Tax credits vs. direct funding: What's best for child care? [1]

This election, the parties are proposing different policies for child care. We explore the pros and cons of each.
Author: Cleveland, Gordon
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Justin Trudeau's Liberals are rolling out what would be an historic investment of $30 billion over 5 years where provinces will directly fund child care services to bring the fees down to $10 a day per child. Jagmeet Singh and the NDP support this approach. But Erin O'Toole's Conservatives want to make child care affordable by giving parents tax credits instead.

So, what are the pros and cons?

Tax credits can start money flowing by next year to parents who currently use any type of paid child care to support parental employment. You would be able to claim up to $8,000 of your annual spending for a tax credit. And, as long as your family income is less than $150,000, you'll get some money back. For really low-income families (less than $30,000), you would get 75% of the $8,000 back. For families earning $120,000, you would get 57% back. And so on. On balance, most families would be a bit better off, but some would be worse off.

Compare that to the **direct funding option** initiated by the Liberals and supported by the NDP. The federal government will deliver money to the provinces so that they can directly fund licensed child care centres and family homes. This will allow child care services to lower their fees to parents – cutting them in half by the end of next year and dropping them to $10 a day per child by 2025.

This "direct funding" option is much more generous.

The Conservative tax credit option is likely to provide, on balance, a few thousand dollars to families to help them afford child care. In provinces where the cost of child care is currently $50 or $60 a day, the Liberal and NDP direct funding option will provide a benefit of $10,000 or more to improve child care affordability. You can see the difference in the overall cost of the programs. Erin O'Toole's program will cost somewhere around $1 billion a year to the federal government; the direct funding plan will level out at $9.2 billion per year after 2025.

There are major pros and cons in how these two options work, not just in their level of generosity.

- Tax credits cover ANY kind of paid child care that supports parental employment. It could be licensed child care in a centre or home, but it could be an unlicensed neighbourhood sitter or a nanny or care provided by a relative if that relative is paid. So tax credits offer less opportunity to influence the quality of services.
- Tax credits do nothing directly to expand the amount of child care available. Most parents prefer licensed regulated child care services and space shortages are well documented. To address this, the direct funding agreements signed with the provinces and territories commit them to expanding the number of licensed spaces available for families.
- In Quebec, tax credits have been associated with the expansion of for-profit child care facilities. Studies of child care quality in Quebec have found that these new facilities are of much lower quality than the not-for-profit facilities that are directly funded in that province. Lower quality means these facilities are less safe, and less likely to help children get the best start possible.
- Countries, such as Australia and the U.K., that use different forms of child care tax credits, have found that increased funding for parents leads shortly after to increased fees for child care, so the impact of the tax credits on child care affordability diminishes over time.
- Broadly, tax credits support a market approach to the provision of child care services, where providers are free to enter and leave the market, free to charge whatever the market will bear, and where service quality is not strongly regulated or monitored.
- Broadly, direct funding of child care services support a public service approach to the provision of child care services, where maximum fees are controlled, where compensation of staff is enhanced to improve service quality and promote pay equity, and where innovations to support the special needs of children and families (e.g., rural families, families working shifts) are encouraged as a matter of public policy. Even though parents are expected to pay $10 a day per child, and services are offered by private non-profit providers, a direct funding approach is similar in other ways to public kindergarten – a public, regulated, high-quality service.
- However, direct funding of child care services cannot make licensed child care available for all families immediately. There will be several years over which the supply of services is rapidly ramped up to meet demand. Some families will have to continue to to be…

patient, which can be frustrating.
- Only licensed services are supported by direct funding, primarily because it is possible to monitor and support quality in licensed services. Across Canada right now, licensed services are the choice of well over half of all children 0-5 years of age who use any kind of non-parental care. In other words, well over half of the families who currently use child care will benefit by the end of 2022 when fees are cut in half. Fewer than 20% are currently cared for by informal neighbourhood sitters. These children could benefit from the tax credit but would have to move to licensed services to benefit from direct funding.

What's the takeaway?

In sum: If you want to use informal unlicensed child care and you want to get a small amount of financial assistance immediately, the tax credit might be your choice.

If you prefer using licensed child care services and want child care to become a well-funded dependable and affordable service, including for those who follow in your footsteps, then you would opt for direct funding. Not everyone will benefit immediately from the direct funding option, but many, many families will benefit now, and the supply of services will ramp up quickly.

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