulings are returned in the negative. This has been the case for salary packaging provider McMillan Shakespeare, who revealed that their two applications for a private ruling had cost an estimated \$50,000 apiece.<sup>38</sup> The Australian Taxation Office, on the other hand, incurred no such expenditure in order to institute its own salary sacrificing arrangements for child care. In response to a question from the Chairman, it advised:

The Tax Office, as an employer, after reviewing publicly available guidance issued by the tax administration arm of the Office, formed its own view in relation to the application of fringe benefits tax exemption for the salary packaging of child care expense payments.<sup>39</sup>

- 7.45 All this effort, from the committee's point of view, is to satisfy a requirement that is at odds with the encouragement of family-friendly workplaces.
- 7.46 Removing the business premises limitation to the exemption would give employers the opportunity to legitimately assist employees with child care without having to make a long-term commitment to an inflexible and prohibitively expensive child care facility. Removing the fringe benefits tax liability for child care altogether would be even better.

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37 Inspector-General of Taxation, *Annual report 2005-06* (2006), pp 4-5.

38 Podesta A, transcript, 1 November 2006, p 3.

39 Australian Taxation Office, correspondence, 14 August 2006, p 4.

- 7.47 This would mean that small and medium sized businesses could better compete against large firms in attracting and retaining staff who want family-friendly working provisions. It would allow, for example, a small business owner to buy several child care places at a local centre for his staff. It would allow, as well, employees to choose where their children are cared for without losing the ability to salary sacrifice for child care fees.
- 7.48 Employers could also be much more responsive to the changing needs of their workforce. Under the current system, it is difficult for an on-site child care facility to cope with changes in demand. Too much demand, and parents are put onto a waiting list; too little demand, particularly on the last few days of the week, and the centre becomes unsustainable. The Australian Chamber of Commerce and Industry have said:
- If an employer can buy childcare from a number of providers, then sudden changes in demand can be managed. It is less likely that an on-site provider would be able to cope with sudden demand changes.<sup>40</sup>
- 7.49 The committee notes that salary sacrificing is used most for vehicles, superannuation and computers, none of which require a business premises test or indeed any other test except that they are work-related. Child care should be treated in the same way.

### Child care facility limitation

- 7.50 Under section 47(2) of the *Fringe Benefits Tax Assessment Act 1986*, the exemption is only available for a 'child care facility', a term that is subsequently defined in section 136(1) as follows:

*Child care facility* means a facility at which a person receives, or is ready to receive, two or more children under the age of six, not being associates of the person, for the purpose of minding, caring for or educating them for a day or part of a day without provision for residential care but does not include a facility at the place of residence of any of those children.

- 7.51 This definition includes long day care centres and after school hours care facilities, but it is unclear whether occasional care and vacation
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40 Australian Chamber of Commerce and Industry, submission to the Joint Standing Committee on Public Accounts and Audit, Inquiry into a range of taxation issues in Australia, sub 43, p 9.

care are captured. Again, there is business confusion about what does and does not qualify for the exemption. In their submission to the Federal Treasurer, Deloitte wrote that, 'The exemption does not contemplate before and after-school care arrangements... further, the exemption does not consider the demands of vacation care'.<sup>41</sup> In the only interpretative decision made by the Commissioner of Taxation on the subject, he deemed that an after school facility located on the premises of an employer did in fact qualify for the exemption.<sup>42</sup>

- 7.52 Family day care, in-home care (nanny care) and other forms of care, because they are provided in a residential setting, do not qualify for the exemption.
- 7.53 Aegis Consulting suggested to the committee that the restrictiveness of the 'child care facility' requirement meant that employers were not free to find creative child care solutions that met the needs and lifestyles of their workers:

If an employer cannot afford to set up a child care facility and they want to provide the exact same dollar amount to employees to use at their local not-for-profit organisation or even to have the grandparents look after their children, they cannot do it. That means the majority of employers in Australia cannot support their employees' child care needs.<sup>43</sup>

- 7.54 Abacus Ark Corporate Child Care told the committee that employers recognised that parents' work was contingent on their ability to find child care, but that fringe benefits tax penalties were putting them off from pursuing in-home care:

We specialise in providing child care services to companies directly, rather than to the general public. They are saying to us, 'Yes, we'd like to subsidise child care, particularly if we need our employees to come in on their day off, for example, or when there is a project on and they need to work back late'. Somebody has to pay for the child care in that situation. [But] the FBT is putting them off, obviously.<sup>44</sup>

- 7.55 There is also an inconsistency between the exemption in section 47(2), for in-house child care, and the additional exemption in section 47(8)

41 Deloitte et al., 'Submission to the Federal Treasurer: Exemption of child care from fringe benefits tax' (2005), 11 November 2005, p 13.

42 Australian Taxation Office, interpretative decision, ATO ID 2001/309.

43 Beri V, transcript, 22 July 2005, p 19.

44 McInnally A, transcript, 22 September 2006, p 37.

for payments made by employers to secure priority access to child care centres for their employees. Section 47(8) was extended to cover priority access payments made not only to long day care centres but to family day care, vacation care, outside school hours care and approved in-home care services.<sup>45</sup> It is illogical for the exemption under 47(2) to persist with a definition of a child care service that does not reflect the child care options currently available to parents.

- 7.56 In the twentieth anniversary year of fringe benefits tax, the committee considers it timely to update the exemption for child care to make its benefits available to a greater number of Australian workplaces.

### **Recommendation 15**

- 7.57 **Fringe benefits tax be removed from all child care, so that all or any child care provision made by employers to assist employees is exempt, inclusive of salary sacrificing arrangements for child care.**

### **Business support for reform**

- 7.58 Evidence given by many employers over the course of the inquiry indicates that employers are increasingly aware of their employees' child care issues. The current competitiveness of the labour market and economic projections of increased skills shortages are strengthening the business case for offering some form of assistance, whether that be a direct child care benefit or the option of a salary sacrifice arrangement. McMillan Shakespeare, who provide salary packaging services to around 1000 employers across the country, told the committee about the costs of child care shortages to employers across the country:

From our discussions with our employer base, which is predominantly state government employers, Federal Government departments and agencies, public hospitals, for example, it has become clear to me that there is an enormous cost and burden being placed upon the state in particular due to the fact that teachers, police officers and nurses often find child care access difficult and as a result would stay away from work to provide that support for their children at various times. A lack of access to child care means that the

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45 For further information on the exemption under section 47(8), see chapter three.

state effectively has to replace the teacher with a replacement teacher for the day to teach the kids; likewise with nurses, the nurses have to be substituted, and I suspect that in the case of police officers it is about extra overtime and shift work that takes place to cover those shifts. So there is a real burden in terms of those occupations to which I refer and their need for child care.

Likewise, I am told by various authorities that they find it very difficult in some cases to get employees to remote locations or out of city locations because of the issues associated with child care. It is very difficult to get people to rural locations if there are no child care facilities because very often both parents have a job, be they police officers or teachers. That is often the case with hospital workers as well. There is a real need for both working parents to find access to child care in remote locations.<sup>46</sup>

- 7.59 Similarly, the Business Council of Australia reported on the stress that child care shortages were placing on their members:

The vast majority of [our member companies] seek to be employers of choice. They are looking to employ the best people that they possibly can and they are increasingly competing in a very tight labour market. Work-family policies are one of those issues which allow them to attract and retain quality staff... [Child care] is an area where there is growing pressure and where businesses are finding that it is cutting across their own employees' ability and willingness to work.<sup>47</sup>

- 7.60 As an example, a chartered accounting firm in Tasmania gave evidence on how the loss of female workers due to child care costs was causing a critical workforce shortage. Current fringe benefits tax arrangements, however, were making it prohibitive for employers to assist:

There seems to be no logical reason that I can possibly think of why child care on an employer's premises should be exempt from fringe benefits tax when child care provided anywhere else would not be exempt from fringe benefits tax...

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46 Podesta A, transcript, 1 November 2006, p 7.

47 Cilento M, transcript, 10 April 2006, pp 2-3.

From the point of view of being an employer, I can say to you that it has a massive effect on us. The public accounting profession has a huge number of females coming into it. They come out of university, they are 21 years old and we spend a massive amount of time on training them, but by and large we will lose those females four or five years down the track because child care is just too expensive for them.

I know that we as an employer would be more than happy to consider giving child care support if it were not subject to fringe benefits tax.<sup>48</sup>

- 7.61 McMillan Shakespeare felt that their clients, who include employers in the government, non-profit, and private sectors, would welcome the opportunity to assist with child care without the penalty of fringe benefits tax:

I think employers would be delighted to see that test being removed. If the provision of child care was fringe benefits tax exempt, if it were just seen as part of the cost of employment, like laptop computers, mobile phones, income protection insurance, for example – if it were seen as just part of our Australian workplace culture and needs – then I think employers would be delighted.<sup>49</sup>

- 7.62 Aegis Consulting spoke about one of its clients, tourism and services group Accor, who employ about 10,000 people in Australia, and of MacDonald's:

Most of [Accor's employees] are casuals but Accor would love to be able to give them the opportunity to salary sacrifice or even in some circumstances give them an extra top-up for child care, because it is an industry that relies on people where there are skills shortages. As you know, the workforce of McDonald's is pretty casual but they are firmly behind the notion of having flexibility to provide that kind of child care benefit to their employees.<sup>50</sup>

- 7.63 On 11 November 2005, Deloitte and 37 other corporate participants lodged a submission with the Federal Treasurer appealing for reform

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48 Leighton C, partner of Ruddicks Chartered Accountants, Joint Committee of Public Accounts and Audit, Inquiry into Certain Taxation Matters, transcript, 24 August 2006, pp 32-33.

49 Podesta A, transcript, 1 November 2006, p 8.

50 Beri V, transcript, 22 July 2005, p 28.



of the fringe benefits tax treatment of child care. The group, which included many top Australian companies, asked the Treasurer to remove both the business premises and the child care facility limitation to the exemption.<sup>51</sup>

- 7.64 The committee has received correspondence from Shell Australia Ltd expressing full support for the reforms proposed by Deloitte and their partners.<sup>52</sup> Other major representative business groups, such as the Business Council of Australia and the Australian Chamber of Commerce and Industry, have spoken in support of fringe benefits tax reform for child care.<sup>53</sup>
- 7.65 Health insurance and health care corporate BUPA Australia have said to the committee that child care is poorly supported by the existing fringe benefits tax legislation. The expense and logistical problems posed by operating a child care facility were the reasons why they chose not to provide salary sacrificing arrangements to their staff.<sup>54</sup>
- 7.66 As a further example, Monash University has written to the committee to:
- ...express general concern about the restrictions imposed by fringe benefits tax on an individual organisation's capacity to enable staff to benefit from salary packaging...
- Monash University would encourage the implementation of suggested amendments which would enable a shared provision of child care, for example as a partnership between the University and other employers in the local community. This could be of benefit both to our staff and to the strengthening of our relationships with other local organisations.<sup>55</sup>
- 7.67 The committee believes that this interest in child care by employers is encouraging, and that ideas such as this one show promise. It is contradictory to the best interests of government, business and workers that employers continue to decide against child care assistance due to tax penalties.

51 Deloitte et al., 'Submission to the Federal Treasurer: Exemption of child care from fringe benefits tax' (2005).

52 Shell Australia Ltd, correspondence, dated 27 September 2006.

53 Ker P, 'Family still "women's business"', *The Age*, 11 April 2006, p 9; Australian Chamber of Commerce and Industry, supplementary sub 153, p 7.

54 BUPA Australia, correspondence, dated 27 September 2006.

55 Monash University, correspondence, dated 27 September 2006.

- 7.68 Employers who are already offering salary sacrificing for child care have reported that the administrative burden on the business is minimal. The Commonwealth Scientific and Industrial Research Organisation told the committee:

We allow salary sacrifice directly from our pay system, and that is administratively efficient for us. In a sense, it is no different from allowing people to make deductions to a bank or anywhere that takes electronic funds transfers. So it is pretty efficient and it is not administratively burdensome for us.<sup>56</sup>

The Department of Foreign Affairs and Trade agreed:

We are the same: salary sacrificing is not an administrative burden at all. In terms of the child care centre, we have a staff member who has, as part of their responsibilities, the management of the contract and a liaison role with the child care centre, but I would not consider it to be at all onerous. In fact, it is relatively easy. There is an issue in terms of being able to get staff back to work a little quicker, so it is an easy trade-off.<sup>57</sup>

## Tax deductibility for child care

- 7.69 In this section, the committee will explore a solution that could be available simultaneously with increased salary sacrificing; i.e., a tax deduction for work-related child care.
- 7.70 A single father of four children, Paul Richards, forwarded to the committee a letter he received from the Treasurer in response to his question about whether child care could be made tax deductible. In this person's case, his fly-in fly-out job necessitated overnight care, so he could not use long day care or access any financial assistance that would enable him to work. The Treasurer wrote:

Expenses of a predominantly private or domestic nature, such as child care expenses, do not qualify for deductions.

If individuals were able to access deductions for child care, the benefit received would reflect their marginal tax rate,

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<sup>56</sup> Smith W, transcript, 11 October 2006, p 11.

<sup>57</sup> Williams P, transcript, 11 October 2006, p 11.

resulting in different treatment of individuals contingent on their income. The individuals who would benefit most would, of course, be on the top marginal tax rate. Individuals without a tax liability would not be able to benefit from deductions.<sup>58</sup>

- 7.71 The committee accepts that tax deductibility for child care, if applied as the sole form of government assistance for child care, would not be advantageous for people with a low or nil tax liability. This problem has been considered seriously by the committee and is addressed later in this chapter.
- 7.72 But there is a logical inconsistency in the Government's policy position on tax deductibility for child care. Public servants in the Treasurer's own department can salary sacrifice for child care, as can employees of the Australian Taxation Office. Through the fringe benefits tax exemption, an elite number of Australian employees are permitted to deduct the cost of child fees from their pre-tax income. They enjoy, in fact, tax deductibility for child care. The Australian Taxation Office, in evidence, confirmed that while the mechanisms were different, the monetary outcomes of salary sacrificing for child care and a tax deduction for child care were exactly the same.<sup>59</sup>
- 7.73 The public service has a role as a model employer, and the committee congratulates the agencies offering salary sacrificing for child care for taking leadership.<sup>60</sup> But the Government's obligation is to make sure that other workers can also access these benefits. The self-employed and those working for small businesses need equity in their child care choices. Why should a tax deduction not also be available to those who do not have a workplace offering on-site child care?
- 7.74 The policy idea of tax deductibility for child care is not new. Since the 1970s, governments have repeatedly rejected calls to make child care costs a tax deduction. In 1980, for example, the Women Members Group of the Australian Society of Accountants made a submission to the Federal Treasurer urging that tax deductions for child care expenses be made available to working mothers and single fathers. The group claimed that:

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58 Annexure B to Richards P, sub 170, p 1.

59 D'Ascenzo M, Commissioner of Taxation, and Chooi A, transcript, 29 November 2006, p 8.

60 Australian Government agencies offering salary sacrificing for child care are detailed in figure 7.3.

... such a system, by decreasing the net cost of going out of work, would encourage more women to earn taxable income, thereby increasing tax revenue. It also argued that welfare payments would be reduced and employment created as a result of increased demand for child care places, and that facilitating women's return to the workforce after the birth of their children would result in a better return from public investment in the education and training of women.<sup>61</sup>

These arguments still resonate.

## Child Care Tax Rebate

- 7.75 The Child Care Tax Rebate, announced in the 2004-05 Budget, acknowledges for the first time the vital role that taxation plays in women's ability to work. It is not means-tested and provides vertical equity for child care costs across the income scale, while targeted assistance remains in the form of the means-tested Child Care Benefit.
- 7.76 It could, however, go further in stimulating workforce participation outcomes. Unlike a tax deduction for a work-related expense, the Child Care Tax Rebate is not strongly linked to workforce participation and does not make explicit recognition of child care as an essential cost of working.<sup>62</sup>
- 7.77 The rebate is capped at \$4,000, which may not be sufficient for families dependent on formal care, particularly if they are living in the inner metropolitan areas of cities like Sydney. Additionally, as the committee explored in the previous chapter, the Child Care Tax Rebate is only payable for approved care, meaning that many families miss out.
- 7.78 The following section will examine arguments for and against making child care expenses tax deductible.

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61 Cass B and Brennan B, 'Taxing women: The politics of gender in the tax/transfer system', *eJournal of tax research* (2003), University of New South Wales, vol 1, no 1, p 48.

62 There is a child care benefit test for the Child Care Tax Rebate, but it is not stringent. The then Assistant Treasurer the Hon Mal Brough MP moved in 2005 to ensure that parents who worked less than 15 hours a week would continue to have access to the rebate provided that they participated in work, training or study at some time during the week. Hon Brough MP, Assistant Treasurer, 'Child care rebate assured in tax changes', media release, 7 December 2005.

## Essential cost of working

- 7.79 Despite the rejection of a number of attempts by Australian taxpayers to claim child care expenses as a deduction, the courts and the Federal Commissioner of Taxation have accepted that in many cases child care expenditure is necessary for a person to be able to work. In fact, they have been generally sympathetic to taxpayers. Justice Mason noted in 1972 that:

The [child care] expenditure was incurred for the purpose of earning assessable income and it was an essential prerequisite of the derivation of that income.<sup>63</sup>

- 7.80 Similarly, Chief Justice Bowen and Justices Toohey and Lockhart acknowledged in 1984 that:

It may be accepted that the placing of [the taxpayer's] child in a kindergarten (and the incurring of expenses thereby) was a prerequisite to the taxpayer's employment. It was not suggested that any other course was open to her if she was to take on any of the three jobs in question.<sup>64</sup>

- 7.81 This is consistent with evidence received by the committee that for many parents, child care is an unavoidable cost incurred in taking paid work. It is often calculated against potential increased income when a parent decides whether to return to the workforce. The committee received many impassioned comments on the necessity of child care to the working parent:

As a civilized society we should be ready to accept that if parents are to work they need child care - not all families are fortunate to have relatives to take care of the children or earn enough (a minimum of A\$60k in Sydney), to pay for quality child care. It should be deductible for families.<sup>65</sup>

Child care is absolutely essential to me being able to be employed, so why is it not tax deductible? Why is my briefcase, my computer, my corporate clothes, my study expenses etc all tax deductible, whereas child care is not? Child care costs me 150 per cent more than my mortgage

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63 *Lodge v FC of T* 1972.

64 *Martin v FC of T* 1984.

65 Carroll G, sub 40, p 3.

costs, and this is... only for 3 days per week for two children.<sup>66</sup>

Child care is a work-related expense for the vast majority of parents, and thus should be tax-deductible for working parents.<sup>67</sup>

If something as obscure as a handbag or a briefcase is deemed to be a necessary tax-deductible cost of employment, I struggle to see how child care costs for a working parent could sensibly be interpreted otherwise.<sup>68</sup>

In my book, child care has to be considered a work related expense... If you are paying child care, taxable income is a grossly exaggerated figure as opposed to what you are actually taking home. I pay \$6,000 per annum in child care. If that \$6,000 was taken off my taxable income I would get tax breaks and far more assistance. I find it really strange.<sup>69</sup>

Deductibility for individuals with child care expenses for work-related reasons acknowledges that today there is a nexus between child care expenses and income: some of us with children cannot work unless our children are looked after. Without child care, we would not be working.<sup>70</sup>

## Nexus between child care and income

7.82 The courts have held that the essential nature of child care is not sufficient to qualify for a deduction under section 8-1 of the *Income Tax Assessment Act 1997*. As outlined in chapter three, allowable deductions must be 'incurred in gaining or producing the taxpayer's assessable income'. That is, they must arise directly from the nature of the activity whereby a person earns an income.

7.83 It is possible that many of the deductions presently allowable as business expenses have a less direct relationship to work activity than, say, a plumber or carpenter to his tools. In a well-known Canadian case, *Symes v The Queen* 1993, a married woman working full time in a Toronto law firm attempted to claim deductions for the

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66 Fulton P, sub 38, p 1.

67 Name suppressed, sub 95, p 2.

68 Carr B, Women Lawyers Association of NSW, transcript, 13 March 2006, p 57.

69 Fenney-Walch B, transcript, 11 April 2006, p 16.

70 Jacobsen S, 'Child care is taxing', *Law Institute Journal* (2005), vol 79, no 12, p 83.

cost of employing a nanny. Justice L'Heureux-Dubé, a Supreme Court judge who dissented from the final decision, wrote:

One must ask whether the many business deductions available, for cars, for club dues and fees, for lavish entertainment and the wining and dining of clients and customers, and for substantial charitable donations, are so obviously business expenses rather than personal ones.<sup>71</sup>

- 7.84 In Australia, where boardroom lunches and magazine subscriptions are tax-deductible, but child care is not, there is a similar confusion about what constitutes a legitimate expense of doing business.

### **'Private and domestic' expense**

- 7.85 Further to the fact that a deductible expense must be incurred in gaining or producing income, there is a disqualification in the *Income Tax Assessment Act 1997* of deductible expenses that are private or domestic:

You cannot deduct a loss or outgoing under this section to the extent that... it is a loss or outgoing of a private or domestic nature.

- 7.86 For over 30 years it has been a principle of Australian tax law that child care costs are essentially expenses of a private nature. In a society dominated by a traditional breadwinner model, this assumption was unchallenged. At the time of Justice Mason's decision in 1972, which created precedent for the taxation treatment of child care in Australia thereafter, the average participation rate for women was only 37.1 per cent.<sup>72</sup> The concept prevailed of the breadwinner husband earning income to provide for the family, supported by a wife at home performing the 'private' tasks of housekeeping and caring for children.
- 7.87 Increasingly, however, the sole breadwinner division of labour resembles fewer and fewer Australian households. Women's still-growing participation in the workforce means that there can no longer be an assumption that a worker has someone at home to perform the 'private' tasks that support their ability to work. Parents of both genders now move more fluidly between the spheres of public

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71 *Symes v the Queen* 1994 [Canada], L'Heureux-Dubé J, dissenting report, p 81.

72 Australian Bureau of Statistics, *Census of population and housing* (1971), cited in *Australian social trends, 2003* (2003), Cat No 4102.0, p 134.

and private labour: from the kitchen to the workplace; and from the child care centre to the home office. It is unsurprising that there are continuing tensions in our income tax law about what expenses are legitimately 'work-related'.

- 7.88 Justice L'Heureux-Dubé in the Canadian case offers a thoughtful interpretation of the public/private divide:

In my view, it is important to look closely at the dichotomy of business as opposed to personal expenses. If we survey the experience of many men, it is apparent why it may seem intuitively obvious to some of them that child care is clearly within the personal realm. This conclusion may, in many ways, reflect many men's experience of child care responsibilities.

In fact, the evidence before the Court indicates that, for most men, the responsibility of children does not impact on the number of hours they work, nor does it affect their ability to work. Further, very few men indicated that they made any work-related decision on the basis of child-raising responsibilities.

The same simply cannot be said for women. For women, business and family life are not so distinct and, in many ways, any such distinction is completely unreal, since a woman's ability to even participate in the workforce may be completely contingent on her ability to acquire child care. The decision to retain child care is an inextricable part of the decision to work, in business or otherwise.<sup>73</sup>

- 7.89 In the case mentioned above, a majority of 5-2 in the Supreme Court of Canada held that child care expenses were not deductible. The decision was split along gender lines; the five men sitting on the case found that the expenses were not deductible, whilst the two women sitting on the case found the opposite.<sup>74</sup>
- 7.90 The presiding chief justice, while not in the end able to justify a work-related deduction under the law, nevertheless found the case a challenging one. He noted that the traditional characterisation of child

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73 *Symes v the Queen* 1993 [Canada], L'Heureux-Dubé J, dissenting report.

74 Young C, 'Taxing times for women: Feminism confronts tax policy', *Sydney law review* (1999), vol 19, viewed on 13 October 2006 at <http://www.austlii.edu.au/au/journals/SydLRev/1999/19.html>.



care expenses as private in nature pre-dated significant numbers of women of child-bearing age entering the workforce:

Proper analysis of this question demands that the relationship between child care expenses and business income be examined more critically.<sup>75</sup>

- 7.91 In his judgement he invoked the legal principle that if expenses arose from personal circumstances rather than business circumstances, then the expense was personal and non-deductible.

There are obvious tautologies within this approach. 'Personal expenses' are said to arise from 'personal circumstances' and 'business expenses' are said to arise from 'business circumstances'. But, how is one to locate a particular expense within the business/personal dichotomy?

- 7.92 As an example of this difficulty, Chief Justice Lamer cited an earlier case from the Canadian Federal Court, where the presiding judge had concluded that a taxpayer had used good business and commercial judgement in using child care to enable her to take paid work. 'The decision', he had said:

... was acceptable according to business principles which include the development of intellectual capital, the improvement of productivity, the provision of services to clients and making available the resource which she sells, namely her time.<sup>76</sup>

- 7.93 In concluding his judgement, he took the step of saying that the law should be changed to take account of the evidence the court had heard.

We propose to permit deduction of the child care expenses that face many working parents today. The problem of adequately caring for children when both parents are working, or when there is only one parent in the family and she or he is working, is both a personal and a social one. We consider it desirable on social as well as economic grounds to permit a tax deduction for child care expenses, under carefully controlled terms [i.e. for work-related child care only].<sup>77</sup>

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75 *Symes v the Queen* 1994 [Canada].

76 Federal Court, Trial Division 1989 3 FC 59 (Cullen J) [Canada], cited in *Symes v the Queen* 1994 [Canada].

77 *Symes v the Queen* 1994 [Canada].

- 7.94 Australian courts have been less forthright in airing ambiguities in this question of child care expenses. In his judgement of 1972, Justice Mason noted some tensions in the legislation, although he did not speculate on how they had arisen, and how the distinction of 'work-related' and 'private' expenses might have been made more complex by the fact that the appellant was a single working mother:<sup>78</sup>

I express no opinion on the question whether an expenditure which is incurred in gaining or producing assessable income may nevertheless be of a 'private' or 'domestic' nature.

- 7.95 Justice French, in his judgement for *Hyde v FC of T* 1988, went further:

It is evidently the fact, and is accepted by the Commissioner, that the taxpayer's expenditure on child minding was necessary to enable him to undertake the employment from which he derived his assessable income... One can accept that the taxpayer may well feel some sense of grievance at the fact that the expenditure cannot be claimed as a deduction, but as the courts have said on occasions before today, the answer to that grievance will not be found in the courts but in changing the law and that is a matter for the legislature.<sup>79</sup>

- 7.96 The committee notes that the courts have, in previous cases, changed their minds on their interpretation of the law and have reversed long-entrenched policy positions. An example is *Ha and Hammond v NSW* 1997 in the High Court of Australia, which overturned previous findings on the definition of excise duties and led to the dismantling of state taxes on fuel, alcohol and tobacco worth billions of dollars.
- 7.97 The best solution, however, is for legislators to take responsibility for clarifying the status of child care, and acknowledge it as an expense legitimately and necessarily incurred in the 'business' of earning an income. The courts have invited the legislature to take this course of action, and the committee believes that it should be undertaken.

## Benefits of a tax deduction for child care

- 7.98 Offering families a tax deduction would acknowledge child care as a legitimate cost of working, and would align government expenditure in this area more closely with workforce participation outcomes. This is consistent with OECD recommendations that Australia's child care

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<sup>78</sup> *Lodge v FC of T* 1972.

<sup>79</sup> *Hyde v FC of T* 1988.

assistance be made more conditional on employment.<sup>80</sup> By giving a benefit proportional to the marginal tax rate of the worker, a tax deduction would actually give an incentive for increased participation in the workforce, as it would reward parents by returning to them some of their own hard-earned income which would otherwise go to government revenue.

- 7.99 Certainly, the individuals who gave evidence to the committee in favour of a tax deduction saw government expenditure on child care not as a welfare payment but as an investment for workforce participation. Many parents, and especially mothers, are keen to use their skills, experience and talent in society at large:

I am asking... that you give long and hard consideration as to how the tax system can help families with their child care costs. Why can you not consider making child care (and that includes nannies) tax deductible? Can't you see that meaningful support like that will enable an army of qualified, enthusiastic and capable women to return to the workforce?<sup>81</sup>

It would make a big difference to us as a family if child care costs could be claimed as a tax deduction. Child care costs are a work related expense. I would not have to use child care if I did not have to work. I do not mind paying tax as I believe we all need to contribute to pay for the community and social structure that we have, however, I believe that as child care is primarily used to support working parents it should be seen as an expense incurred because of work and treated as such by our tax system.<sup>82</sup>

The Tax Office's narrow view of the modern world is shameful. This is the 21st century where woman are encouraged to not only be parents but also to have careers and contribute to the economy. It is the century of flexible hours, globalisation and virtual offices. It is the century where Australian women are constantly being encouraged to not only have children to help address the ageing population crisis but also publicly admonished if they don't return to work...

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80 OECD, *Economic survey of Australia 2006* (2006), p 11; see also Jaumotte F, 'Labour force participation of women: Empirical evidence on the role of policy and other determinants in OECD countries' (2003), *OECD Economic studies*, no. 37, p 88.

81 MacDonald E, sub 154, p 2.

82 Langham J, sub 171, p 2.

I would encourage the committee to embrace the 21st century and understand the dilemma facing working women and families who employ nannies and allow these to be legitimate tax deductions. In doing this they may also encourage more women to return to work, either for organisations or to start their own business, thereby contributing even further to the Australian economy.<sup>83</sup>

7.100 Similarly, a single father wrote to the committee:

These last 12 years I have been raising four children and I work at every opportunity I can. There are a few reasons I don't work now mostly related to raising my kids. One thing which would be of a great help to me and most probably others was if employing a live in nanny could be regarded as a legitimate work-related tax deduction.<sup>84</sup>

7.101 The South Australian Premier's Council for Women also made a submission to the inquiry urging that a tax deduction for child care would offset the costs of working for parents, and would be an incentive in encouraging their participation in the workforce.<sup>85</sup>

7.102 The comments above, of course, also incorporate a plea for flexibility in the type of child care costs considered as legitimate deductions. The committee considers that if such a deduction were to be implemented, it should include in-home care, consistent with its findings from chapter six about the need to recognise a more flexible range of child care options to suit contemporary workers.

7.103 Also following on from the previous chapter, a tax deduction that included in-home care would further assist with the fight to legitimise the nanny industry and reduce the size of the black economy. Parents claiming tax deductions would need to provide the tax file numbers (TFNs) or Australian business numbers (ABNs) of their child care providers, and so would have a strong incentive to make sure that they are hiring a carer who is registered and qualified. Parent employers would withhold a small amount of withholding tax which they would then remit to the Australian Taxation Office.

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83 Moulder A, attachment to The Elite Nanny Service, supplementary sub 157, p 4.

84 Richards P, sub 170, p 1.

85 South Australian Premier's Council for Women, sub 67, p 13.

## Ensuring a fair distribution of assistance

- 7.104 The most common criticism of proposals to make child care tax deductible - or to expand salary sacrificing for child care - is that it will only benefit high income earners paying higher marginal rates of tax. The question is one that the committee has considered seriously.
- 7.105 Government policy has been to target family assistance for low to medium income earners, and over the last decade this has successfully raised the real disposable income levels of many families. Table 7.1 shows increases in real net tax thresholds for families since 1996-97; or rather, the level of private income at which income tax paid first exceeds cash benefits received. A dual income couple with two children, for example, are now earning over \$50,000 before they begin to pay any tax:

**Table 7.1** Increases in real net tax thresholds for families, 1996-97 to 2006-07

Family type	Real net tax threshold		
	1996-97	2006-07	Per cent change
Sole parent	\$34,594	\$48,065	38.9
Single income couple with children	\$34,021	\$48,065	41.3
Dual income couple with children (75:25 split)	\$34,650	\$51,829	49.6
Dual income couple with children (60:40 split)	\$34,749	\$50,910	46.5
Dual income couple with children (67:33 split)	\$34,703	\$51,808	48.1

*Source* Budget paper no 1, 2006-07 Federal Budget, Statement 5: Revenue, Table B1, p 5-26. Dollar amounts are calculated in 2005-06 prices. Families are assumed to have two children – one aged three years and the other aged eight years. The numbers in brackets represent the wages of each working adult in the family, expressed as a proportion of average weekly ordinary time earnings for full time employees (AWOTE).

- 7.106 Given increasingly generous assistance to low and middle income families, the committee considers that there is a need to acknowledge higher income earners as the biggest contributors to income tax collected by the Australian Government. Their tax contribution funds, in part, the assistance received by many other families.

- 7.107 As Sinclair Davidson writes:

When rhetoric is swept aside and taxation data is examined more carefully, evidence shows that, contrary to popular belief, it is relatively high income earners who are paying the lion's share of personal income tax.<sup>86</sup>

<sup>86</sup> Davidson S, 'Who pays the lion's share of personal income tax? (2004)', *Perspectives on tax reform*, no 4, Centre for Independent Studies, p 1.

- 7.108 For the 2003-04 income year, the last year for which tax return data is available from the Australian Taxation Office, 50 per cent of personal income tax - or \$47.8 billion - was collected from the 14 per cent of taxpayers who were in the top marginal bracket.<sup>87</sup> While this distribution may have been flattened somewhat by structural tax cuts announced in the 2006-07 Budget, there is no doubt that tax paid by higher income earners represents a proportionally significant contribution to government revenue.
- 7.109 Higher income earners who pay the most tax can only receive any real assistance for child care by way of salary sacrificing, which as this chapter shows, is limited to the elite echelons of the public service and employees of a handful of large corporations.
- 7.110 Giving workers a tax concession for child care expenses would acknowledge the economic contribution made by personal income tax dollars, and give back to these workers some of what they have earned through their own exertions. It acknowledges that in a competitive global economy, Australia cannot afford to lose some of its most highly-educated and highly-skilled workers to parenthood or caring responsibilities.
- 7.111 Furthermore, the committee believes that tax measures for child care may be useful to employees across a broad range of income strata. Professor Peter McDonald of the Australian National University argued that, combined with policy initiatives to ensure a basic level of equity of benefit, salary sacrificing was not necessarily discriminatory:
- Salary sacrificing could be extended to right across the range of incomes. I think it could be beneficial to those on lower incomes as well.<sup>88</sup>
- 7.112 Similarly, Aegis Consulting told the committee that being able to pay for child care with pre-tax income, either through salary sacrificing or a tax deduction, would be expected to make it attractive for many more women to want to participate in the workforce:
- We would not lose all those women in that bracket between about \$20,000 and \$50,000 per year, who are sitting at home because it is not worth going to work.<sup>89</sup>

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87 The Treasury, *Pocket brief on Australia's tax system* (2006), viewed 10 August 2006 at <http://www.treasury.gov.au/contentitem.asp?NavId=002&ContentID=866>.

88 McDonald P, transcript, 15 February 2006, p 2.

89 Tranent A, transcript, 22 July 2005, p 23.

- 7.113 Modelling shows, however, that some families would not receive a benefit from a tax deduction for child care which is superior to the current system of Child Care Benefit and Child Care Tax Rebate.
- 7.114 Accordingly, the committee recommends that the Child Care Benefit and Child Care Tax Rebate be retained. A choice should be afforded to working parents to opt for the Child Care Benefit and Child Care Tax Rebate, or to claim work-related child care costs as a tax deduction, either by way of a claim through their annual income tax return or by salary sacrificing.
- 7.115 In this way, no-one will receive any less than they do presently, but those who are producing more will benefit to a greater extent by keeping some of their own earned income.
- 7.116 Ultimately, under the committee's proposed model, families will have the responsibility of choosing which form of assistance best suits their needs. Parents who have provided evidence to the committee have a high degree of awareness of what they think their options should be. These families want to exercise choice about how they organise their work and family life.

#### **Recommendation 16**

- 7.117 **The existing Child Care Benefit and Child Care Tax Rebate be retained.**

**A choice should be afforded to working parents to opt for the Child Care Benefit and Child Care Tax Rebate, or to claim work-related child care costs as a tax deduction, either by way of a claim through their annual income tax return or by salary sacrificing.**

#### **Recommendation 17**

- 7.118 **The *Income Tax Assessment Act 1997* be amended to allow child care expenses incurred for the purposes of earning assessable income to be a tax deduction in the hands of the parent taxpayer who incurs the expenses.**

**A tax deduction shall only be claimed for the days of work on which the taxpayer can demonstrate that the care was necessary in order for them to work.**

**A tax deduction between parents in a couple family shall be apportioned between them in proportion to income earned by each.**

**Any unused portion of the tax deduction shall not be transferable between spouses.**

**Where a taxpayer elects to claim a tax deduction for child care expenses, Child Care Benefit and the Child Care Tax Rebate shall not be payable.**

**Where a taxpayer elects to claim the Child Care Benefit and Child Care Tax Rebate, a tax deduction shall not be available.**

## **Note for implementation**

- 7.119 An unintended side effect of introducing tax deductibility for child care costs would be flow-through effects for the Family Tax Benefit and Child Care Benefit income tests. Any reduction in taxable income reduces the income base used to test these payments. In order to prevent distortion, the tax deduction would be disregarded for the purposes of Family Tax Benefit and Child Care Benefit income tests. These income tests are already based on Adjusted Taxable Income (ATI), rather than actual taxable income, for exactly this reason. Adjusted Taxable Income takes into account things such as deductible child maintenance expenditure, tax-free pensions or benefits, and net rental property losses, so that families do not receive more or less than they were intended to receive through inflation or deflation of their taxable income.<sup>90</sup>

## **Conclusion**

- 7.120 In the preliminary stages of drafting this report, the committee commissioned Econtech, a modelling firm, to cost proposed changes to child care support. The first model put to Econtech was to replace the Child Care Tax Rebate with a general tax deduction and to make all employer-provided child care exempt from fringe benefits tax. Econtech calculated the net cost to the Australian Government of this proposal at \$218.5 million annually (in addition to current outlays). However, Econtech also found that low income earners would decrease the number of hours they worked under this new system

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<sup>90</sup> Australian Government, *Family Assistance Guide* (2006), version 1.82, section 3.2.1, viewed on 24 November 2006 at [http://www.facs.gov.au/guides\\_acts/fag/faguide-3/faguide-3.2/faguide-3.2.1.html](http://www.facs.gov.au/guides_acts/fag/faguide-3/faguide-3.2/faguide-3.2.1.html).



and would be worse off.<sup>91</sup> Accordingly, the committee has not put this proposal forward as a recommendation.

- 7.121 Following this analysis, Econtech was asked to model the cost of a second proposal, which is reproduced in the recommendations of this report. However, Econtech modelled a slightly different proposal due to time constraints and the fact that the cost data published in the Australian Bureau of Statistics' Child Care Survey is net of Child Care Benefit (rather than showing both the amount of Child Care Benefit received and what the child care provider initially charged).
- 7.122 The second proposal modelled by Econtech was the same as the recommendations in this report, except that the tax deduction had some elements of the Child Care Tax Rebate, for example it was applied to a family's child care costs net of the Child Care Benefit. Although this is slightly different to the recommendations in this report, the committee is confident that the estimates provide a useful indication of the costs of its proposals. Econtech estimated that this second proposal would have a net cost to the Australian Government of \$262 million annually.<sup>92</sup>
- 7.123 In the context of other government programs, such as Family Tax Benefit Part A (\$12.3 billion annually), Family Tax Benefit Part B (\$4.1 billion annually) and the Child Care Benefit (\$1.6 billion annually), spending \$262 million annually to improve flexibility in child care delivery is good value for money. The committee's proposals are affordable and the committee believes a significant number of Australians would be better off if they were implemented without delay.
- 7.124 The cost to revenue identified should be regarded as an investment to stimulate greater full time female participation, particularly targeting tertiary-qualified mothers to rejoin the full time workforce. As the committee's research has shown, the majority of today's university graduates are women, and the choices they make about work and family will make a difference to our national prosperity. These women will make up an increasing proportion of the workforce in the future, with total women graduates in the workforce likely to outnumber male graduates in the decades to come.<sup>93</sup>

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91 Econtech, Appendix E, p 20.

92 Econtech, Appendix E, p 23.

93 Trends in human capital distribution are detailed in chapter one.

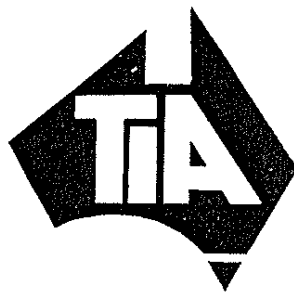
- 7.125 In light of the Access Economics report at Appendix D, showing potential gains of increased female participation in full time work of between 2.9 and 4.4 per cent of national income, it is in the national interest to implement the recommendations made.

### **Additional comments by the Hon Alan Cadman MP**

- 7.126 A crucial principle established in this report is that all parents should be able to claim some tax relief for sharing their incomes with their young dependent children. Greater emphasis and higher allowances should be given to children under the age of five, even though older children on balance 'cost more', as parents can more easily manage their work/home responsibilities once children reach school age.
- 7.127 The present Child Care Rebate is limited to \$4,000 for formal child care. Child care needs to be extended to as wide a range of services as possible. The rebate currently limits the type of child care. By providing support through the Family Tax Benefit, choices can be expanded and the options of using grandparents, relatives, in-home care and other types of child care become accessible. An increase to the Family Tax Benefit (Part A) by \$4,700 for each child under five would give families the opportunity of choosing the type of child care which is best suits them, and counteracts high effective marginal tax rates. No longer would it be a matter for the goodwill or generosity of the employer or the family making a decision to salary sacrifice.
- 7.128 Expensive child care is not available to everybody, nor do all parents endorse the use of centre-based care as the best means of caring for their young children. The registration of informal care will help reduce the prospect of abuse but continue to give parents choice. Once a real choice is available for parents, then work participation and family satisfaction both increase.
- 7.129 These changes would cost approximately \$1.7 billion but with other options escalating in cost, together with the complex administration involved, it provides a realistic and practical alternative to some of the proposals put forward by those giving evidence to this committee. Under this proposal, recommendations 14 and 15 would become superfluous as families would have additional resources, by way of the Family Tax Benefit (Part A), to use on the child care of their choice.

## Annexure C

**TAXATION INSTITUTE OF AUSTRALIA**



**TAXATION AND CHILD CARE**

**A Submission to the Commonwealth Government  
proposing changes to the tax treatment of  
child care expenses**

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Ms Yolanda Lee - National Council of Women

Ms Lillian Leseur - Employers Federation of NSW

Ms Sandra Triulzi, Manager, Recruitment and Equal Employment Opportunities - Westpac Banking Corporation

Dr Neil Warren - Warren Ventures Pty Ltd

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**AN EVALUATION OF THE TIA PROPOSAL FOR CHANGES  
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## Executive Summary

Currently in Australia, the only taxation relief available for expenditure on child care is granted to employers under the Fringe Benefits Tax Assessment Act 1986 (FBTAA) for expenditure on certain eligible child care facilities and contributions for the allocation of places for employees' children in those centres. There is no taxation relief provided to individuals in relation to child care expenditure which may be incurred to enable those taxpayers to earn assessable income.

This situation should be compared to the position in many overseas jurisdictions, which, by recognising that relief is appropriate, are far more generous in their treatment of allowable child care expenditure for tax purposes under their relevant income tax legislation, as well as having a more generous interpretation of what is allowable child care. For example, in the United States, a taxpayer is allowed a tax credit equal to 20% to 30% of the amount paid for household services and for expenses for the care of a "qualifying individual" and in Canada, a deduction is allowed for child care expenses incurred for the care of an eligible child up to a maximum dollar amount. Also, in New Zealand, a taxpayer who pays for the services of a housekeeper is entitled to a tax rebate.

The Institute submits that the Commonwealth Government should follow the lead of these overseas jurisdictions in allowing some form of tax benefit to working parents incurring child care expenses. The present lack of relief in the form of a tax deduction or rebate entitlement, discriminates against families and individuals who incur such expenditure, as the present tax system ignores the fact that child care costs are a legitimate income earning expense. The Institute, however, recognises that the Government's substantial fee relief scheme provides significant benefits and to this end the Institute's proposals are designed to supplement the existing scheme.

The major recommendations by the Taxation Institute are for:

1. An amendment to the Income Tax Assessment Act 1936 (ITAA) to allow a deduction up to a maximum limit of \$120 per week per child, indexed, for child care expenditure which demonstrates a strong nexus with the derivation of income earned by working parents.

2. Alternatively, an amendment to the ITAA to allow a rebate based on maximum expenditure of \$120 per week per child, indexed, for child care expenditure which demonstrates a strong nexus with the derivation of income earned by working parents.
3. The definition of eligible child care subject to either a deduction or a rebate, should be extended to cover care both within and outside the taxpayers' home and extend the definition of eligible persons for whom care can be provided.
4. An amendment to the ITAA to allow an income tax deduction for donations to organisations to assist in their work in setting up child care facilities.
5. An amendment to the FBTA so that all contributions made in relation to child care expenses, whether made directly to a child care centre or whether paid as part of a salary package, are exempt benefits.
6. An amendment to the Sales Tax legislation to recognise that approved child care centres perform an educative role and therefore should be exempt from the imposition of sales tax.

In Part B of the Taxation Institute's Submission, there is a detailed costing of the various proposals recommended by the Institute. It is evident from this costing, that in the short term the cost to the Government of the proposals is relatively minimal. In fact, in the medium to longer term, the Government will substantially benefit from the proposals suggested. This is because the proposals encourage increased hours of work and increased entry into the workforce by presently non-income earning parents, and thus the initial cost of the concession will be likely to be overwhelmed several times over by the increase in personal income and indirect tax collections and subsequent reductions in social welfare payments. This is clearly evidenced in the findings set out in Part B of the Submission.

In the short term, the maximum cost to Government is estimated as follows:

- A. in the case of the deduction of up to \$120 per week per child, \$143 million annually;
- B. in the case of a 20% tax rebate based on maximum expenditure of \$120 per week per child, \$89 million annually; and

- C. in the case of an extension of FBT exemption to all contributions made relating to child care expenditure, it is concluded that the cost is likely to be insignificant. However, even assuming a 100% take-up, the maximum cost would not exceed \$162 million.

However, as has been previously mentioned, the longer term effects of allowing a deduction or rebate for child care expenses or granting an extended FBT exemption, would in fact be revenue positive for the Government. The estimated fiscal impact of allowing a rebate based on maximum expenditure of \$120 per week per child, which is assumed to result in a 10% increase in participation in the workforce by non-earning parents, will result in an estimated annual revenue gain of \$739 million to Government.

# THE TAXATION INSTITUTE PROPOSAL FOR CHANGES TO THE TAX TREATMENT OF CHILD CARE EXPENSES

## 1.0 Introduction

Child care is no longer an elitist issue, but one of increasing importance for many employers and unions, especially since the number of women participating in the workplace has expanded dramatically in the last ten to fifteen years to more than 40% of the total workforce.

The treatment of child care expenditure incurred by working parents under the present taxation system is inequitable. The lack of relief in the form of a tax deduction/rebate entitlement discriminates against families and individuals who incur such expenditure, as the system ignores the fact that child care costs are a legitimate income earning expense.

This Submission urges the Government to introduce measures to provide much needed tax relief in the area of child care.

It is envisaged that the recommended tax measures be integrated with the prevailing system of fee relief, and would enable an allowable deduction or rebate to be claimed in respect of child care costs incurred by working parents.

## 2.0 The Need for Tax Reform

### 2.1 Changes in Social Attitudes and Expectations of a Woman's Role in Society as reflected in Government policy

Changing attitudes in society as to what a woman's role should be have been reflected in the measures adopted by the Commonwealth Government in the past few years. For instance, the introduction of anti-discrimination and sexual harrassment legislation reflects a policy of equality for both men and women in the workforce.

The Commonwealth Government, in March 1990, ratified Convention No. 156 of the International Labour Organisation which is directed at improving the position of workers with family responsibilities. Article 1 of this Convention states that men and women workers with responsibilities for dependant children or other family members in need of their care or support, should not be prevented by those obligations from either preparing for, entering, participating in or advancing in economic activity. Article 3 is even stronger in that it seeks to make it an aim of national policy of signatories to prevent discrimination against those wishing to work, and, insofar as it is possible, to enter employment without conflict with their family responsibilities. As a signatory to this Convention, the Commonwealth Government has effectively committed itself to a policy of actively encouraging methods of assisting employees to undertake family responsibilities without those responsibilities impinging on their ability to participate in the workforce. Obviously, the encouragement of some form of child care is one aspect of this increased role of Government.

Consequently, a Work and Family Unit has been established within the Department of Industrial Relations to liaise with various State and community bodies on the needs of workers with family responsibilities.

The establishment of the Office for the Status of Women and the introduction of the 1986 Affirmative Action legislation in order to implement the Government's policy of equality between the sexes reflects society's attitude that men and women should be treated equally in all aspects of life. The Australian economy can no longer function without women playing a major role in the workforce. Women are **expected** to be active members of the workforce and many find it a financial necessity to work. Community standards and expectations in relation

to working women have changed dramatically.

The Government also has been active in increasing the numbers of women in the workforce via the establishment of the Affirmative Action Agency to monitor and evaluate progress and outcomes of the legislation within private sector organisations.

The Federal Opposition announced that they would introduce a child care rebate system as the first step towards full tax deductibility for child care expenses in the time leading up to the May 1990 election.

There is, therefore, obviously strong community support for the Government to take proactive steps in relation to child care.

## 2.2 Fee Relief and Government Grants and Subsidies

The Institute recognises the positive steps taken by Governments in introducing a number of initiatives to meet the growing demand for child care. These initiatives have generally been by way of direct grants to registered child care centres and fee relief schemes. The recommendations made by the Institute would be intended to work in conjunction with these measures and are not intended to replace them. See further Appendix II.

The amount contributed by families for child care under the present fee relief scheme is based on the assessed family income which is the gross family income minus a \$30 allowance for each dependant child. Those with an assessed family income of up to \$340 per week pay \$15 per week for child care for one child and \$17 for two or more children. When the assessed family income is more than \$340 per week, the minimum fee increases by 12c/\$1 for a single child and 20c/\$1 for 2 or more children. Fee relief ceases once assessed family income exceeds \$1048 per week (where one child is in care) or \$1260 (where 2 or more children are in care).

In addition to direct fee relief, grants and subsidies provided by Government result in an effective reduction in fees charged by registered centres by \$15 per week.

The present fee relief subsidy coupled with direct grants cost the Commonwealth Government \$245.7M in 1990/91 and is estimated to cost \$375.3M in 1991/92.

With maximum benefits reducing once gross family income exceeds \$20,866 it is obvious, however, that it is



predominantly aimed at benefitting single income families. Consequently, in households where both parents are working, the combined family income would, in most situations exclude any form of fee relief from being available.

Note: In the 1991-92 Budget, a number of improvements were announced to this system of fee relief, which are set out in some detail in Appendix B of Part B of the Submission.

## 2.3 Empirical Evidence - The Consequences of a Lack of Appropriate Tax Measures

Notwithstanding the measures taken by the Government in relation to providing relief measures for child care, there are obviously still problems existing which need to be considered.

### 2.3.1 Disincentive to Work

Women are not motivated to actively seek employment because the high cost of child care will negate the financial rewards of employment.

A survey by the Australian Bureau of Statistics in September 1990, found that 19% of non-earning women stated that their main reason for not seeking work was the non-availability of suitable child care facilities as compared with 12% in September 1986. Of these women 48% stated that the cost of child care was prohibitive. The high cost of child care coupled with the lack of places in existing centres further exacerbates the disincentive effect.

### 2.3.2 Inability to work due to family commitments

In the absence of child care assistance or private arrangements, one family member will invariably be required to stay at home to care for the children. For historical and social reasons, it has usually been the female responsible for this role in the past.

A survey conducted in September 1979 found that 14.5% of females who were responsible for children under 6 years of age wanted a job if child care was available.

A similar survey undertaken in September 1982 on discouraged job seekers found that 16.5% of females who were not in the labour force and who were responsible for children under 6 years of age wanted a job if child

care was available.

### **2.3.3 Participation in Workforce**

In June 1990 women comprised 42% of the labour force compared to 1961 when they comprised only 25% of the workforce. Over the same period, the proportion of married women in the labour force rose from 17% (in 1954) to 53% (in 1990). In the decade 1980-1990, the participation rate of all women grew by 8%, for married women, 11% and for men, it fell by 3%.

A total of 43% of all women and 41% of all men in the labour force have dependant children and, of these parents in the labour force, 17% of men and 13% of women have children under 4. (Per ABS Labour Force)

### **2.3.4 Result of Change in tax Treatment of Child Care Expenses**

Part B of the Submission, in particular Part V entitled "Sensitivity Analysis of the Potential Behavioural Response of Families to a System of Tax Deductions/Rebates" discusses the positive effect on participation rates in the workforce from a change in the present tax treatment. In particular, Table 9 sets out the gains to Government accruing from this resulting increase in participation in the workforce. In particular, if it is assumed that there is only a 10% increase in participation by women with dependants under 5 in the workforce, the result will be a substantial revenue gain to the Government amounting to \$739 million.

### 3.0 The Current Tax Treatment of Child Care Expenditure in Australia

#### 3.1 Tax Deductibility

There is no specific provision in the ITAA that allows a deduction for child care expenditure incurred by a working parent.

In seeking to obtain an income tax deduction for child care expenditure, a taxpayer must rely on the general deduction provision; section 51(1) of the ITAA.

Section 51(1) allows a deduction for losses and outgoings incurred in gaining or producing assessable income. Alternatively, a deduction is allowable under the section where a loss or outgoing is necessarily incurred in carrying on a business for the purpose of gaining or producing such income.

However, a deduction is not allowed under the section to the extent to which the loss or outgoing is an outgoing of capital, or is of a private or domestic nature, or is incurred in relation to the gaining or production of exempt income.

The Australian Taxation Office ("ATO") has consistently denied a deduction under section 51 to working parents in relation to child care expenditure incurred to enable the parents to pursue income producing activities. This is so notwithstanding a strong nexus between the expenditure incurred and the resultant increase in income earned by the parent.

For instance, in the ATO's Income Tax Ruling, IT 2331 - "Income Tax: Deductions Allowable to Members of Parliament", the Commissioner of Taxation states that a deduction will not be allowed to Members of Parliament for child care expenses incurred to enable an MP to attend his/her electoral or party functions. Such expenditure is considered to be of a private or domestic nature. The Commissioner has taken this view notwithstanding that it is a requirement of office for many MPs to spend time away from home to carry out parliamentary duties and the child care expenditure sought to be claimed as a deduction is incurred to enable the MP to perform those duties.

The courts and tribunals have supported the ATO's stance in denying a deduction for such expenditure. They have

consistently held that child care expenditure:

- . is not incurred in the course of gaining or producing assessable income; and/or
- . is of a private or domestic nature.

For instance, in the leading case of Lodge v FC of T 72 ATC 4174, the High Court held that the taxpayer was not entitled to a deduction for fees paid to a nursery school to which her child was sent to enable the taxpayer to carry on her income producing activities as a legal coster. This was so notwithstanding that the expenditure was incurred for the purpose of earning assessable income and was an essential prerequisite to the derivation of that income.

The courts generally look to the essential character of the expenditure itself and not to whether the expenditure is an essential prerequisite to the derivation of assessable income.

In this regard, it is essential that the expenditure be "incidental and relevant" to the gaining of assessable income. In Lodge's case for instance, the Court found that the character of the nursery fees was neither relevant nor incidental to the taxpayer's work (ie. the preparation of a bill of costs).

However, the decision in Lodge's case does not necessarily preclude the deductibility of child care expenses in all instances. In Hyde v. FC of T 88 ATC 4748, Mr Justice French stated that the decision in Lodge was decided on the particular facts of that case, and that it would be a mistake to extend it to "...a statement of general principle that there could never be a situation in which child care expenses are deductible".

Notwithstanding his Honour's comments, a plethora of cases have been brought before the courts in which it has been argued child care expenditure should be deductible under section 51 and have attempted to distinguish the facts of Lodge's case (refer Appendix 1). Invariably, in these cases the argument for deductibility of child care expenditure has failed.

The concept of tax deductibility of child care expenses should be treated independently from other so called "private" expenditure because of the socio-economic costs of the present child care system. Because of the often prohibitive costs of child care, many employees are forced out of productive employment. The consequences of

this are discussed at para 2.3 of this Submission. Perhaps the major concern is the long term cost to employers from a loss of skilled workers.

If, on an after tax basis, child care were to become less expensive, then the adverse consequences discussed at para 2.3 would be substantially lessened.

In the case of other "private" expenditure, currently non-deductible under section 51(1), eg. the cost of food, transport to and from work, the cost of such items does not generally result in the same economic disincentive to work. Consequently, such expenses do not result in the same costs to the Economy. The Institute does not recommend any change to the existing tax treatment of these items.

Jurisdictions such as Canada, NZ and the US now recognise that the payment by a taxpayer of child care expenses is so closely linked to the derivation of assessable income to be an expense deductible in calculating the taxation liability of a taxpayer. In all three jurisdictions, the expenditure must be incurred to enable the taxpayer to derive assessable income or be necessary because of the employment or business activities of both the taxpayer and his or her spouse.

Jurisdictions such as Canada allow a deduction against assessable income whereas in the US and NZ, a rebate is allowed up to a specified maximum. (See 4.1 to 4.3)

#### 3.1.1 Recommendation

The Institute recommends that because the payment of child care expenses is so closely linked to the derivation of assessable income it should be an allowable tax deduction up to a limit of \$120 per week, indexed. The details of this proposal including costing based on an upper dollar limit of \$100 and \$120 per week per child is set out in Part IV of Part B of the Submission.

Any tax deductibility would be intended to supplement the present fee relief system. The proposed method whereby this change to the existing tax system will work is set out in Appendix II.

#### 3.1.2 Limitations on Deductibility

Any change of law allowing for a deduction would only be allowed for expenditure actually incurred. Consequently, no deduction would be available for

"notional" amounts representing, eg, the value of child care carried out by a taxpayer's spouse. Where there is no outgoing of expenditure there can be no deduction claimed.

In addition, a deduction would only be allowable for direct payments for child care, not incidental costs eg. travel, food etc.

Based on the Institute's costing, an upper limit on the tax deduction claimable of \$120 would apply as per Part IV of Part B of the Submission. This figure is recognised by the Institute as representing a realistic upper limit on deductible expenditure even though, as can be seen from Part B, the cost to the Government of an uncapped deduction is not substantial.

Where one spouse is working and there is a spouse at home full time capable of caring for any dependant children, it is not proposed that a tax deduction be allowed to the working spouse for the cost of external child care. This is because the expenditure in such a situation is not necessarily incurred for the purposes of s.51 of the ITAA. The tax deduction would be claimable, in the case of a single parent family by that parent or, in the case of a 2 parent family by the secondary earner (ie. the last parent to enter the workforce).

The definition of child care expenses for which it is proposed that a deduction should be allowed should be more generous than currently exists in the FBTAA. Both the FBTAA and the ITAA should contain a similar provision whereby eligible expenditure includes care both within and outside the family home and the provision of occasional care and emergency care (as is the situation in US, Canada and NZ) and more generous age restrictions. It is noted that the figures in Table 9 of Part B assume a more generous age limit. It is strongly submitted that the concept of care and education should recognise the various stages of a dependant's lifestyle for example:

- . Early childhood
- . School age
- . Elder care
- . Other care (related to mentally and physically disabled dependants)

As previously noted, any change to the law whereby a deduction or a rebate is to be allowed for child care expenditure would be intended to operate in conjunction

with the present fee relief system. In this way, lower income earners would continue to be the major beneficiaries under this important Government initiative. However, under the Institute's proposal, all taxpayers incurring expenditure on eligible child care expenses would be entitled to a deduction.

The proposal results in the reduction of a substantial portion of the "black economy" in the child care area. As with the system in Canada, a taxpayer is required, as a condition to deductibility, to obtain from the recipient of the payment the quotation of their TFN. In this way, all income claimed as a deduction/rebate would be returned as assessable income by the recipient and would result in either additional tax revenues including reduced dependant spouse rebate claims or, alternatively, lower social security payouts where recipients of fees are also in receipt of Government assistance such as pensions or Family Assistance Supplements.

As can be seen from the figures set out in Part B of the Submission, the revenue gains to the Government from such a scheme are likely to be quite substantial.

As well as these direct revenue gains, there will be other economic gains accruing from this proposal, as enunciated at para 5.3.

It should be emphasised that to allow a deduction for such expenditure would not be inconsistent with Government policy under which it is already providing assistance via fee relief since:

- (a) A large number of taxpayers currently incurring child care expenses do not qualify for fee relief, eg, because the assessed family income exceeds the maximum allowable or because their children do not attend an approved child care centre;
- (b) There are numerous examples within the current income tax regime, where a tax deduction/rebate is allowed in addition to Government assistance being granted, eg the medical expenses rebate claimable under section 159(P), which exists alongside the benefits provided under the Medicare and Pharmaceutical Benefits Schemes.

If such expenditure was deductible to an individual taxpayer, it would follow that if an employer paid the expense as part of a salary package, then the benefit provided would not be subject to FBT - see para 3.4.1.

### 3.2 Rebate Entitlement

An outright deduction may be perceived as benefitting higher income earners. However, the Institute is recommending a capped deduction, which is regarded as more equitable. Also, since the Institute regards child care as an employment related expense it should correctly be taken into account in calculating assessable income. However, it is submitted that lower income earners are the major beneficiaries under the fee relief system, leaving the majority of average income earners without government assistance. The allowance of a rebate under Division 17 of Part 3 of the ITAA for expenditure incurred in relation to child care expenses similar to the concessional rebates for "private" expenditure, such as medical and self education expenses could be an alternative to outright deductibility, since under such a system all taxpayers, regardless of their effective tax rate, would be put on an equal footing.

It is mentioend, however, that a practical difficulty exists in relation to rebates in that, where the claimant's taxable income is below the tax free threshold, the benefit of the rebate is effectively lost. This aspect is referred to in Part III of Part B of the Submission.

#### 3.2.1 Recommendation

It is recommended that, as an alternative to outright deductibility of expenses incurred on child care, a rebate based on an upper dollar limit of expenditure of \$120 per week per child (indexed) be allowed. Such a system is in place in US and NZ. The costing of such a proposal (which is \$89 million) is set out in Part III of Part B of the Submission.

The Institute recommends that consideration be given to allowing a transferable rebate which, as shown in Part III of Part B of the Submission, would cost only marginally more than a non-transferable rebate claimed by the secondary earner. This would obviate the practical problem discussed at para 3.2 in relation to claimants with taxable incomes less than the taxable threshold.

The same rules would apply to a claim for a rebate as would apply in relation to deductibility and, therefore, the commentary at paras 3.1.1-3.1.2 above, is equally applicable here.



### 3.3 Donations to Fund Child Care Centres

The high after tax cost of contributions by employers towards the cost of a child care centre or to assist an organisation such as the Kindergarten Union of NSW in establishing centres (due to FBT or non-deductibility) may discourage such expenditures from being made.

No deduction is currently allowed under section 78 of the ITAA for such donations and a deduction would only be allowed under section 51 in the limited situation where the donation results in an increase in business to the donor.

The economic effect of such a proposal is difficult to quantify but would be expected to be minimal. As an example, total donations to the Kindergarten Union of NSW during the 1990 year amounted to some \$20,000 Australia-wide. The effect of tax deductibility for donations to equivalent organisations would not be substantial.

#### 3.3.1 Recommendation

Donations to organisations to assist in their work in research and setting up child care centres should be deductible under section 78 of the ITAA to encourage such contributions to be made.

It is the Institute's understanding that no deduction is currently allowed for donations to community child care centres because their main function is taken to be the care and supervision rather than education of children. This is taking a narrow view of "education" and, given this narrow interpretation, organisations which work in the area of child care should be separately listed under section 78(1)(a).

### 3.4 Present FBT Position

Employers are exempt from FBT for expenses incurred in providing child care to their employees' children where the child care facilities are located on the employer's business premises, ie. premises on which the employer conducts business operations within the meaning of section 47(2) of the FBTAA. The employer is also exempt from FBT on contributions made to secure priority of access for children of employees at an eligible child care centre pursuant to section 47(8) of the FBTAA.

The definition of child care facility under section 136 only exempts benefits provided where the facility is set up to cater for two or more children under the age of 6,

and only if not provided at the child's home. This definition, it is submitted, is too narrow, in that there may well be situations where there are no children under the age of 6 being cared for in such a centre.

The current FBT provisions discriminate against smaller employers for whom the cost of establishing such a facility would be prohibitive. The option of sharing the cost of such a centre among a number of smaller employers may not always be feasible (assuming this practice would be permissible under section 47(2)). Only larger employers can afford to set up and provide child care facilities for their employees. Moreover, "blue collar" employees would be less likely to receive such benefits from their employer.

The current concept of eligible dependants attending child care centres is also arguably far too limited, in that in the case of external centres for which a priority access payment is made, the position of children over the age of 6 who are still fully dependent on a taxpayer and for whom appropriate child care is required is not adequately catered for. Presently, eligible child care centres must be set up to provide care to children, a majority of whom are of preschool age. There is no recognition of the needs of older dependants. The only exception to this is the position of vacation and outside school hours care which by its nature caters for older children. However, this care must be provided on the employer's business premises ie. premises over which the employer retains control and such a centre must satisfy the tests set out in section 136, discussed above. If it is provided in any other form, it will classify as a taxable fringe benefit. The various countries mentioned in Chapter 4, all provide a more generous interpretation of "eligible dependant". In fact, in some jurisdictions such as the United States, a concession is allowed for expenditure relating to adult dependants who, for example, may be mentally or physically incapacitated in some way.

Currently the net FBT cost of child care for a corporate employer on non FBT exempt expenditure of \$100 is \$108. This represents an effective cost net of tax of \$61 plus an FBT cost of \$47. Therefore, it is currently tax ineffective for an employer to provide such non-exempt benefits unless it is provided by way of a salary sacrifice to a taxpayer who is paying tax at the top marginal rate of 47 cents in the dollar. Even in such cases, the saving is only marginal.

#### 3.4.1 Recommendation

The FBTAA should be amended so that all contributions towards the cost of child care for employees' dependants would qualify for the FBT exemption.

Therefore, it would follow that if an employer were to pay the child care fees payable by an employee (eg. as an expense payment fringe benefit) this should also be treated as an exempt benefit for FBT purposes.

Also, the FBTAA should be amended to increase the present age restriction for persons for whom care is provided so that eligible child care covers dependants under the age of 16. For example, the definition in section 159(J) of the ITAA could be adopted.

At Part VI of Part B of the Submission, the cost of expanding the current FBT exemption is discussed further.

#### **3.4.2 Limitations on Extension of FBT Exemption**

It could be made a condition of exemption that the employer had to obtain a quotation of the recipients TFN (as is the case in Canada - see para 4.3).

It may be appropriate to apply a cap on benefits for which exemption will apply, similar to that proposed for the deduction or rebate, although the cost to revenue of providing such an exemption without a cap is insignificant.

It is envisaged that FBT exemption would operate in addition to any deductibility or rebate.

#### **3.5 Sales Tax Anomaly**

Unlike pre-schools, child care centres are not exempt from the imposition of sales tax. This is because such centres are not considered to be "educational". In the Institute's view, it should no longer be accepted that such centres do not perform an educational role.

##### **3.5.1 Recommendation**

It should be recognised that approved child care centres do perform an educative role in the community and this should be reflected in their classification for sales tax purposes.

## Summary of Recommendations

- . The ITAA be amended to allow a deduction up to a maximum limit of \$120 per week per child, indexed, for child care expenditure which demonstrate a strong nexus with the derivation of income earned by working parents;
- . Alternatively an amendment to the ITAA to allow a rebate based on maximum expenditure of \$120 per week per child, indexed, for child care expenditure which demonstrates a strong nexus with the derivation of income earned by working parents.
- . Any deduction or rebate would be intended to work in conjunction with the present fee relief system so that lower income earners will still be the major beneficiaries under that subsidy system.
- . The definition of eligible child care subject to either a deduction or a rebate should be extended to cover care both within and outside the taxpayers home and extend the definition of eligible persons for whom care can be provided.

- . The ITAA be amended to allow an income tax deduction in respect of donations to organisations to assist in their work in setting up child care facilities;
- . The FBTAA be amended so that all contributions made in relation to child care expenses whether made directly to a child care centre or whether paid as part of a salary package, are exempt benefits; and
- . The sales tax legislation should be amended to recognise that approved child care centres perform an educative role and therefore should be exempt from the imposition of sales tax.

## 4.0 Towards A Level Playing Field - A Comparison With Other Tax Jurisdictions

### 4.1 United States

In an attempt to encourage non-working parents to enter the workforce, the US Congress has provided tax relief measures in relation to child care expenditure. A taxpayer who maintains a qualified dependant (a child under 13 years of age or any physically or mentally incapacitated dependant or spouse) is entitled to claim a tax credit which cannot exceed total income tax liability. This credit is equal to the applicable percentage of the employment related child and dependant care expenses paid by the individual during the tax year. Employment related expenses include expenses for household services and the care of a qualified individual to enable the taxpayer to be gainfully employed or be able to seek employment. Household service expenses include those paid for the ordinary and usual services of maintaining a household and that are attributable in part to the care of the qualifying individual eg. a maid or cook.

Care provided outside the home, such as expenses incurred at external dependant care centres and nursery schools, also qualifies for the credit.

The maximum credit is 30% of expenses for taxpayers on an adjusted net income of up to \$US10,000 reducing by 1% for every additional \$US2,000. Where adjusted net income exceeds \$US28,000 the maximum credit is 20%. In addition, the maximum amount of expenditure entitling a taxpayer to a credit is \$US2,400 (where one qualifying individual) and \$US4,800 (where 2 or more qualifying individuals).

Further assistance to working parents has been provided since 1981, whereby employers have been encouraged to establish qualified dependant care assistance plans. Employers are able to claim deductions for the costs of the plans and the employee in calculating taxable income excludes from his/her gross income the value of any benefits received under the plan (to the extent that the benefit qualifies as child and dependant care expenses incurred to enable the taxpayer to be gainfully employed) up to a maximum of \$US5,000 in a tax year. The amount of any employment related expense in child and dependant care in calculating the credit available to an employee must be reduced by any benefit received by an employee

under an employer provided plan that was not included in gross income under this provision.

No credit can be claimed unless the taxpayer reports on their tax return details including the taxpayer identification number of the dependant care provider.

#### 4.2 Canada

In Canada, a deduction is allowed under section 63 of the Income Tax Act (Can) for child care expenses incurred for the care of an eligible child, ie. a child of the taxpayer or the taxpayer's spouse or a child dependant on the taxpayer, under the age of 14 or who has a mental or physical disability. The maximum deduction is \$C4,000, for each child under the age of 7 or with a severe mental/physical impairment, with up to \$C2,000 per year, for each additional eligible child.

A child care expense is any expense incurred for the purpose of providing for any eligible child of the taxpayer, child care services including baby sitting, day nursery or services provided at a boarding school or camp, if those services were provided to enable the taxpayer to perform duties of employment, carry on a business or undertake a course of study or research for which an allowance is received.

The recipient of the payment can be connected to the taxpayer by blood, marriage or adoption and the only proviso is that documentation to support the expenditure must be provided and any individual payee's Social Insurance number must be quoted.

#### 4.3 New Zealand

Under New Zealand tax law, a taxpayer who pays for the services of a housekeeper is entitled to a tax rebate. The rebate is calculated on payments made by a married but not separated taxpayer to a person or institution for the care of the taxpayer's child, either inside or outside the family home, where the services are necessary because of the employment or business activities of both the taxpayer and his or her spouse. The amount of the rebate is the lesser of \$NZ310 or one third of all qualifying payments.

#### 4.4 United Kingdom

Under the British tax legislation from 6 April 1990, the "cash equivalent" of the benefit of workplace nurseries or play schemes provided by employers for employees is

excluded from the calculation of assessable income to employees subject to tax on benefits received. This exemption extends to nurseries run at the workplace or elsewhere and to those run jointly with other employers or local authorities. It covers facilities provided by employers for older children after school or during school holidays.

The exemption only applies where:

- . the employee has "parental responsibility" for the child, resides with the child, or maintains a child or stepchild;
- . the care is provided on premises which are not wholly or mainly used as a private dwelling;
- . either the care is provided on premises which are made available by the employer alone, or the care is provided under arrangements made by persons who include the employer and which make him at least partly responsible for financing the provision of care; and
- . in circumstances where the premises and care given are registered under the relevant Acts.



## 5.0 Compatibility of Tax Reform With Government Social and Economic Policies

### 5.1 The Effects of Proposed Tax Treatment

Should the proposed tax treatment be introduced in respect of child care expenses, direct productivity increases within the economy may result.

Taxpayers who were previously prevented from working because of the high cost of child care, will now be able to seek employment without the resulting income being dissipated by the high after tax cost of child care facilities. As a result, reliance on Government funding (ie. unemployment or single parent benefits) should fall.

This is evident from the discussion of the sensitivity analysis at Part V of Part B of the Submission.

The costing analysis described in Part B demonstrates the significant potential revenue gain flowing from allowing the proposed tax treatment for child care expenses.

The proposed tax treatment of child care expenses is likely to create a demand for the provision of child care facilities which may then be satisfied by private organisations which will in turn stimulate employment in the Economy. This would also alleviate one of the other major problems facing employees in relation to child care ie. the availability of child care places.

Productivity should also increase as absentee days of working parents would decline as a result of children being adequately cared for, particularly if emergency or sick care were to be recognised as part of "eligible child care". Further, non-earning parents may be enticed to return to the workforce at an earlier stage and the necessity to replace women leaving the workforce to have children may be reduced as such women may return to their former jobs after a relatively short period of time. Employers, and consequently the community as a whole, will thus be able to reduce the costs associated with employing and training new workers.

### 5.2 Consistency with Government Policy

The Government has vocally supported equal opportunities for women in the work place. An Equal Opportunity Board has been established so that claims of discrimination may be dealt with. Whilst penalties for discrimination have

been enacted, the Government is still in effect discriminating against working mothers. By not allowing a deduction or rebate for child care expenses mothers are effectively being forced by the Government to remain at home to care for their children. By allowing a deduction or rebate for child care expenses, working mothers will be given a better chance to return to the workforce.

### 5.3 Other Economic Benefits

Other economic benefits which may flow from the introduction of tax reform measures include:

- . greater opportunities for home work for child care workers, as parents would be able to afford to employ them to care for children within the family home;
- . reduced need for social security support, as part-time employment opportunities for child care workers will increase; and
- . Increased revenues should arise from increased participation in the workforce by primary carers and by those involved in the care of children returning as assessable income the fees received by them.

Taxation Institute of Australia

13 November 1991

## APPENDIX 1 - Cases on Non-Deductibility of Child Care Expenses

A number of child care cases brought before the courts have argued for the deductibility of such expenses and have attempted to distinguish the facts of Lodge's case.

In Case J70 77 ATC 579 the taxpayer senator was allowed a deduction under a former section 82D (which allowed a deduction against assessable income for cost of a housekeeper engaged in caring for a dependant of a taxpayer) in respect of a housekeeper engaged in keeping house for her and caring for her child. Due to her heavy workload she was away from home for 177 days. A deduction was allowed as "special circumstances" existed which would make it just to allow the taxpayer's claim.

In Case V39 88 ATC 335 child care expenses were partially allowed as deduction to a Member of Parliament. The decision reiterates the position that child care expenses are of a "private" nature and therefore non-deductible. However, the Tribunal made a small allowance to allow a deduction for the services rendered by a mothercraft nurse that related to the taxpayer's Parliamentary responsibilities, despite the evidence being vague. This case provides no breakthrough but it may evidence a relaxing of the Tribunal's attitude.

In Case R48 84 ATC 384, the taxpayer argued that there was a statutory duty imposed on her by section 81(1) of the Community Welfare Services Act 1970 to provide adequate care for her child. The Tribunal denied the claims based on the principles in Lodge.

In a New Zealand case Case K59 10 NZTC 483, the taxpayer carried on a business from her home. She argued that had she paid an employee typist to do the work, she would have been free to look after the child, but would have been able to claim a deduction for the typist which would have been dearer than the child care costs. The taxpayer's claim was dismissed and it was held that the law was "quite inflexible in this particular case".

In Martin v. F.C. of T. 83 ATC 4722, the taxpayer argued that her employer required her to incur child care expenses so as to be more effective at her work.

The taxpayer relied on the decision in F.C. of T. v. Ballesty 77 ATC 4181, where a professional footballer successfully claimed a deduction for travel between his home and football matches played at his team's home ground. It was argued successfully that the travel expenditure had stemmed from an activity which was productive of the assessable income or was incurred in

gaining the assessable income.

It was one of the terms of the contract that the footballer make the best contribution he could to the winning of matches or to the success of the training sessions and, as a practical matter, the emotional stress he was under before a game dictated that he travel alone so as not to come into contact with other people.

The home to work travel expenses in this case satisfied both limbs of section 51(1) as being relevant and incidental to the derivation of the taxpayer's assessable income.

In Martin's case the provision of child care was equally as essential to the gaining of the taxpayer's income as the car travel was to the gaining of the footballer's income. The child care was a necessary expense, without it Mrs Martin's income would have suffered a very direct effect, she would not have been able to work.

However, in Martin's case the expenses did not satisfy the first limb of section 51(1) that they be relevant and incidental to the taxpayer's work.

It could be argued that if on the one hand, a footballer can claim a deduction for expenses incurred in travelling alone in his car because of temperamental factors peculiar to him, then why should a single working mother not be able to claim a deduction for expenses incurred in having her child cared for, on the basis that she will perform/study more effectively, when this provision of care will clearly give her the peace of mind to perform at a higher level.

Martin's case deals with this point somewhat unsatisfactorily. In that case, Hunt J. at p.4725 held that "...the travel itself is perceived to have a direct effect upon the gaining of assessable income, is more easily seen to be that which is productive of that income in or in the course of gaining that income". It was alluded by Hunt J. that Ballesty's case might have been incorrectly decided. He went on further to add that it was really a matter for Parliament and not for the courts to decide whether child care expenses are proper deductions from assessable income.

In Jayatilake v. F.C. of T. 91 ATC 4516, the taxpayer was denied child care costs incurred that were necessary to allow the taxpayer to participate in studies which would increase the taxpayer's chances of obtaining job promotion. The Full Federal Court held that the essential character of the child care expenses was neither incidental nor relevant to the taxpayer's activities as a computer systems officer. It was not persuaded that it should depart from the reasoning in Martin's case and Lodge's case, the authoritative cases challenged by the

taxpayer. In this case the expenses did not satisfy either limb of section 51(1) since they did not have the necessary nexus to the performance of the work. Their Honours commented that if the law on this question is to be changed, it is a matter for the Legislature, not the Court. The High Court recently refused the taxpayer special leave to appeal from the decision in this case.

## APPENDIX II - Tax Deductibility and Fee Relief

The Taxation Institute's proposal to allow either:

- (a) a deduction; or
- (b) a rebate

to taxpayers for the cost of eligible child care is intended to supplement the existing fee relief system. This is to ensure that those intended to benefit under the present system of fee relief; that is, those on lower incomes, continue to reap the greatest benefits from that existing system. How the proposal will work in practice, as set out in Tables 1 and 2, will be to allow a tax deduction or, alternatively, a rebate, on expenses incurred by an individual which are not met by the Government under the fee relief system.

Currently, the amount contributed by families for child care is based on the assessed family income (AFI), which is the gross family income per week less a \$30 allowance for each dependant child.

Families with an AFI up to \$340 a week are charged a minimum fee of \$15 for fulltime care for a single child and \$17 for two or more children in care. When the AFI exceeds \$340 a week the fee increases by 12 cents in every dollar for a single child and 20 cents in the dollar for 2 or more children. The balance of fees payable, up to a ceiling of \$100 per week, is met by the Government under the fee relief system. Where 1 child is in care, the fee relief benefit cuts out where the AFI exceeds \$56,236 per year and where 2 or more children are in care, at \$68,599. This effectively results in no fee relief being available where two parents are earning average weekly earnings.

Under the Taxation Institute's proposal, a tax benefit would be available for any expenditure incurred by a taxpayer not covered by the Government fee relief subsidy.

The after tax benefit of such a proposal can be seen from the following Tables:

Based on one child in care - total child care fees of  
\$120/week.

Table 1

<u>Gross Family</u> <u>Income p.a.</u>	<u>\$ per week</u>	<u>AFI</u>	<u>Family</u> <u>Pay</u>	<u>Fee</u> <u>Relief</u>
5,216	100	70	35	85
10,433	200	170	35	85
15,650	300	270	35	85
20,866	400	370	39	81
26,083	500	470	51	69
31,300	600	570	63	57
36,517	700	670	75	45
41,733	800	770	87	33
46,950	900	870	99	21
52,166	1000	970	111	9
56,236	1078	1048	120	-

On an after tax basis the effect would be as follows:

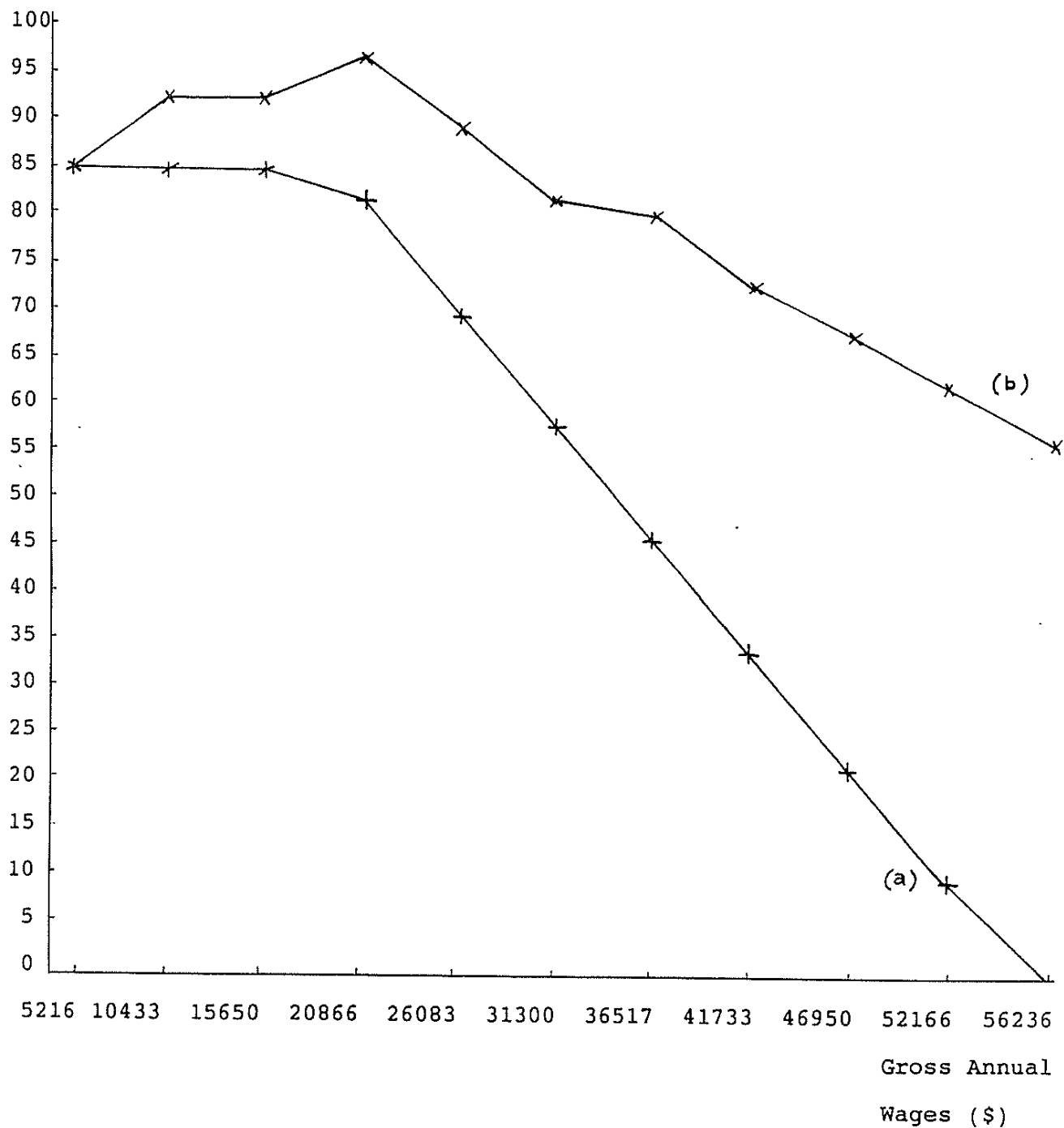
Table 2

<u>Gross Family</u> <u>Income</u>	<u>Tax Rate</u>	<u>Family</u> <u>Pay</u>	(a) <u>Tax</u> <u>Deduction</u>	(b) <u>Fee</u> <u>Relief</u>	<u>Total</u> <u>Benefit</u> <u>(a + b)</u>
5,216	NIL	35	NIL	85	85.00
10,433	20.5	35	7.17	85	92.17
15,650	20.5	35	7.17	85	92.17
20,866	38.5	39	15.01	81	96.01
26,083	38.5	51	19.63	69	88.63
31,300	38.5	63	24.25	57	81.25
36,517	46.5	75	34.87	45	79.87
41,733	46.5	87	40.45	33	73.45
46,950	46.5	99	46.03	21	67.03
52,166	46.5	111	51.61	9	60.61
56,236	46.5	120	55.80	-	55.80



As can be seen from Table 2, those on lower incomes will still benefit to a greater extent from the combined tax/fee relief system than those on middle and higher incomes. This is due to the fact that the fee relief is still worth more in dollar terms than the after tax benefit of a tax deduction for expenditure on child care fees. Subsequently, those on middle and higher incomes are no better off, they are merely put in a more equitable position since the expenditure incurred is regarded as an income related deduction thus reducing tax liability. The increased benefit to higher income earners of allowing a deduction for child care expenditure is further shown in the following Graph, where it can be seen diagrammatically that the majority of taxpayers will benefit to a much greater extent than under the existing fee relief system.

Benefit (\$)



(a) Fee Relief

(b) Fee Relief Plus Tax Benefit

# AN EVALUATION OF THE TIA PROPOSAL FOR CHANGES TO THE TAX TREATMENT OF CHILD CARE EXPENSES

by

Neil Warren

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### EXECUTIVE SUMMARY

This paper evaluates the TIA proposal for changes to the tax treatment of work-related child care expenses. The TIA proposes that these expenses should be eligible for a tax rebate or an income deduction in the hands of secondary earners in families, and that child care expenses paid as fringe benefits which are not currently exempt from Fringe Benefits Tax (FBT), should become exempt. These changes are seen as a complement to the current system of child care fee relief operated by the Federal Department of Health Housing and Community Services.

The study finds that there is much to recommend the TIA proposal and that it is surprising that the potential benefits have not been identified long before this TIA submission. It is shown that while the current child care fee relief is important in enabling lower income groups to have access to child care, introducing tax concession for work-related child care expenses will help working families with child care expenses that are not eligible for fee relief.

Probably the most important observation in this review of the TIA proposal is that a concentration by government on the first round cost of tax concessions for work-related child care expenses will present a quite misleading picture of the benefits and costs of proposal. It is shown in this report that while there is an initial cost to the Federal government from introducing the TIA proposals, it is fundamental to consider possible behavioural responses in the economy to the tax changes.

The overriding conclusion from the analysis in this study is that probably the biggest winner from the TIA proposals in the medium to longer term is the Federal Government (as shown in Table 9). This is because if the proposal encourages increased hours worked or increased entry into the workforce by females spouses, combined with the inevitable growth in the child care industry, the initial cost of the concession will be overwhelmed several times over, by the increase in personal income and indirect tax collections and reductions in social welfare payments.

## AN EVALUATION OF THE TIA PROPOSAL FOR CHANGES TO THE TAX TREATMENT OF CHILD CARE EXPENSES

### I METHODOLOGY

In Australia, all levels of governments provide some form of assistance to those providing and utilizing child care services. Local Governments sometimes provide rent free accommodation, State Governments can provide a salary subsidy (as in New South Wales) and the Federal Government can provide both capital assistance to child care centres and fee relief for the parents of children in selected centres.

This paper will however, only focus on the issue of Federal Government assistance. In particular, it will examine only the current system of Federal Government child care fee relief and consider other measures raised by the Taxation Institute of Australia as means of assisting families with work-related child care expenses. Obviously, if changes other than those considered in this report occurred in parallel with those discussed below, they will have some implications for our results. However, such changes are unlikely to occur immediately upon the introduction of any reforms by the Federal Government and so will not concern this study.

Undertaking an evaluation of alternative methods of providing assistance to families with work-related child care expenses, requires considerable information on not only the current system of child care assistance, but on the likely impact of other forms of assistance if introduced.

The information requirements for such an evaluation are onerous. In essence, they require a detailed modelling of the Australian household sector at the person level. Such a model requires information on each person's expenditure on child care, their different sources of income and their relationship to other persons in the household in which they reside. Also, data is required on the current tax and welfare system and the current system of assisting with work-related child care expenses. Fortunately, all this information is available.

Detailed income and expenditure data by the household sector is available from the 1988-89 Household Expenditure Survey (HES) unit record data released by the Australian Bureau of Statistics. This data source includes detailed data on the income and expenditure of some of persons in some 7225 households.

Data on the tax system is available from the Australian Taxation Office and some Australian Bureau of Statistics publications on taxation revenue. Information on the social security system is available from the Department of Social Security and on the current system of child care fee relief, from the Department of Health Housing and Community Services.

Each of these data sources must be brought together to model the household sector's current utilization of child care and the benefits from current and alternative systems of assistance for work-related child care expenses. This task is

undertaken by adapting STATAX, a "micro" model of the household sector in Australia (which is discussed in Warren(1987, 1990, 1991a)), to focus on this issue.

While the original HES data refers 1988-89, this data has been projected forward to 1990-91 using a detailed static microsimulation model which forms part of STATAX. The new data which is created accords with the detailed pattern of results obtained from the Australian Bureau of Statistics Labour Force Survey (Cat No. 6203.0) during 1990-91.

Of particular importance when evaluating the TIA proposal for changes to the tax treatment of child care expenses, is the HES data on current child care expenses. The HES survey identifies three categories of child care expenses (which are detailed in Appendix A) by the persons who made these outlays within the by households:

- a) Child care services- institutions (HES code 417)
- b) Child care services- nec (HES code 418)
- c) Child care services undefined (HES code 419)

Several major changes were made to STATAX to enable an evaluation of the TIA proposal on changes to the tax treatment of child care expenses. Firstly, the STATAX social welfare module was changed enable the modelling of the current child care fee relief system (as detailed in Appendix B). Secondly, the STATAX personal income tax module was extensively amended to enable the modelling of either a system of child care income deductions or tax rebates.

Thirdly, extensive changes to STATAX were made to enable an examination of the impact on the Federal budget of certain hypothetical response scenarios to the TIA proposal for changes to the tax treatment of child care expenses.

All estimates reported in this paper are made for fiscal 1990-91, with any full year effects being estimated using the personal income tax schedule effective since 1 January 1991. This is the same approach as when STATAX was recently used to evaluate the TIA Proposal for "An Australian Residents Withholding Tax" (1991).

The extent of Federal government financial support for child care services is detailed in Appendix C. While the assistance provided takes many different forms, our concern in this paper is with the child care fee relief system whose operation is detailed in Appendix B. The operation of fee relief is designed firstly, to target very accurately, lower income working families with work-related child care expenses, and secondly, to maintain close control on the cost of the scheme by controlling the number of subsidized places which are available in any long day care or outside school hours child care centre.

Before examining the distribution of benefits from child care fee relief, it is worth first examining who are currently utilizing child care services. This information is presented in Table 1. The table format first needs some description before we can interpret the results. The population of households is firstly divided into 14 groups and these are detailed in Appendix D. The households in each of these 14 groups are then grouped into deciles (10% of the group) after having been ranked by gross household income. Data on each of the group decile's gross income is





TABLE 1b CHILD CARE FEES PAID TO NON-INSTITUTIONS OR NEC  
(HES Code 418 AND 419)

HOUSEHOLD GROUPS														
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
	M1WK=0	M1WK>0	M2WK=0	M2WK>0	SWTT	SMWPT	SE	FARMER	UB/SB	MCNGBNI	MNGB	SNGBNSP	SNGBSP	NIDRS
GROUP														
DECILES		SPH												
1	-	2.71	-	19.34	-	8.72	3.71	12.84	-	23.03	-	-	-	-
2	-	1.56	-	21.16	-	19.04	16.37	1.16	-	85.71	-	-	-	-
3	-	6.48	-	19.45	40.53	21.10	-	-	13.78	-	-	-	-	-
4	-	0.98	-	44.47	143.81	8.70	5.83	3.21	5.80	-	-	-	1.62	-
5	-	8.35	-	32.62	-	21.26	3.87	5.70	-	-	-	-	0.64	-
6	-	0.86	-	40.38	-	-	27.92	14.29	1.16	-	-	-	-	-
7	-	2.13	-	39.01	25.68	18.38	9.37	0.60	-	-	-	-	11.71	-
8	-	4.43	-	50.79	-	-	6.66	-	-	-	-	12.79	-	-
9	-	7.83	-	53.83	-	5.80	12.84	11.93	-	-	-	-	-	-
10	-	11.45	-	51.01	-	73.14	30.69	0.87	4.36	-	1.86	-	1.28	-
ALL	-	5.69	-	36.71	70.97	23.63	14.04	7.86	7.19	75.38	1.86	12.79	5.66	-
GROUP														
DECILES		NUMBER OF HOUSEHOLDS (000s)												
1	-	3.7	-	10.1	-	1.4	2.0	1.1	-	0.1	-	-	-	-
2	-	1.8	-	4.9	-	2.0	1.4	0.8	-	0.7	-	-	-	-
3	-	6.2	-	9.4	1.3	1.4	-	-	1.7	-	-	-	-	-
4	-	3.5	-	12.7	1.0	0.9	2.9	0.5	0.3	-	-	-	0.7	-
5	-	8.3	-	11.5	-	1.2	1.5	1.1	-	-	-	-	0.2	-
6	-	2.3	-	6.7	-	-	1.0	3.0	0.6	-	-	-	-	-
7	-	2.6	-	16.4	0.7	1.4	1.2	2.1	-	-	-	-	1.4	-
8	-	3.4	-	5.9	-	-	4.5	-	-	-	-	1.7	-	-
9	-	6.9	-	5.4	-	0.7	0.2	1.3	-	-	-	-	-	-
10	-	3.1	-	8.6	-	1.4	4.9	0.7	2.5	-	0.6	-	1.0	-
ALL	-	41.8	-	91.5	3.1	10.5	19.7	10.5	5.0	0.9	0.6	1.7	3.3	-
GROUP														
DECILES		DISTRIBUTION OF HOUSEHOLDS (%)												
1	-	8.8	-	11.0	-	13.8	10.2	10.1	-	16.5	-	-	-	-
2	-	4.3	-	5.3	-	18.7	7.2	7.6	-	83.5	-	-	-	-
3	-	14.8	-	10.3	43.7	13.4	-	-	33.3	-	-	-	-	-
4	-	8.3	-	13.9	32.8	8.8	14.6	5.1	5.1	-	-	-	21.1	-
5	-	19.8	-	12.5	-	11.4	7.8	10.5	-	-	-	-	7.0	-
6	-	5.6	-	7.3	-	-	5.2	28.7	11.9	-	-	-	-	-
7	-	6.2	-	17.9	23.4	13.4	6.3	19.7	-	-	-	-	41.7	-
8	-	8.2	-	6.5	-	-	22.8	-	-	-	-	100.0	-	-
9	-	16.6	-	5.9	-	6.8	0.9	12.1	-	-	-	-	-	-
10	-	7.4	-	9.4	-	13.7	24.9	6.3	49.8	-	100.0	-	30.3	-
ALL	-	100.0	-	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	-

Table 1 presents data only on those households in each of the group decile with a positive amount of the appropriate child care payments. The results in this table indicates the extensive use of child care services by working families, whether they are provided by formal child care centres (HES code 417) or by persons (HES code 418 and probably HES code 419). It is also clear that these services are used by families where the secondary earner is working and non-working.

The Table also shows that the higher income households are less prone to using child care. This could in part be attributed to these households comprising parents who are older (and thus have higher incomes as they move through their life cycle) and who therefore have older children who are less in need of child care services.

The question now is who are the beneficiaries of the current system of child care fee relief which provides an hourly rate subsidy to eligible families? Appreciating this fact is important if only to contrast it with those who are likely to receive assistance under the TIA proposals. Consequently, the child care fee relief system detailed in Appendix B was incorporated into STATAX.

The benefits from such a system for various household groups are detailed in Table 2 where those households who effectively receive a positive child care subsidy from the Federal government are reported. The benefits from the current child care fee relief system were estimated using the following steps:

- 1) Select families which currently pay child care fees to centres (HES code 417), have children under 5, where both the spouses in a married couple are working or at least looking for work or where a sole parent is working or looking for work.
- 2) Applying the rules detailed in Appendix B for fee relief to the selected families assuming only the children under 5 are place in long day care, estimating in the final analysis, their subsidized hourly cost of child care.
- 3) Estimating the number of hours their children were was in long day care by dividing the amount they paid as actual child care expenses (HES code 417) by the estimate of the subsidized hourly cost of child care. If they appeared to have their child in long day care of more than 50hours, it was assumed that the amount above 50hours at the subsidized hourly rate was due to a higher hourly rate being changed than the recommended hourly fee.
- 4) The subsidy to a family is then the number of hours the child is in long day care multiplied by the hourly subsidy paid by the Federal government in the form of Child Care Fee Relief.

Applying these steps to HES data in STATAX resulted an estimated full-year (1990-91) cost of child care fee relief of \$148m as against an official estimate of \$178m for 1990-91 as outlined in Appendix C.

TABLE 2 BENEFICIARIES IN EACH GROUP DECILE FROM A CHILD CARE FEE RELIEF

	HOUSEHOLD GROUPS													
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
	M1WK=0	M1WK>0	M2WK=0	M2WK>0	SFFT	S4MPT	SE	FARMER	UB/SB	MCNGBNI	MNGB	SNGBNSP	SNGBSP	NIDRS
GROUP														
DECILES	SPW													
1	-	-	-	30.26	76.69	-	-	47.35	-	-	-	-	-	-
2	-	-	-	12.14	-	-	183.00	-	-	1.93	-	-	-	-
3	-	30.25	-	22.69	-	142.61	57.47	172.13	-	-	-	-	-	-
4	-	20.00	-	6.74	42.53	72.32	101.69	54.66	-	-	-	-	-	-
5	-	-	-	8.21	-	15.62	33.31	85.00	-	-	-	-	-	-
6	-	-	-	10.32	7.84	32.52	26.21	183.00	-	-	-	-	-	-
7	-	-	-	2.35	37.24	-	10.68	52.95	4.35	-	-	-	-	-
8	-	-	-	8.31	-	28.68	9.07	14.18	-	-	54.57	-	-	-
9	-	-	-	5.30	-	12.17	5.43	85.00	-	-	20.23	-	-	-
10	-	-	-	-	125.56	-	-	-	45.08	-	-	4.43	-	-
ALL	-	24.19	-	15.53	50.73	61.03	42.24	80.39	23.83	1.93	52.74	4.43	-	-
GROUP														
DECILES	NUMBER OF HOUSEHOLDS ('000s)													
1	-	-	-	8.9	1.8	-	-	0.7	-	-	-	-	-	-
2	-	-	-	7.7	-	-	0.8	-	-	0.1	-	-	-	-
3	-	0.1	-	8.9	-	2.2	1.6	0.7	-	-	-	-	-	-
4	-	0.2	-	7.4	2.9	1.1	1.6	1.4	-	-	-	-	-	-
5	-	-	-	6.8	-	1.3	2.6	0.6	-	-	-	-	-	-
6	-	-	-	0.6	1.2	0.1	1.6	0.8	-	-	-	-	-	-
7	-	-	-	3.0	0.7	-	1.3	1.9	0.1	-	-	-	-	-
8	-	-	-	0.9	-	2.2	3.3	0.7	-	-	1.7	-	-	-
9	-	-	-	0.5	-	1.2	0.7	1.0	-	-	0.1	-	-	-
10	-	-	-	-	0.5	-	-	-	0.1	-	-	1.1	-	-
ALL	-	0.3	-	44.7	7.2	8.0	13.4	7.8	0.3	0.1	1.8	1.1	-	-
GROUP														
DECILES	DISTRIBUTION OF HOUSEHOLDS (%)													
1	-	-	-	19.9	25.2	-	-	8.9	-	-	-	-	-	-
2	-	-	-	17.1	-	-	5.6	-	-	100.0	-	-	-	-
3	-	40.9	-	20.0	-	27.2	12.1	9.4	-	-	-	-	-	-
4	-	59.1	-	16.6	40.3	13.5	11.6	17.4	-	-	-	-	-	-
5	-	-	-	15.1	-	16.3	19.8	7.1	-	-	-	-	-	-
6	-	-	-	1.3	17.2	0.7	11.8	10.1	-	-	-	-	-	-
7	-	-	-	6.7	9.9	-	9.8	24.9	52.2	-	-	-	-	-
8	-	-	-	2.0	-	27.6	24.3	8.7	-	-	94.7	-	-	-
9	-	-	-	1.2	-	14.7	5.0	13.4	-	-	5.3	-	-	-
10	-	-	-	-	7.3	-	-	-	47.8	-	-	100.0	-	-
ALL	-	100.0	-	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	-	-

Modelling the changes to the child care fee relief scheme after 1 January 1992 as detailed in Appendix B involved some amendments to the approach taken above. In particular, the changes from 1 January 1992 primarily concern an extension of the fee relief system to outside school hours care (OSHC). Modelling this change using HES data in STATAx involved assuming that any family paying child care fees to centres (HES code 417) and with no children under 5, must have children over 5 in OSHC. Having established the number of children in OSHC, the rules detailed in Appendix B for fee relief are applied. The estimated full year (1990-91) cost of the post 1 January 1992 scheme of child care fee relief using STATAx was \$159m.

While these results do not exactly replicate the estimated Budget outcome (Appendix C) for 1990-91 of \$178m, they do indicate that the approach adopted results in an estimate of approximately similar magnitude. Also, it indicates that any estimates made in this paper of the cost of changing the tax treatment of child care are not likely to be too dramatically different from those which might arise in practice.

Moreover, if the implementation of changes to the tax treatment of child care expenses brings with it a marked response by secondary earners in married couples with children, then all the estimates, including the cost of child care fee relief (if places are expanded), are all subject to some variation.

Table 2 indicates that the greatest benefit from the post 1 January 1992 fee relief scheme accrues to those groups at the lower end of the income ranges in the groups to which they belong. This is not surprising because of the means test applied when determining a families eligibility to child care fee relief.

### III THE TIA CHILD CARE TAX REBATE PROPOSAL

There are several possible approaches to providing direct relief to persons whose employment is dependent on putting their children in long day care or after-school hours care. Currently, two basic avenues are used by the Federal government:

- i Child care fee relief
- ii Employer tax incentives

While (i) involves a subsidy on the hourly fee for child care and is means tested on family income (as detailed earlier), (ii) has involved amendments to FBT legislation. Currently, child care expenditure by an employer is exempt from Fringe Benefits Tax (FBT) if they are for an in-house child care facilities or for the effective purchase of a block of places in a commercial child care centre for the children of employees. However, any other payment by the employer for child care expenses of employee's is subject to FBT.

Four other possible methods of assisting employees with work related child care expenses are proposed by the TIA, not so much as substitutes to current arrangements, but as complements. These are:

- iii Allowing a person a non-refundable non-transferable tax rebate for work related child care expenses with a limit where their child care expenses are no more than their earned (wage and salary and self employment) income; OR
- iv Allowing a person a non-refundable transferable tax rebate for work related child care expenses with a limit where their child care expenses are no more than their earned (wage and salary and self employment) income; OR
- v Allowing a person an income deduction for work related child care expenses from their earned (wage and salary and self employment) income.
- vi The exemption from FBT of all child care expenses paid as a fringe benefit to an employee by an employer.

The remainder of this section will examine tax rebates for child care expenses (*iii* and *iv* above). Section IV will focus on income deduction for child care expenses (as in *v* above) and Section VI, FBT concessions (*vi*).

**Table 3 The Cost of Allowing a Non-Refundable Tax Rebate for Child Care Expenses(\$m)**

	\$m
Non-Transferable Tax Rebate:	
Base Case: No Cap, 20% Rebate Rate	98
Case A: Cap of \$100pw per child , 20% Rebate Rate	86
Case B: Cap of \$120pw per child , 20% Rebate Rate	89
Base Case: No Cap, 25% Rebate Rate	122
Transferable Tax Rebate:	
Base Case: No Cap, 20% Rebate Rate	101
Case A: Cap of \$100pw per child , 20% Rebate Rate	89
Case B: Cap of \$120pw per child , 20% Rebate Rate	92
Base Case: No Cap, 25% Rebate Rate	126

The cost of various tax rebates for work-related child care expenses paid by persons assuming unchanged levels of child care take-up is detailed in Table 3. The virtue and the vice of using non-refundable non-transferable tax rebates as the mechanism for assisting those persons for whom child care expenses are a direct result of earning wage and salary or self employment income, is that they are reasonably inexpensive but may in fact offer little benefit to many of those it is

intended to assist. This particularly includes persons such as married women in part-time employment. This is because some secondary earners in married couples will not have income above the tax threshold (\$5400pa). Therefore, a non-refundable non-transferable tax rebate only assists those who pay income tax, since at a maximum, such a rebate can only act to exhaust the claimant's persons tax liability.

One possible avenue for overcoming this constraint is for these rebates to be transferable between working spouses. The concept of transferable rebates is nothing new in Australia since unused pensioner rebates are already transferable between spouses (Regulation 151(6), *Income Tax Regulations*, effective 1 July 1990).

**TABLE 4a BENEFICIARIES IN EACH GROUP DECILE FROM A CAPPED (\$1043PA) NON-REFUNDABLE NON-TRANSFERABLE TAX REBATE (AT 20%) ON WORK-RELATED CHILD CARE EXPENSES**

	HOUSEHOLD GROUPS													
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
	M1WK=0	M1WK>0	M2WK=0	M2WK>0	SWT	SWMT	SE	FARMER	UB/SB	MCNGBNI	MNGB	ENGBNSP	ENGBSP	NIDRS
GROUP														
DECILES	TAX CHANGE \$PW													
1	-	-	-	-5.49	-9.54	-	-	-	-	-2.94	-	-	-	-
2	-	-	-	-5.33	-6.14	-3.84	-	-	-	-15.33	-	-	-	-
3	-	-1.16	-	-6.14	-8.11	-4.34	-1.73	-	-	-	-	-	-	-
4	-	-	-	-7.81	-12.10	-7.77	-4.34	-	-	-	-	-	-	-
5	-	-	-	-7.61	-	-3.62	-3.90	-	-	-	-	-	-	-
6	-	-	-	-9.52	-5.32	-1.16	-8.38	-	-	-	-	-	-	-
7	-	-	-	-10.43	-15.43	-5.12	-4.84	-	-	-3.00	-	-	-	-
8	-	-	-	-9.25	-	-0.93	-7.68	-	-	-	-	-1.28	-	-
9	-	-	-	-11.18	-	-12.47	-6.23	-0.93	-	-	-	-	-	-
10	-	-1.03	-	-10.24	-20.00	-13.12	-3.49	-0.17	-12.84	-20.00	-	-1.16	-	-
ALL	-	-1.05	-	-8.19	-10.69	-7.27	-5.16	-0.66	-12.84	-13.26	-	-1.23	-	-
GROUP														
DECILES	NUMBER OF HOUSEHOLDS (000s)													
1	-	-	-	13.4	1.8	-	-	-	-	0.1	-	-	-	-
2	-	-	-	8.5	0.6	0.6	-	-	-	0.8	-	-	-	-
3	-	0.2	-	16.1	1.3	3.6	2.8	-	-	-	-	-	-	-
4	-	-	-	16.4	3.9	0.9	2.1	-	-	-	-	-	-	-
5	-	-	-	19.4	-	1.9	4.2	-	-	-	-	-	-	-
6	-	-	-	9.3	1.2	0.1	2.6	-	-	-	-	-	-	-
7	-	-	-	18.9	0.9	0.9	2.3	-	-	0.1	-	-	-	-
8	-	-	-	8.5	-	1.2	4.4	-	-	-	-	1.7	-	-
9	-	-	-	7.3	-	1.9	1.6	1.2	-	-	-	-	-	-
10	-	2.0	-	12.2	0.5	3.2	2.3	0.7	0.1	0.2	-	1.1	-	-
ALL	-	2.3	-	130.1	10.3	14.2	22.2	1.9	0.1	1.3	-	2.9	-	-

Table 3 indicates that the cost of having these rebates transferable but non-refundable is little more than when they were non-transferable. A closer examination of the data revealed that when families put their children in child care, it is because the secondary earner is earning a not insubstantial income by working more than just a few hours per week. Consequently, many secondary earners paying for child care have earned incomes above the tax threshold of \$5400pa and therefore in many cases, can take advantage of the tax break that the rebate for child care expenses offers them. Therefore, if a tax rebate for child care expenses was to be introduced, it is probably appropriate that it be introduced as a transferable rebate since this would cost only marginally more than if the rebate was non-transferable but offer assistance also to part-time married women with earnings below the tax threshold.

Table 4 illustrates the distribution of the benefits from a non-refundable transferable and non-transferable tax rebate for child care expenses where those expenses are limited to an amount equal to the earned income of the secondary earner. The groups identified in this table are the same groups identified in Tables 1 and 2. Also, the Table reports only those who received a tax reduction in each of the group deciles due to the rebate. The benefit to working couples in the lower income deciles is apparent, particularly when it is recognised that average income in each of these group deciles (shown in Appendix D) increases faster up the deciles than does the average tax reduction due to the tax rebate. That is, the tax reduction relative to income was higher for the lower income groups than to the higher income groups.

#### IV THE TIA CHILD CARE TAX DEDUCTION PROPOSAL

The alternative to a tax rebate for child care expenses is an income deduction for work-related child care expenses. The cost of this proposal is considerably more than for tax rebates. In fact, the income deduction with no cap would cost \$162m as shown in Table 5, compared to uncapped non-transferable rebates which cost \$98m and uncapped transferable rebates costing \$101m. Why?

This is because of several factors. Firstly, an uncapped income deduction also affects Medicare collections by some \$7m.

Secondly, in most cases the effective tax rate to apply to the child care deduction is at least 20%, if not higher. This can be shown using the effective personal income tax schedule for the secondary earner spouse in a family.

While the Personal Income Tax schedule operating in Australia since 1 January 1991 is as shown in Table 6, this in effect only applies to a single employed person with no dependents.

**TABLE 4b BENEFICIARIES IN EACH GROUP DECILE FROM A CAPPED (\$1043PA) NON-REFUNDABLE TRANSFERABLE TAX REBATE (AT 20%) ON WORK-RELATED CHILD CARE EXPENSES**

	HOUSEHOLD GROUPS													
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
	M1WK=0	M1WK>0	M2WK=0	M2WK>0	SWTT	SWTPT	SE	FARMER	UB/SB	MCNGBNI	MNGB	ENGBNSP	SNGBSP	NIDRS
GROUP														
DECILES	TAX CHANGE \$PW													
1	-	-	-	-4.59	-9.54	-	-	-	-	-2.94	-	-	-	-
2	-	-	-	-5.22	-6.14	-3.84	-	-	-	-15.33	-	-	-	-
3	-	-1.16	-	-6.17	-8.11	-4.34	-1.73	-	-	-	-	-	-	-
4	-	-	-	-7.33	-12.10	-9.63	-3.29	-	-	-	-	-	-	-
5	-	-	-	-7.53	-	-3.62	-3.90	-	-	-	-	-	-	-
6	-	-	-	-9.58	-5.32	-1.16	-8.38	-	-	-	-	-	-	-
7	-	-	-	-10.89	-15.43	-5.12	-4.84	-	-	-16.69	-	-	-	-
8	-	-	-	-9.25	-	-0.93	-7.68	-	-	-	-	-1.28	-	-
9	-	-	-	-11.41	-	-12.47	-6.23	-0.81	-	-	-	-	-	-
10	-	-1.03	-	-10.24	-20.00	-13.12	-3.49	-0.17	-12.84	-20.00	-	-1.16	-	-
ALL	-	-1.05	-	-7.95	-10.69	-7.42	-4.94	-0.71	-12.84	-14.77	-	-1.23	-	-
GROUP														
DECILES	NUMBER OF HOUSEHOLDS (000s)													
1	-	-	-	18.2	1.8	-	-	-	-	0.1	-	-	-	-
2	-	-	-	9.3	0.6	0.6	-	-	-	0.8	-	-	-	-
3	-	0.2	-	16.8	1.3	3.6	2.8	-	-	-	-	-	-	-
4	-	-	-	17.9	3.9	1.1	3.7	-	-	-	-	-	-	-
5	-	-	-	20.2	-	1.9	4.2	-	-	-	-	-	-	-
6	-	-	-	9.6	1.2	0.1	2.6	-	-	-	-	-	-	-
7	-	-	-	18.9	0.9	0.9	2.3	-	-	0.1	-	-	-	-
8	-	-	-	8.5	-	1.2	4.4	-	-	-	-	1.7	-	-
9	-	-	-	7.3	-	1.9	1.6	3.4	-	-	-	-	-	-
10	-	2.0	-	12.2	0.5	3.2	2.3	0.7	0.1	0.2	-	1.1	-	-
ALL	-	2.3	-	138.9	10.3	14.3	23.8	4.1	0.1	1.3	-	2.9	-	-

**Table 5 The Cost of Allowing an Income Deduction for Child Care Expenses(\$m)**

	\$m
Base Case: No Cap	162
Case A: Cap of \$100pw per child	137
Case B: Cap of \$120pw per child	143



**Table 6 Nominal Personal Income Tax Schedule for a Single Person**

Income Ranges(\$pa)	Marginal Tax Rate
0 - 5400	0%
5400 - 20700	20%
20701 - 36000	38%
36001 - 50000	46%
50001 plus	47%

There exist under the current Australian personal income tax, special tax rebates for recipients of pensions and government benefits, sole parents, those who live in certain geographic zones, those who are married and have dependents and those who have medical expenses.

For a married couple with children not in receipt of any government pension or benefit or any zone or medical rebates, their Personal Income Tax schedule is in effect, that shown in Table 7. While in practice the Dependent Spouse Rebate (DSR) accrued to the primary earner, its size is determined by the income of the secondary earner. Therefore, we could view this DSR and its withdrawal (at 25% on income above \$282pa) as effectively a universal rebate to the primary earners with dependents and its withdrawal as a tax on the income of the secondary earner in the married couple. This interpretation results in the tax schedules for the primary and secondary earners in a working married couple with children as shown in Table 7.

The schedule for the primary earner assumes that they always in effect receive the dependent spouse tax rebate (DSR) which in this case is \$1296 comprising \$1080 for a dependent spouse and \$216 for dependent children. This yields an effective threshold for the primary earner of \$11880pa ( $\$5400 + \$1296 / .2$ ). The situation is quite different for the secondary earner in a married couple. As they increase their income above \$282pa, the DSR is reduced by 25% of the income earned above \$282pa. Therefore, when the secondary earner's income goes above \$5466 (or  $\$282 + (\$1296 / .25)$ ), the rebate will be completely withdrawn. With the secondary earner beginning to pay tax directly above the \$5400 threshold at a marginal rate of 20%, the secondary earner confronts an effective marginal tax rate of 45% (equal to the 20% personal income tax rate and 25% DSR withdrawal rate). When the earnings of the secondary earner go above \$5466pa, they will confront a marginal tax rate schedule similar to that of a single person with no children with a similar income.

**Table 7 Effective Personal Income Tax Schedule for Spouses in a Married Couple with Children**

7a Primary Earner Spouse with Children (DSR is \$1296pa)

Income Ranges(\$pa)	Marginal Tax Rate
0 - 11880	0%
11881 - 20700	20%
20701 - 36000	38%
36001 - 50000	46%
50001 plus	47%

7b Secondary Earner Spouse with Children (DSR is \$1296pa)

Income Ranges(\$pa)	Marginal Tax Rate
0 - 282	0%
283 - 5400	25%
5401 - 5466	45%
5467 - 20700	20%
20701 - 36000	38%
36001 - 50000	46%
50001 plus	47%

The secondary earner in a married couple clearly confronts a tax schedule where the marginal tax rate is in most cases, at least 20% and more often than not, 25% or more.

In fact, the income deduction approach has some basic similarities to a system of transferable tax rebates except that now, the marginal tax rate that is applied is not fixed but dependent on the income of the secondary earner. That is, when the secondary earner's income fall below the tax threshold of \$5400, while they might not directly receive any tax refund, they effectively do through their spouse receiving an increased DSR which is what is effective reflected in Table 7b.

The cost of an income deduction for child care expenses as shown in Table 5 is therefore considerably more than that for a non-refundable transferable tax rebate because the effective tax rebate rate under an income deduction approach will in most cases be at least 20% and in many cases, considerably higher as evident in Table 7b.

**TABLE 8 BENEFICIARIES IN EACH GROUP DECILE FROM A CAPPED (\$5214PA) INCOME DEDUCTION FOR WORK-RELATED CHILD CARE EXPENSES**

	HOUSEHOLD GROUPS													
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
	M1WK=0	M1WK>0	M2WK=0	M2WK>0	SWFT	SWFTPT	SE	FARMER	UB/SB	MCNGBNI	MNGB	SNGBNSP	SNGBSP	NIDRS
GROUP														
DECILES	TAX CHANGE \$PW													
1	-	-	-	-5.20	-9.84	-	-	-	-	-2.94	-	-	-	-
2	-	-	-	-5.63	-12.05	-3.84	-	-	-	-15.33	-	-	-	-
3	-	-2.28	-	-7.12	-12.70	-4.40	-1.73	-	-	-	-	-	-	-
4	-	-	-	-9.29	-22.85	-7.77	-3.55	-	-	-	-	-	-	-
5	-	-	-	-11.11	-	-5.63	-7.10	-	-	-	-	-	-	-
6	-	-	-	-15.86	-10.72	-1.16	-14.19	-	-	-	-	-	-	-
7	-	-	-	-16.68	-31.54	-5.44	-7.35	-	-	-20.58	-	-	-	-
8	-	-	-	-15.47	-	-2.20	-15.13	-	-	-	-	-1.36	-	-
9	-	-	-	-23.15	-	-13.25	-12.31	-0.56	-	-	-	-	-	-
10	-	-1.66	-	-20.17	-39.25	-28.84	-5.48	-0.17	-18.77	-48.25	-	-2.28	-	-
ALL	-	-1.72	-	-12.04	-18.80	-11.33	-8.39	-0.47	-18.77	-19.29	-	-1.72	-	-
GROUP														
DECILES	NUMBER OF HOUSEHOLDS (000s)													
1	-	-	-	18.2	1.8	-	-	-	-	0.1	-	-	-	-
2	-	-	-	9.3	0.6	0.6	-	-	-	0.8	-	-	-	-
3	-	0.2	-	16.8	1.3	3.6	2.8	-	-	-	-	-	-	-
4	-	-	-	17.9	3.9	0.9	3.7	-	-	-	-	-	-	-
5	-	-	-	20.2	-	1.9	4.2	-	-	-	-	-	-	-
6	-	-	-	9.6	1.2	0.1	2.6	-	-	-	-	-	-	-
7	-	-	-	18.9	0.9	0.9	2.3	-	-	0.1	-	-	-	-
8	-	-	-	8.5	-	1.2	4.4	-	-	-	-	1.7	-	-
9	-	-	-	7.3	-	1.9	1.6	2.2	-	-	-	-	-	-
10	-	2.0	-	12.2	0.5	3.2	2.3	0.7	0.1	0.2	-	1.1	-	-
ALL	-	2.3	-	138.9	10.3	14.2	23.8	2.9	0.1	1.3	-	2.9	-	-

The distribution of the benefits from an income deduction for child care expenses is shown in Table 8. These benefits are much more widely spread than is a rebate, particularly at the lower end of the income distribution in each group. It is apparent also that the benefit to the higher income spouse's with children in long day care is also much higher than when they are only entitled to a tax rebate. This is because the rebate is available only at a fixed rate under a tax rebate system but with the income deduction approach, it accrues to the taxpayer at a rate equal to their personal income tax marginal tax rate.

## V SENSITIVITY ANALYSIS OF THE POTENTIAL BEHAVIOURAL RESPONSE OF FAMILIES TO A SYSTEM OF TAX DEDUCTIONS/REBATES

The most important question to be asked of the discussion above is "What happens to the results when there is a marked response by families to the new tax treatment of work related child care expenses?" If one of the objectives of this proposal is to provide more incentive for women to enter the workforce (as well as to recognize that child care expenses are a real cost of undertaking employment), then it is not unreasonable to expect there to be some response to the reforms. This section will examine what impact several hypothetical scenarios could have on our results.

Two approaches will be adopted to demonstrating what impact any behavioural response to tax rebates/deductions for child care expenses could have on the Federal government budget. The first will focus on what might happen to different individuals and the second, the incorporation of any broad responses by the beneficiaries of the tax changes into STATAX.

### A. INDIVIDUAL RESPONSES

If we assume at outset that no individual can claim a tax rebate or deduction for work-related child care expenses unless they quote the tax file number (of the person or centre), then we can assume that the outlays by individuals will directly (if the child carer is a person) or indirectly (if the child carer is a child care centre) flow through to other persons who are providing this care. Consequently, one person's outlays are another person's income (either through wages (child carers) or profit (child care centre owners)). Taking some hypothetical scenarios can help indicate what burden the tax changes could place on the Federal budget. For simplicity, we shall begin with the case of a child care rebate which is transferable and given at the rate of 20%.

Let us now examine Example 1 in which it is assumed that the job found by spouse entering employment (Spouse A in Example 1) is a *new* job and not one gained at the expense of another person. However, even if it was, this displaced person would need to have had an effective marginal tax rate (assuming the wage rate was the same) of some  $(132.14/350)$  38% for there to be a negative impact on the fisc and this is not possible unless the displaced person was another dependent spouse with similar circumstances. The gains to the Federal government are clear and sizeable in this example.

**EXAMPLE 1**

A dependent spouse (Spouse A) enters the workforce full-time and places their 4 year old child with a child carer (Spouse B) who is receiving the Family Allowance Supplement (FAS) for their own children and where a DSR for claimed for both Spouse A and B. Also, a transferable tax rebate is allowed for earnings related child care expenses.

Spouses of Spouse A and B Earning \$345.20pw

Spouse A

Original Status

Earning no income, no child care expenses

Tax = 0pw

FAS for child under 13 years = \$26.50pw

Disposable Income after child care = \$26.50pw

New Status and Claiming a Child Care Expense Tax Rebate

Earning \$350pw, child care expenses \$100pw

Tax (using Table 7b) = Tax less Child Care Tax Rebate  
= 74.14 - 100\*.2 = \$54.14pw

FAS for child under 13 years = \$0pw

Disposable Income after child care = 350-100-54.14= 195.86pw

Net Change in Status after child care expenses

From earning \$350pw, the family's after child care expenses disposable income has increased => 195.86-26.50 = \$169.36pw

Spouse B

Original Status

Earning no income, no child care expenses

Tax = 0pw

FAS for child under 13 years = \$26.50pw

Disposable Income after child care = \$26.50pw

New Status and Claiming a Child Care Expense Tax Rebate

Earning \$100pw, no child care expenses

Tax (using Table 7b) = Tax less Child Care Tax Rebate  
= 23.65 - 0\*.2 = \$23.65pw

FAS for child under 13 years = \$0pw

Disposable Income after child care = 100-23.65=\$76.35pw

Net Change in Status after child care expenses

From earning \$100pw, the family's after child care expenses disposable income has increased => 76.65-26.50 = \$49.85pw

Federal Budget Financial Position

Original Status

Tax less FAS = 0 - \$26.50 \* 2 = -\$53.00pw

New Status

Tax less FAS = (23.65 + 54.14) + \$0 \* 2 = \$77.79pw

**Net Fiscal Impact (Net Return to Government) \$130.79pw**

Another qualification to Example 1 is the possibility that Spouse A and B could come to some arrangement so that Spouse A does not claim a rebate for the child care expense and Spouse B does not report it as income. Some evidence of this possibility has been evident in Canada where tax concessions have been given for child care expenses.

The incentive for this activity is quite apparent in Example 2 below which is a variant on Example 1. While this action costs Spouse A \$20pw, the benefit to Spouse B is \$50.15pw, far out weighing the loss to Spouse B. In fact, of the \$100pw that Spouse B receives from child caring, if they reported this income they would find their disposable income only increasing \$49.85, that is by less than half the amount they received.

If Spouse B was forced to report this income by Spouse A wanting to claim the expense as a tax rebate, it is likely that Spouse B would want to increase the amount that they charge for child caring in order to receive a more appealing after tax rate of return on their child caring activities. There are clearly some tax arbitrage opportunities that would need to be worked out between Spouses A and B. Nevertheless, the incentive for Spouse B not to report their earning exists.

What Examples 1 and 2 indicate is just how high the effective marginal tax rates (EMTR) are for those persons on low private (non-government) income who are receiving income means tested government benefits (see Warren 1991b) and the incentive this provides either not to increase their earnings or to undertake any income earning activity through the black economy.

The fact is, however, that even if child caring takes place in the black economy, the Federal Government is still a net gainer from the allowing a transferable tax rebate for child care expenses. This would also be the case if the rebate was not transferable or if an income deduction was allowed for these expenses. The major implication from raising the spectre of the black economy is that the gains to the government may be less than possible.

If we assume that there are in fact distinct limits on the scope for undertaking child caring in the black economy - because most will no doubt be provided by child care centres - then it is likely that the changes to the tax treatment of child care expenses will increase employment in this sector and not cost but earn the government revenue through increased tax receipts and decreased social welfare payments.

What the examples above have indicated is that one of the main beneficiaries of the TIA proposals for changes to the tax treatment of child care expenses is the Federal government. This is especially true if those who are to become the child carers are currently dependent spouses or unemployed persons. Even if the child carer only works part-time as a carer, there is still likely to be significant benefits to the government because of the high withdrawal rates attached to social welfare payments possibly received by the child carer's family. For example, an unemployed person has their benefit reduced dollar for dollar above \$70pw and FAS recipients, at a rate of 50% above a family income threshold of \$345.20pw.

**EXAMPLE 2      EXAMPLE 1 with Non-Reporting of Child Care Expenses and Income**

Spouse A

Original Status

Earning no income, no child care expenses

Tax = 0pw

FAS for child under 13 years = \$26.50pw

Disposable Income after child care = \$26.50pw

New Status and NOT Claiming a Child Care Expense Tax Rebate

Earning \$350pw, child care expenses \$100pw

Tax (using Table 7b) = Tax less Child Care Tax Rebate  
= 74.14 - 0\*.2 = \$74.14pw

FAS for child under 13 years = \$0pw

Disposable Income after child care = 350-100-74.14 = 175.86pw

Net Change in Status after child care expenses

From earning \$350pw, the family's after child care expenses disposable income has increased => 350-100-74.14-26.50 = \$149.36pw

Spouse B

Original Status

Earning no income, no child care expenses

Tax = 0pw

FAS for child under 13 years = \$26.50pw

Disposable Income after child care = \$26.50pw

New Status and NOT Reporting Earnings

Earning \$100pw, no child care expenses

Tax (using Table 7b) = Tax less Child Care Tax Rebate  
= 0.0 - 0\*.2 = \$0pw

FAS for child under 13 years = \$26.50pw

Disposable Income after child care = 100-0.0+26.50=\$126.50pw

Net Change in Status after child care expenses

From earning \$100pw and not reporting this income to either the ATO or DSS, the family's after child care expenses disposable income has increased but the full amount of the child care earnings of \$100pw.

Federal Budget Financial Position

Original Status

Tax less FAS = 0 - \$26.50 \* 2 = -\$53.00pw

New Status

Tax less FAS = (0.00 + 74.14) - \$26.5 \* 1 = \$47.64pw

**Net Fiscal Impact (Net Return to Government) \$100.64pw**

Fiscal Loss due to Black Economy

FAS Spouse B + Tax Spouse A + Tax Spouse B

26.50 - 20 + 23.65 = 30.15

Gain to Spouse A from not claiming Tax Rebate = -\$20pw

Gain to Spouse B from no reporting Earnings = \$50.15

**EXAMPLE 3**

A spouse (Spouse A) is already working full-time and decides to place their 4 year old child in child carer (Spouse B) instead of an unpaid relative who is receiving the Family Allowance Supplement (FAS) for their own children and where a DSR for claimed Spouse B. Also, a transferable tax rebate is allowed for earnings related child care expenses.

Spouses of Spouse A and B Earn \$345.20pw

Spouse A

*Original Status*

Earning \$350pw, no child care expenses

FAS for child under 13 years = \$0.00pw

Disposable Income =  $350 - 74.14 = \$275.86pw$

*New Status*

Earning \$350pw, child care expenses \$100pw

Tax (using Table 7b) = Tax less Child Care Tax Rebate  
 $= 74.14 - 100 \times .2 = \$54.14pw$

FAS for child under 13 years = \$0pw

Disposable Income after child care =  $350 - 100 - 54.14 = 195.86pw$

*Net Change in Status after child care expenses*

From earning \$350pw, the family's after child care expenses disposable income has decreased  $\Rightarrow 275.86 - 195.86 = \$80.00pw$

Spouse B

*Original Status*

Earning no income, no child care expenses

FAS for child under 13 years = \$26.50pw

Disposable Income = \$26.50pw

*New Status*

Earning \$100pw, no child care expenses

Tax (using Table 7b) = Tax less Child Care Tax Rebate  
 $= 25.00 - 0 \times .2 = \$25.00w$

FAS for child under 13 years = \$0pw

Disposable Income after child care =  $100 - 25 = \$75.00pw$

*Net Change in Status after child care expenses*

From earning \$100pw, the family's after child care expenses disposable income has increased  $\Rightarrow 75.00 - 26.50 = \$48.50pw$

*Federal Budget position*

*Original Status*

Tax less FAS =  $0 - \$26.50 = -\$26.50pw$

*New Status*

Tax less FAS =  $(25.00 - 20.00) + \$0.00 = \$5.00pw$

**Net Fiscal Impact (Net Return to Government) \$31.50pw**



The results in the Examples above also indicate another story which should not be lost on us. This is that the DSR (as shown in Table 7b) acts as a clear disincentive for dependent spouses to enter the workforce. Combine this with the likelihood that FAS might be withdrawn as they earn more income, that medicare payments increase, and we might find that they are confronting marginal tax rates over 76% on some of their income from child caring. These high effective marginal tax rates are the reason why in the example above, the government benefited so markedly from changes to the tax treatment of child care expenses.

Let us contrast the situation discussed above with one where Spouse A is already working. The results from this case are shown in Example 3.

Again, the government gains from this possibility. Even if the child carer is not in receipt of any government benefit, the government will benefit because the DSR is withdrawn.

There are in fact few cases where the government is not a major beneficiary from allowing a 20% transferable tax rebate for child care expenses or at worst, finds its budget position little changed.

A transferable tax rebate of 20% might therefore appear as a small price for government to pay for encouraging employment in the child care industry where they ultimately will be one of the biggest beneficiaries. Some of the potential benefit to government would be offset if child care expenses were income deductible rather than attracting a transferable tax rebates at the basic rate of 20%. However, this would only be the case where the spouse whose employment is dependent on putting children in child care has earnings above \$20700pa.

#### **B. AGGREGATE RESPONSE**

The above results indicate the potential gains to the Federal government from offering a tax rebate (or income deduction) for child care expenses. There is some merit in seeking to extend this analysis in some general way into an aggregate or economy wide response. Undertaking such an approach is however, fraught with difficulties. While there has been much literature on the labour supply response of women to marginal tax rates (Apps and Savage, 1986), it is difficult transferring broad observations about labour supply elasticities to a "micro" model such as STATAx. This is because very specific information is required about the response of each household to the tax reforms.

As a consequence, the approach adopted will be to examine two broad response scenarios by households and examine what this means for the Federal Budget and for households.

#### **SCENARIO 1**

Part-time women with children less than 9 years of age, increase their hours worked by 20% and pay 25% of this increase as child care payments. This child care payment is received as a wage of \$3780pa by one out of every two female spouses who are unemployed or not in the labour force, and whose spouse is unemployed. Also, it is assumed that these people do not put their children into child care centres (and therefore, their no impact on the cost of child care fee relief). This could be effected in practice by the Federal government not increasing the number of subsidized places in child care centres.

#### **SCENARIO 2**

Assume a 10% increase in the female workforce (each receiving Full-time Female AWE of \$491.38pw) who have children less than 5 years of age (or a rise in female full-time employment of 52600). Also, assume that these employees put their children into child care centres for 50 hours (at a cost of \$100pw) and that these centres can offer child care fee relief. The child care payment is assumed to result in a wage of \$7019pa by one out of every two female spouses who are unemployed or not in the labour force, and whose spouse is unemployed.

The results from modelling these scenarios in STATAX when a capped non-transferable non-refundable system of tax rebate for child care expenses operates, is detailed in Table 9. The major virtue of "micro" models of the household sector such as STATAX is they model the household sector in considerable detail. Therefore, when for example a household's income increases, this will cause changes in their tax liability and social welfare receipts. What results in Table 9 is the very real potential for the introduction of tax concessions for child care expenses has not only to increase household's income but to yield considerable benefits to the government.

Moreover, while Table 9 illustrates just two possible scenarios, it highlights how inappropriate it would be to simply focus of the first round effects of this particular reform. Afterall, the real arguments for this reform come from the behavioural response to the changes to the tax treatment of child care.

The major cause of the big gains to government in the scenarios in Table 9 (and the examples in the previous section) is the high effective marginal tax rates (EMTR) that operate for low income families. This has been shown in the last rows of Table 9 and highlighted by our assumption about who will be the beneficiaries from the tax change. While it could be said that we have chosen the extreme case when examining who will become the "child carers", it should be noted as shown in Table 9, that the net fiscal impact is positive even if we assumed the government received no tax from the child carers (which is extremely unlikely).

**Table 9** Impact After Incorporating Behavioural Response into a Capped (\$1043pa) Non-refundable Non-Transferable Tax Rebate (at 20%) for Work-related child care expenses: 1990-91

	NO Response Case	BCC <sup>a</sup>	Scenario 1 ACC <sup>a</sup>	BCC <sup>a</sup>	Scenario 2 ACC <sup>a</sup>
<b>Factor Income</b>					
Wages and Salaries(\$m)	-	891	1113	1348	1760
Change in Total Wages and Salaries <sup>b</sup> (%)	-	0.50	0.62	0.75	0.98
<b>Federal Budget</b>					
Personal Income Tax	-86	143	162	201	240
Medicare	0	13	13	24	25
Social Welfare	0	-26	-107	-122	-365
Child Care Fee Relief	0	-6	-6	4	4
Net Fiscal Impact excluding Indirect Taxes (\$m)	-86	188	288	343	626
plus Federal Indirect Taxes <sup>c</sup>	0	70	83	100	113
<b>Net Fiscal Impact (\$m)</b>	<b>-86</b>	<b>258</b>	<b>371</b>	<b>443</b>	<b>739</b>
Effective Marginal Tax Rate (%) (excluding Federal Indirect Taxes) on Additional Private Income of:					
* Spouse working					
longer Hours		21.1	21.1	25.4	25.4
* Child carer		-	45.0	-	68.7
* Both Spouses		21.1	25.9	25.4	35.6
Effective Marginal Tax Rate (%) (including Federal Indirect Taxes) on Additional Private Income of:					
* Spouse working					
longer Hours		29.0	29.0	32.9	32.9
* Child carer		-	50.1	-	71.8
* Both Spouses		29.0	33.3	32.9	35.6

a BCC refers to the outcome before Childcaring employment effects are included and ACC refers to the situation after childcaring employment effects are included.

b Wages and Salaries in 1990-91 were \$178836m

c These results assume: a) household consume all their increase in disposable income; b) that as Warren (1991c) estimated for 1988-89, the incidence of Federal Taxes other than the personal income tax and company tax is 10% of household gross income. The results also exclude any increase in State indirect tax revenue which is most unlikely.

These results would hold true even if a system of tax deductions for child care expenses operate in place of rebates. One difference is that the cost of the income deductions would be greater to the government than the cost of a tax rebate which was set at the lowest marginal tax rate (20%). However, the tax incentive for those with children to enter the workforce would be greater under an income deduction approach and so the behavioural response could be greater, thus potentially offsetting for the government, any additional revenue lost from introducing income deductions for child care expenses in place of rebates.

## VI THE POTENTIAL INTERACTION BETWEEN TAX DEDUCTIONS, REBATES AND THE FBT PROVISIONS ON CHILD CARE

An alternative approach by government to assist with an employee's work related child care expenses is to exempt child care fringe benefits not currently exempt from FBT. The TIA proposal recommends this action as a complement to tax concessions on work-related child care fees paid directly by employees. This would mean that an employee could take part of their remuneration package as child care payments and their employer would not be levied FBT. Currently, such a situation only arises with regard to child care fringe benefits where those benefits are derived either from:

- a) an employer funded child care facility or;
- b) from the employer purchasing a block of places or paying a percent of costs, at a commercial long-day care centres which is attended by the children of the employee receiving the child care fringe benefit.

Table 10 set out information on what would be the benefit to a person who currently has their employer pay their work related child care expenses (which are currently subject to FBT) as against a situation where these fringe benefits are not subject to FBT. In this table we assume (for simplicity) that the employee pays a flat marginal tax rate (and this would not be too different from that confronting any person within some chosen income bracket). In this table it is assumed that  $t$  is the personal income tax rate,  $t_c$  is the Company Tax Rate,  $t_f$  is the fringe benefits tax rate, and  $t_r$  is the child care tax rebate rate.

The key to understanding Table 10 is understanding that the fringe benefits provided to employees are tax deductible for the employer but the Fringe Benefits Tax (FBT) paid by the employer is not tax deductible for the employer. Therefore, any employer when costing the salary equivalent to them - the employer - of a fringe benefit paid to an employee must sum the fringe benefit (FB) and the grossed-up value of the FBT paid (since the FBT is not tax deductible). The latter is equivalent to  $t_e = (t_f / (1 - t_c))$  times the fringe benefit. If the fringe benefit is FB then the wages equivalent (WE) or salary sacrifice as a result of taking the FB is:

$$WE = FB * [1 + t_e] = FB * [1 + t_f / (1 - t_c)]$$

If FB was equal to \$100,  $t_f = .4825$  and  $t_c = .39$ , the WE is \$179.10, and FBT would be 48.25. Note that if the employer were to pay the employee \$179.10 instead of the

fringe benefit of \$100, it would (since this is tax deductible in full) effectively cost the employer \$109.25. That is, paying the \$100 fringe benefit effectively costs FBT of \$48.25 and a FB cost of \$61 (or  $FB \cdot (1 - t_c)$ ), a total effective cost of \$109.25.

The effective fringe benefit tax rate ( $t_b$ ) for the employee is therefore:

$$t_b = t_e / (1 + t_e) = t_f / (1 - t_c + t_f)$$

In the example above,  $t_b$  is 44.16%. Only if the FBT rate and the company rate are the same would the FBT rate equal  $t_b$ . However, what this also implies is that for any person who has an effective marginal tax rate on the salary sacrifice (WE) due to their FB of less than 44.16%, they should not take their remuneration in the form of fringe benefits but pay for them from their disposable income.

**Table 10 Child Care Expenses paid Directly by Employer**

	FBT on Child Care	No FBT on Child Care
Total Income	$Y'$	$Y'$
Child Care Expenses	$C$	$C$
Cash Income	$Y_c = Y' - C(1 + (t_f / (1 - t_c)))$	$Y_c = Y' - C$
Taxable Income	$Y_t = Y_c$	$Y_t = Y_c$
Tax	$T = t \cdot Y_c$	$T = t \cdot Y_c$
Disposable Income		
After Child Care	$DY_a = Y_c - T$	$DY_a = Y_c - T$
or	$Y'(1 - t) - C(1 + (t_f / (1 - t_c)))(1 - t)$	$Y'(1 - t) - C(1 - t)$
Change in $DY_a$ from the Change in the Tax Treatment of Child Care or the difference	$C(1 + (t_f / (1 - t_c)))(1 - t)$ $C(t_f / (1 - t_c))(1 - t)$	$C(1 - t)$ 0
eg (\$pw)		
Total Income	600.00	600
Child Care Expenses	0	0
Cash Income	420.90	500
Taxable Income	420.90	500
Tax ( $t = .4$ , $t_c = .39$ , $t_f = .4825$ )	168.36	200
Disposable Income		
After Child Care ( $DY_a$ )	252.54	300
Change in $DY_a$ due the the Change in the tax Treatment of Child Care		
..difference	-47.46	0

Currently the FBT rate is 47% but from 1 April 1992, it will be raised to 48.25%.

Table 10 illustrate two cases where the employee has the employer pay their child care expenses. In the first column we have the current situation where the child care centre is private and the employer has no association with this centre. The employee shown in this case has a disposable income after child care expenses of \$252.54. If these child care expenses were exempt from FBT then the situation in the second column would arise and our employee would in this case have a disposable income after child care expenses of \$300.

**Table 11 Child Care Expenses Paid Directly by Employee**

	No Income Deduction for Child Care	Tax Rebate for Child Care	Income Deduction for Child Care
Total Income	$Y'$	$Y'$	$Y'$
Child Care Expenses	$C$	$C$	$C$
Cash Income	$Y_c = Y'$	$Y_c = Y'$	$Y_c = Y'$
Taxable Income	$Y_t = Y_c$	$Y_t = Y_c$	$Y_t = Y_c - C$
Tax	$T = t \cdot Y_c$	$T = t \cdot Y_c - t_r C$	$T = t \cdot (Y_c - C)$
Disposable Income After Child Care or	$DY_a = Y_c - T - C$ $Y'(1-t) - C$	$DY_a = Y_c - T - C$ $Y'(1-t) - C(1-t_r)$	$DY_a = Y_c - T - C$ $Y'(1-t) - C(1-t)$
Change in $DY_a$ due to the Change in the Tax Treatment of Child Care or the <i>difference</i>	0	$t_r C$	$t C$
eg (\$pw)			
Total Income	600	600	600
Child Care Expenses	100	100	100
Cash Income	600	600	600
Taxable Income	600	500	500
Tax ( $t=.4, t_c=.39, t_r=.2$ )	240	220	200
Disposable Income After Child Care ( $DY_a$ )	260	280	300
Change in $DY_a$ due to the Change in the tax Treatment of Child Care .. <i>difference</i>	0	+20	+40

What is apparent, not surprisingly, is that the employee gains most from a situation where there is no FBT on child care. The question now is how exempting child care expenses paid by the employer from FBT compares to other possible alternatives. Column 1 of Table 11 shows the situation where the employee pays all the child care expenses themselves and they attract no tax concession. This situation is superior to the case where FBT is imposed on

equivalent nominal child care fees paid directly by their employer. However, this is because their marginal tax rate ( $t$ ) is 40% and only if their effective marginal personal income rate on the income equivalent to their child care expenses was greater than 44.16% (as noted above), would there be any benefit to them from getting their employer to pay their child care expenses.

Table 11 also compares the two alternatives discussed in detail in earlier sections. In particular, it demonstrates the gains to employees when they are allowed a tax rebate or an income deduction for child care expenses. The choice by an employee about whether they would prefer to have their employer pay their child care expenses - whether they are free of FBT or not (Table 10) - or pay these expenses directly themselves when they are allowed as an income deduction, is very much dependent on  $t_c$ ,  $t_f$ ,  $t_r$  and  $t$ . Even assuming that  $0 < t_c, t_f, t_r < 0$ , no unambiguous preference ranking exists.

Each individual needs to examine their own situation, especially their own effective marginal tax rate  $t_b$  on the income equivalent to their child care expenses, the fringe benefit tax rate ( $t_f$ ), and the tax rebate rate ( $t_r$ ) and their own marginal tax rate ( $t$ ) and not least the company tax rate ( $t_c$ ). Some observations can however be made.

- i) An employee would not have their employer pay their child care expenses if  $t_b > t$
- ii) An employee is best off if they can claim an income deduction for their child care expenses. This is effectively equivalent to having your employer pay your child care expenses and there being no FBT on these payments.
- iii) A tax rebate is inferior to an income deduction as long as  $t > t_r$

The TIA proposal is that the introduction of tax rebate or income deductions for child care should be complemented with changes to the FBT provisions to ensure that any fringe benefits received by a parent for child care expenses are also given concessionary treatment. In the case of child care fringe benefit, this would imply that they should be exempt from FBT.

If child care expenses paid by an employer were made exempt from FBT, the effective benefit to the employee is comparable to the full income deductibility of child care expenses. This should not be seen as a cost to the Government however, since these expenses would not have been incurred if it was not for the changes to FBT on child care. In contrast, the costs shown in Table 5 for income deductibility are real costs in that they are expenses currently being incurred which will then become income deductions.

What Table 10 illustrates, is that with such a change to FBT, an employee would be indifferent between having their employer pay their child care expenses or having child care expenses income deductible. If the income deduction was capped, or tax rebates for child care expenses were introduced, incentive would then arise for employees to have their employer pay their child care expenses out of their salary package. For secondary earner, particularly those working part-

time, this may not be an option. However, it might be an option for the primary earner spouse who could have their employer pay the family's child care expenses out of their salary package.

The cost of the changes to FBT are difficult to estimate. Since it is unlikely that many employees are currently receiving child care expenses (other than those currently exempt from FBT) as part of their salary package, the initial cost of removing this tax from these payments is likely to be insignificant.

The discussion in this section leads us to conclude that the pattern of results presented in Table 9 are unlikely to be too influenced by the introduction of the TIA proposal for changes to FBT treatment of child care expenses. This is the case both for the estimates of the impact of the changes in the first round (before any behavioural response) and after any behavioural response has occurred, especially if income deductibility for child care is introduced.



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## APPENDIX A      HES 1988-89 Unit Record Data

The 1988-89 HES Unit Record Data provides detailed data on the income, expenditure and characteristics of the household sector. This survey by the ABS covers some 7225 households living in private dwellings in 1988-89 (see ABS Household Expenditure Survey 1988-89, Unit Record File on Magnetic Tape, Cat No 6544.0)

Data on income and expenditure is identified at the individual and household level. In relation to the TIA study, data is reported on three categories of child care:

a)      Child Care Service - Institutional (HES Code 417)

Includes:

- Child Care Centre fees
- Creche fees
- Fees (Child Care centre)
- Fees (Kindergarten)
- Fees (Nursery)
- Fees (pre-school)
- Kindergarten Fees
- Nursery Fees
- Playgroup fees (institution)
- Pre-School Fees

b)      Child Care Service - nec (HES Code 418)

Includes:

- Baby sitting fees (paid to a person)
- Child carer (person)
- Fees (baby sitter)
- Playgroup fees (nec and undefined)

c)      Child Care Service - undefined (HES Code 419)

Includes:

- Child care services undefined

The data reported in HES clearly identifies the broad range of child care options available to parents. The problem for this study of the TIA proposal, was to identify those child care expenses which are paid at a child care centre offering fee relief under the current system, and secondly, to determine what child care expenses are of parents could potentially attract a tax concession under the TIA proposals.

The first step was to determine approximately, what proportion of the fees reported in HES can be attributed to fees paid at a child care centre which offers child care fee relief. The approach adopted was to first assume that any child care fees paid to a child care centre (HES code 417) could potentially attract fee relief. This meant that any attempt at modelling the current system of child care assistance must be focused solely on the use of HES code 417.

Secondly, it was assumed that while the fees included in HES code 417 include fees other than those paid to centres which could offer fee relief, the modelling of the current fee relief system (detailed in Appendix B) will ensure that expenditure by spouses not in the labour force on say creches, is excluded. That is, the application of the work test (or seeking work test) to the two spouses or the sole parent, will minimize errors in modelling the current system.

Having determined who the persons are in HES (with the data adjusted to 1990-91 values and population weights) that pay child care fees to centres (HES code 417), we then determine the fees they should be paying (as detailed in Appendix B) at the child care centre assuming this centre can offer fee relief. Only those income units with children less than five years of age are considered. This estimate of child care fees is then compared with what is reported in HES and used to determine the number of hours that the children are in long day care. If the amount paid in child care fees is greater than the total fees due given the family income and number of children in care, it is assumed that this is because they pay an hourly rate greater than the rate at which child care relief is calculated (currently \$2.00 per hour).

Using this approach, we obtain an estimate of the cost of child care fee relief of \$148.4m.

## APPENDIX B      Child Care Fee Relief Scheme\*

### 1. CHILD CARE FEE RELIEF SYSTEM BEFORE JANUARY 1992

At the present moment AFI is \$369pw. This is estimated as Gross income per week less \$30pw per child.

i Two levels of care currently operate.

a) Long Day Care Fee Relief: Calculating the fees that a family pay at a long day care where fee relief is offered is reasonably complex and undertaken by DSS. There are various steps involved. The basic task is to gauge what fee a family will have to pay per hour for long day child care.

Step 1: Ascertain the family's Assessed Family Income (AFI) per week and the number of children. AFI is measured as gross family income less \$30per child.

Step 2: Determine the number of hours the child will spend at the long day care centre( $H_0$ ) and the rate charged per hour ( $R_0$ ).

Step 3: If the hourly rate charged ( $R_0$ ) is greater than \$2.00ph, subtract the hourly rate from the government approved hourly rate for child care services ( $R_1$  which is currently \$2.00 per hour). The difference must be paid directly by the family (ie  $CA=(R_1-R_0)*H_0$ )

Step 4: Assume now that the child spends 50hrs in long day child care (ie 8am-6pm). The maximum long day care fee in this case is \$100pw ( $R_1*50$ hrs).

Step 5: Subtract the estimate of AFI (Step 1) from \$369pw. The child care fees (out of the maximum \$100pw) to be paid by the family is \$15pw with one child and \$17 with two or more children, plus 12c in the dollar of AFI over \$369pw for one child and 20c when there are 2 or more children.

Step 6: Calculate the proportion of the child care fees paid by the family relative to the \$100pw.

Step 7: Use this proportion to calculate the share of  $R_1$  (the \$2.00ph child care fees) that the parents will pay (and define this as  $R_2$ ).

Step 8: Calculate the child care fee to be paid by the parent as  $CB=R_2*H_0$ . The government will pay the difference between what the parents pay ( $CB$ ) and the government approved fee ( $R_1*H_0$ ). The amount paid by the government is termed FEE RELIEF

Step 9: Calculate the per week child care fee that is to be paid by the parent as  $CC=CA+CB$ .

eg One child is in long day care for 20hrs pw, the family's AFI is \$369pw, they have one child and pay \$2.00ph. The child care fee they pay is \$6.00pw.

b) Outside School Care: Available at two levels (i) Full relief at 64c per hour and (ii) partial relief at 32c per hour. Very few take up this scheme as it is only available to pensioners, beneficiaries and FAS recipients and because the amount is so small, take-up is low - that is, the scheme is fairly ineffectual.

## **ii Access to Child Care Fee Relief in Long Day Care**

Access to child care fee relief is not only based on income but on the family's priority ranking. These are as follows:

Priority 1 - Working Parents (FT/PT); One parent working(FT/PT) and the other actively looking for work; both parents actively looking for work; one parent working(FT/PT) and the other studying.

Priority 2 - Parent or child with a disability

Priority 3 - Child at risk of Child abuse

Priority 4 - One Parent at home

## **iii Child Care Places**

The child care fee relief system is operated jointly by the Department of Social Security (DSS) and the Department of Health Housing and Community Services (DHHCS). The DHHCS determines, based on funding, which areas are to have offered child care places on which fee relief is to be made available. These child care places are, by various mechanisms, allocated to selected centre. Once these places have been allocated to a centre, the centre will request those parents who are eligible for fee relief, to go to DSS and be assessed for their child care fee relief (using the approach outlined above). The DSS will then notify the parents and the child care centre of the fee relief to be paid by DHHCS. Parents must notify the DSS of any increase or decrease of 25% in their gross income, in which case their child care fee relief will be reassessed.

Prior to January 1991, fee relief was available only to non-profit child care centres only. Once these centres were allocated a certain number of equivalent full-time places, they would receive in advance from DHHCS, an amount equivalent to the number of equivalent full-time places funded over 13 week. Initially, this would be at the State average amount of child care fee relief (which was \$38pw per full-time child in NSW before January 1991). Any short fall or excess is adjusted when further payments are made for the next 13 week payment period. These advances may be incorrect because when the places are made available by DHHCS, it does not know the Department of Social Security (DSS) assessment of the child care fee relief going to the various parents.

Since January 1991, commercial operators of child care centres have been eligible for child care fee relief. Since then the average amount of child care fee relief in NSW per equivalent full-time child is \$58 per week. While non-profit child care centres are also eligible for government grants other than for fee relief, such grants are not available to commercial child care centres.

## 2. CHILD CARE FEE RELIEF SYSTEM BETWEEN 1 JANUARY 1992 AND 31 MARCH 1992

Extensive changes are to be made to the system of fee relief, particularly to outside school hours care (OSHC). These are detailed below:

### **i Two levels of care will again operate but with major changes to the second level.**

a) Long Day Care Fee Relief: As prior to 1 January 1992 and shown above.

b) Outside School Hours Care (OSHC): This system has been extensively restructured. Fee relief in this case is based on a 55% rule. That is, the DHHCS will pay 55% of a scheduled hourly rate. At present they assume a child care hourly rate of \$2.00 as for long day care centres. The only difference with the approach outlined above with respect to long day care is that Step 5 now becomes:

Step 5: Take the estimates of AFI from \$369pw. The child care fees (out of \$100pw) paid by the family is 45% plus 12c in the dollar of AFI over \$369pw for one child and 20c when there are 2 or more children.

The OSHC scheme therefore operates on the basis of a sharing of the child care expenses with the maximum contribution by government of 55%.

### **ii Access to Child Care Fee Relief in Long Day Care**

Access to child care fee relief is not only based on income but a persons priority ranking. The priority classification scheme is changed to the following categories:

a) New Priority 1 - This now includes the previous Priorities 1, 2 and 3. That is, Working Parents (FT/PT); One parent working(FT/PT) and the other actively looking for work; both parents actively looking for work; one parent working(FT/PT) and the other studying; Parent or child with a disability; Child at risk of Child abuse.

b) New Priority 2 - Old priority 4 ie children in families with one parent at home

## 3. CHILD CARE FEE RELIEF SYSTEM AFTER 1 APRIL 1992

The same structure as operated between January and March 1992 except that the rates and amounts have been indexed and the threshold made consistent with

that operating user the Family Allowance Scheme (FAS). This will result in the hourly child care fee being increased to \$2.06, the withdrawal rates for the child fee relief subsidy being increased from 12% and 20% to 12.4% and 20.6%, and the AFI threshold being raised from \$369pw to \$382pw in line with the FAS threshold.

\* I would like to thank Michael Dooley in the Department of Health, Housing and Community Services, Sydney for assistance is providing this brief overview of the current system.

## APPENDIX C      Child Care Fee Relief: Cost to the Federal Government

Detailed below is the cost of child care fee relief since 1989-90. The bracketed items for 1990-91 are some \$70m less than a full year due to a change in the Federal Government's timing of the payment to child care centres. To provide a number comparable in aggregate to other years, we have taken the numbers in the 1990-91 Budget Paper No 1 (p 3.153) for 1989-90 and 1991-91 created a new figure for 1990-91 as shown.

### C.1 Child Care: Outlay by Funding Type

	1989-90	1990-91		1991-92 estim	1992-93 estim
Child Care Fee Relief					
a) Long Day Care					
- Non Profit	91.4	144.4	(109.0)	149.6	161.9
- Commercial	0	29.8	(28.2)	58.9	61.6
b) Other (OSHC)	5.3	6.9	(5.4)	14.6	22.7
Operational Subsidy	82.5	89.6	(65.2)	89.8	94.4
Capital Equipment	7.3	13.5	(5.7)	10.2	10.7
Other	28.5	34.0	(34.5)	52.1	59.7
<b>Total</b>	<b>215.0</b>	<b>315.7</b>	<b>(245.7)</b>	<b>375.3</b>	<b>411.0</b>



# APPENDIX D Groups Identified in Tables

	CODE	DESCRIPTION
1	M1WK=0	HEAD W&S FT, Married, SNW, K=0
2	M1WK>0	HEAD W&S FT, Married, SNW, K>0
3	M2WK=0	HEAD W&S FT, Married, SW, K=0
4	M2WK>0	HEAD W&S FT, Married, SW, K>0
5	SWFT	HEAD W&S FT, Single
6	SMWPT	HEAD W&S PT, Single or Married
7	SE	HEAD Self Employed but not Farmer
8	FARMER	Head Farmer
9	UB/SB	Head UB/SB
10	MCNGBNI	Head NILF Married, Prininc not GB and not IDRS
11	MNGB	Head NILF Married, Prininc GB
12	SNGBNSP	Head NILF Single, Prininc GB but not SP/W
13	SNGBSP	Head NILF Single, Prininc GB, SP/W
14	NIDRS	Head NILF Prininc IDRS

Note: The descriptions above relate to the head of the household. It is possible that while the head does not have children, there could be other persons in the household who do have children. Also, in those groups where no clear statement about the number of children is made (Groups 5 through to 14), these households may or may not have children.

## Description of Codes

Head	Head of Household
W&S	Wage and Salary Earner
FT	Full Time
PT	Part Time
SW	Spouse Working
SNW	Spouse Not Working
Single	Head of Household is a single person
Married	Head of Household is a single person
UB/SB	Unemployment and Sickness Benefits
NILF	Not in the Labour Force
IDRS	Interest Dividends Rent and Superannuation
Prininc	Principal Source of Income
SP/W	Sole Parent and Widow's Pension
GB	Government Benefits and Pensions
Not GB	Not Government Benefits and Pensions
Farmer	Head is a Farmer
K=0	No Dependents
K>0	Number of Dependents greater than zero
Dependent	A person dependent on another and less than 24 years of age

**TABLE D.1 NUMBER AND INCOME IN EACH HOUSEHOLD GROUPS IN 1990-91**

	HOUSEHOLD GROUPS													
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
	M1WK=0	M1WK>0	M2WK=0	M2WK>0	SWFT	SMWPT	SE	FARMER	UB/SB	MCNGBNI	MNGB	SNGNSP	SNGBSP	NIDRS
GROUP														
DECILES														
	HOUSEHOLD INCOME (\$PW)													
1	381.22	408.04	509.41	581.67	332.13	192.23	-74.41	39.89	91.66	167.99	202.30	130.99	137.79	34.06
2	442.85	499.36	761.56	752.03	444.09	282.36	250.20	86.96	157.98	442.65	248.78	148.45	157.09	164.24
3	491.33	556.23	878.70	843.17	505.15	370.01	374.65	117.63	199.41	541.72	256.26	150.40	191.61	240.78
4	556.36	614.76	968.44	926.48	563.90	435.58	467.74	138.16	254.09	625.63	266.29	157.01	199.89	290.58
5	624.58	689.51	1062.96	1018.52	626.09	521.01	583.05	160.76	285.48	684.07	279.94	167.50	220.14	345.18
6	755.46	762.68	1154.41	1108.07	703.78	617.93	690.67	181.38	323.08	769.16	297.53	183.49	240.29	385.79
7	872.46	855.17	1243.14	1217.44	815.30	728.39	794.00	208.32	361.00	855.10	317.54	219.69	258.36	453.63
8	1030.08	971.44	1348.87	1358.33	999.06	856.15	938.01	245.38	447.44	991.96	343.29	295.03	279.34	561.05
9	1306.02	1156.66	1509.09	1567.06	1203.83	1105.72	1191.96	303.13	600.07	1180.91	384.69	470.13	318.72	746.07
10	2303.70	1931.97	2137.34	2321.50	1764.31	2449.99	1995.34	484.77	1106.05	1825.59	559.81	881.01	446.28	1359.02
ALL	847.39	836.86	1150.44	1169.15	794.15	767.32	719.66	195.79	381.48	796.09	313.49	279.80	243.30	456.52
	NUMBER OF HOUSEHOLDS IN EACH GROUP (000s)													
	149.7	637.5	313.5	941.9	766.8	255.6	455.2	303.2	271.8	173.8	527.1	690.4	178.6	292.1