

# The cost and impact of different funding approaches to increase ECEC sector wages

Report for the Australian Childcare Alliance

June 2023

# Introduction

The Australian Childcare Alliance (ACA) is seeking to understand the cost and implications of different options for increasing the wages of teachers and educators.

## Background

Current wage rates for early childhood teachers and educators are considered a significant barrier to workforce attraction and retention. This is reflected in the National Workforce Strategy and in research on the drivers of workforce attraction and retention in ECEC.<sup>1</sup> In the wake of the COVID-19 pandemic, workforce shortages have become acute. Peaks, providers and unions are all calling for significant wage increases.

While there is broad support for a wage increase, the cost of the increase either needs to be borne by government, providers or families (or a combination of all three). The best approach to implement a government funded wage increase is unclear. There are several ways government could fund a wage increase, but they come with trade-offs.

## This Project

The Australian Childcare Alliance (ACA) commissioned dandolopartners (dandolo) to analyse the options and implications of different approaches to increasing wages. In this report we:

- Calculate the total cost of a wage increase
- Develop and refine approaches to implementing a wage increase
- Undertake an analysis of the relative efficiency and impact of these approaches on families, providers and the ECEC workforce.

We have used 15% as a benchmark for the worked examples shown in our report.

# This report

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<sup>1</sup> McDonald, Thorpe and Irvine (2018), Low Pay but Still We Stay: Retention in Early Childhood Education and Care, *Journal of Industrial Relations* 60(5); Irvine et al (2016), *Money, Love and Identity: Initial findings from the National ECEC Workforce Study*. Summary report from the National ECEC Workforce Development Policy Workshop; Future Tracks (2019), *Upskilling in Early Childhood Education: Opportunities for the Current Workforce*, prepared by dandolopartners

# Executive summary

# The expected cost of a wage increase

There is pressure to increase ECEC wages. We estimate that the total cost of a 15% wage increase would be between \$0.9 billion and \$1.3 billion.

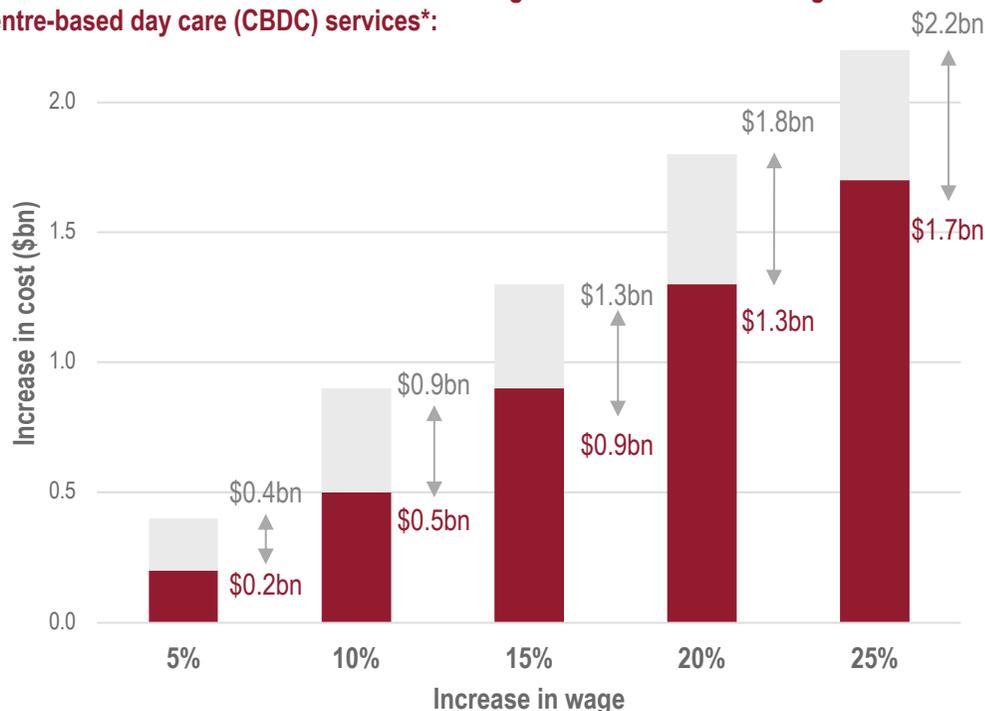
**Current wages and workforce shortages in the early childhood education and care (ECEC) sector have led to calls to increase wages.**

Current wage rates for early childhood teachers and educators are considered to be a significant barrier to workforce attraction and retention. Workforce shortages have become acute with:

- An average 9% of services operating with a Staffing Waiver, reaching nearly 16% in WA;
- Job vacancies doubling since 2019; and
- Providers reporting significant challenges recruiting and retaining staff, to the point of rooms closing and restrictions on enrolling new children<sup>1</sup>.

Peaks, providers and unions are all calling for significant wage increases, as evidenced in their joint support of the first ever application for a supported bargaining authorisation, which will enable negotiations for wage increases for the ECEC sector.

**We estimated the total annual cost of increasing teacher and educator wages in centre-based day care (CBDC) services\*:**



The *higher cost* assumes all teachers and educators receive an equivalent percentage wage increase.

The *lower cost* assumes there is an increase to the award rate. Therefore, only those at award, or below the new award increase, will see an increase in their wage.

If wages increased by 15%, we estimate that the total cost would be between \$0.9 billion and \$1.3 billion. The lower estimate is if there is an increase to the *minimum* rate, while the higher estimate is an increase to all teachers and educators, including those already paid above award.

On average, this is an additional \$150,000 per service, or an investment of nearly \$1,600 per child.

\* We used CBDC workforce data to represent CCS-funded services.

<sup>1</sup> ACECQA, *National Snapshot Q4 2022*; ACA (2022), *Resolving the educator shortage crisis*; ELAA, CELA and CCC (2022), *Investing in our future: Growing the education and care workforce*

# Impact of an unfunded wage increase

If services increase fees to cover an unfunded wage increase, fees could increase by \$10-\$15 a day. Some families will face higher out-of-pocket costs than others.

## An increase in the daily average fee for families will vary across services

We estimate an average 11% fee increase to cover a 15% wage increase.\*

### Jurisdiction

There is an increase of between \$12 and \$15 dollars a day in the ACT, Victoria, WA, SA and NSW. Even in low-fee Tasmania, the increase is up to \$10 a day.

### Regionality

Families living in major cities will see the highest increase in fees.

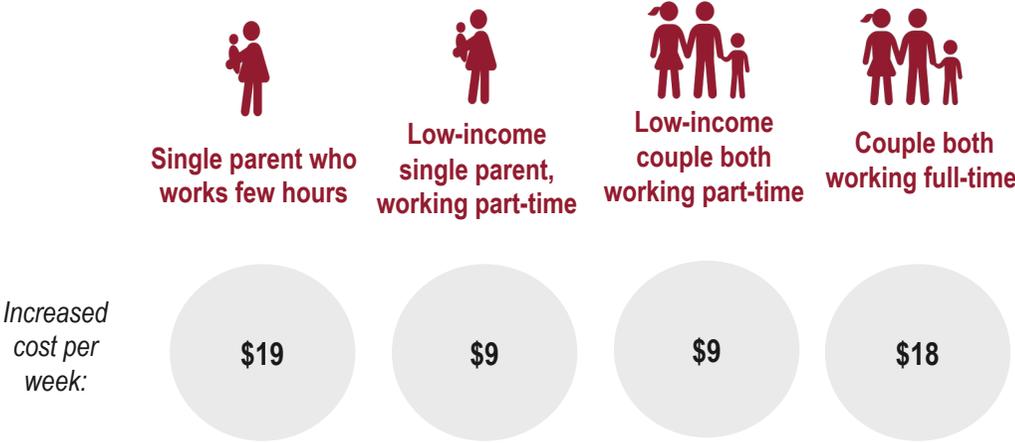
### Socio-economic status

The fee increase will be largest in higher socio-economic areas.

## Impacts on actual out-of-pocket costs for families will depend on their circumstances (income, activity levels and fees charged).

Assuming families access 3 days a week of ECEC, we estimate out-of-pocket costs could increase **on average** by between \$9 and \$19 per week (following an 11% increase in fees and assuming the post June 2023 CCS settings apply).

If services have higher employment costs, they will need to increase their revenue by more and out-of-pocket costs could be considerably higher.



\*To cover the cost of an unfunded 15% wage increase, we assume that the **average service** would increase their fees by 11%. This represents the increase in revenue needed for a service with median employment costs (i.e. wages represent 70% of total costs).

# Options for a funded wage increase

We considered two approaches to fund a wage increase. We measured the approaches against two criteria.

The two approaches we analysed were:



## Direct wage subsidy

The actual cost to services of the increase in wages would be met by a direct government subsidy – with an expectation this is passed on in full to employees.

*Page 15*



## Hourly Rate Cap increase

A wage increase would be built into the existing system through a percentage increase in the Hourly Rate Cap (HRC), which would flow through to services as an increase in revenue.

*Page 16*

For each approach, we considered:



Efficiency of administration and implementation



Impacts for families, services, and the workforce

*Pages 17-24*

# Direct wage subsidy

A wage subsidy is more costly and administratively burdensome but is otherwise efficient to operate. It results in no additional out-of-pocket costs to families, supports service viability and promotes attraction and retention of the workforce.

## Efficiency



### Administrative cost

Moderate

The administrative costs of a direct wage subsidy are considerably higher than an HRC change.

- **For government:** A wage subsidy requires the development and operation of a new system for processing payments to services. Using the cost of administering JobKeeper as a proxy, the administrative cost of a wage subsidy would be around \$7.5m annually.<sup>1</sup> This is less than 1% of the total CCS cost, but considerably more than an HRC increase.
- **For providers:** There is also an administrative burden for providers in managing and documenting the subsidy.



### 'Leakage' of money through the system

Low

'Leakage' refers to inefficient movement of money through the system. In this context it captures the dual risks of providers using the increased revenue for something other than wages, and of government needing to spend more than is strictly needed.

Because a direct wage subsidy can be designed with high requirements for evidence and audit, there are strong mechanisms for ensuring:

- Any investment in wages is passed directly to employees
- No excessive / unnecessary funding is provided.



### Risk of fraud

Low

A wage subsidy can be designed with strong accountability mechanisms, including evidence requirements and routine auditing. This means the risk of fraud is low.

## Impact



### Families

Positive

There is no risk of increased out-of-pocket costs for families, as the increased cost of delivery is met through the wage subsidy.

There are potential positive impacts for families, if services are no longer closing rooms and restricting numbers. Continuity of teacher / educator relationships is also important for children's wellbeing and learning.



### Service viability

Positive

Risks to service viability are significantly mitigated. There are unlikely to be differential effects on providers with different operating models. For example, services that have comparatively high wages bills because they staff over-ratio, already pay above-Award or hire more qualified teachers and educators would not be penalised.



### Workforce

Positive

A wage subsidy is more likely to guarantee all teachers and educators benefit from a wage increase.

Wages are important for workforce wellbeing and recognition, and will contribute to attraction and retention in the workforce. Higher wages will contribute to a more professional and high-quality workforce.

<sup>1</sup> The ANAO reports that the total cost of administering JobKeeper was \$286m. This is the equivalent of \$63 per worker per year, applied to the nearly 120,000 CBDC workers with an ECEC qualification.

# Increasing the HRC

Increasing the HRC is comparatively easy to implement, but its effects are highly variable, inequitable and inefficient.

## Efficiency

 **Administrative cost** **Low**

The administrative cost of an HRC increase is relatively low, because it leverages existing features of the CCS system.

- **For government:** There are establishment costs for government in processing a change to the Minister's Rules and changing CCS ITS settings, but these are likely to be able to be absorbed within existing resourcing. The largest cost is likely to be in communicating the change to families. There are no ongoing administrative costs.
- **For providers:** There are no establishment or ongoing costs for providers, beyond supporting communication of the change to families.

 **'Leakage' of money through the system** **High**

'Leakage' refers to inefficient movement of money through the system – and in this context, captures the dual risks of providers using the increased revenue for something other than wages, and of government needing to spend more than is strictly needed.

The risk of leakage is high because:

- There are no mechanisms to ensure increased revenue is directed to wages. This risk would be mitigated if enforceable industrial agreement compelled high wages.
- It is likely that government expenditure will be more than is required to meet the wage increase. As the analysis on page 21 highlights, a 15% wage increase could require a 25% increase in the HRC to ensure that the services that can increase fees are able to increase revenue sufficiently. Services who cannot increase fees cannot capitalise on the increase in HRC.

 **Risk of fraud** **Low**

The risk of deliberate fraud is not high. However, as noted previously, this mechanism does not ensure that wage increases are passed on to the workforce.

## Impact

 **Families** **Negative**

The only way in which an HRC increase leads to increased revenue for services is via a fee increase. Although families will not bear the full cost of the increase, this mechanism does result in higher out-of-pocket costs.

The magnitude of the increase depends on:

- How much subsidy a family is eligible for – but families on lower subsidy rates are the most exposed (i.e. those who receive less than 50% subsidy).
- How much fees increase by and how close their current fees are to the HRC.

 **Service viability** **Variable**

There is significant variability in operating models in the ECEC sector and an HRC increase will not have a consistent effect across the whole sector as a result. Our analysis shows that:

- Services unable to increase fees do not benefit at all from an HRC increase
- Services with high employment costs (as a proportion of total costs) are the most exposed
- Services with low employment costs (as a proportion of total costs) *and* the ability to increase fees are likely to experience substantial windfall gains.

 **Workforce** **Variable**

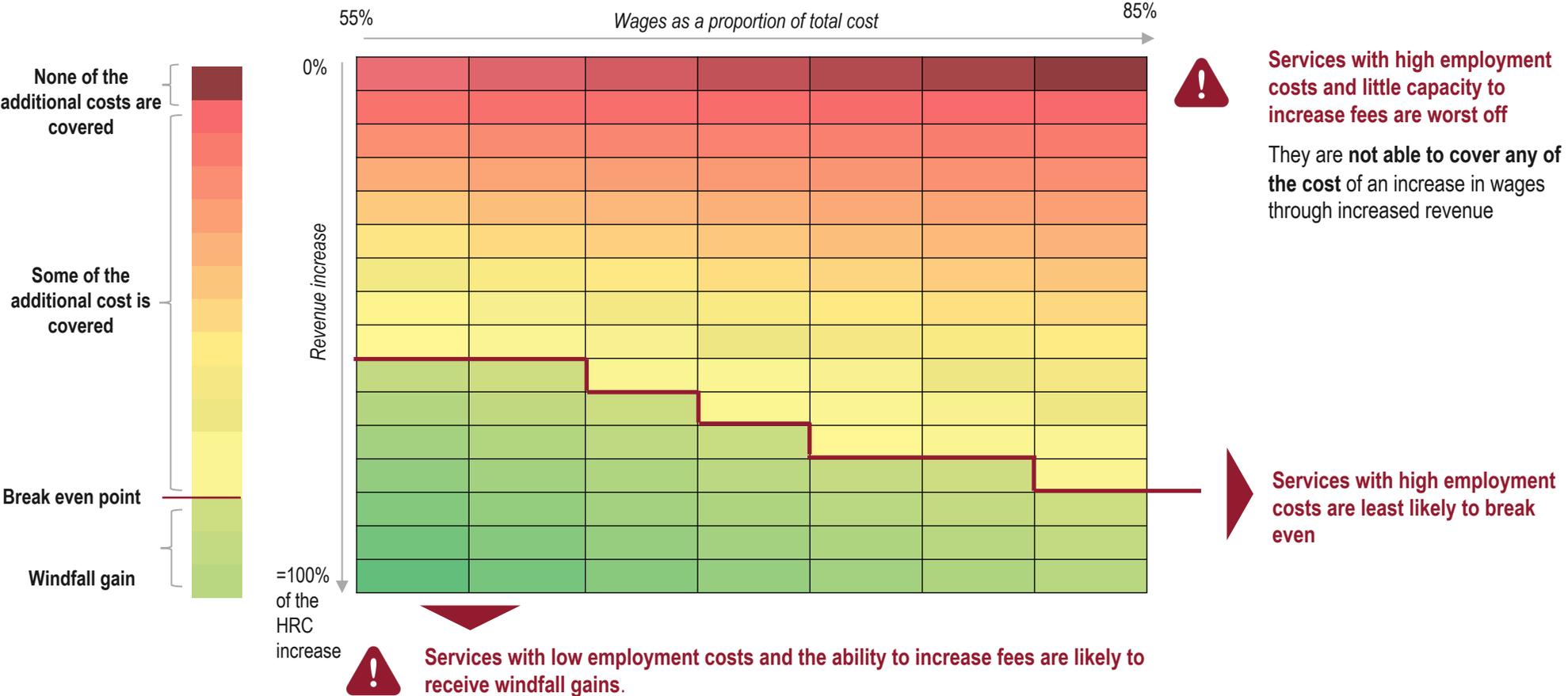
An HRC increase does not ensure or enable all services to increase wages. Some employees will benefit, but services that are already investing significantly in their workforce are the most disadvantaged by an HRC increase.

# Adequacy of an HRC increase

An HRC increase has highly variable and inequitable effects. Services with higher employment costs and limited ability to increase fees are significantly exposed, while others are likely to benefit from windfall gains.

We modelled the circumstances in which an HRC increase will allow services to increase their revenue enough to meet the cost of a wage increase. The model assumes the HRC increase matches the wage increase and takes into account the two key variables that influence whether or not services will break even – their ability to increase fees and whether they have high or low employment cost.

This heat map shows how much of the total cost of a wage increase is covered by an equivalent increase in the Hourly Rate Cap



Services with low employment costs and the ability to increase fees are likely to receive windfall gains. They will receive **more than enough revenue** to cover the increased costs.

Services with high employment costs and little capacity to increase fees are worst off. They are **not able to cover any of the cost** of an increase in wages through increased revenue.

Services with high employment costs are least likely to break even.

Note: We do not have data on the number of services in each of these scenarios and therefore cannot estimate the proportion of services likely to be out of pocket. For the purpose of this model, we have assumed an equal distribution of services into each category.

# The cost and implications of a wage increase

# Calculating the cost of a wage increase

We matched the CBDC workforce with wages and costs and applied two approaches to estimate the costs of a wage increase.

To estimate the total investment required to deliver the wage increase, we:



## 1. Built a profile of the CBDC workforce\*

This included a breakdown by:

- Jurisdiction
- Qualification and experience levels\*\*
- Employment status (full-time, part-time, casual)\*\*
- Employees paid at or above Award level.\*\*

## 2. Matched workforce profile with average wage rates and costs

This included the direct costs associated with a wage increase:

- Payroll
- Superannuation
- Long service leave loadings
- Workers' compensation

## 3. Applied a proportionate wage increase

For this we considered two options:

- All teachers and educators wages are increased by the same amount: for example, all wages increase by 15%, including the workforce already paid above Award.
- Lifting the award rates so that workers paid at Award rates see an increase, but those already paid above Award remain at their current wage.

## Estimated the total cost of the wage increase

The total cost of a wage increase will depend on the size of the increase. We modelled a range of wage increases, from 5% to 25%

See Appendix 1 for a full explanation of the methodology

\* We used CBDC workforce data to represent CCS-funded services.

\*\*Due to data restrictions, we assumed equivalent breakdown of these factors within each jurisdiction. Therefore, our analysis will not reflect any jurisdiction-based variability in these factors.

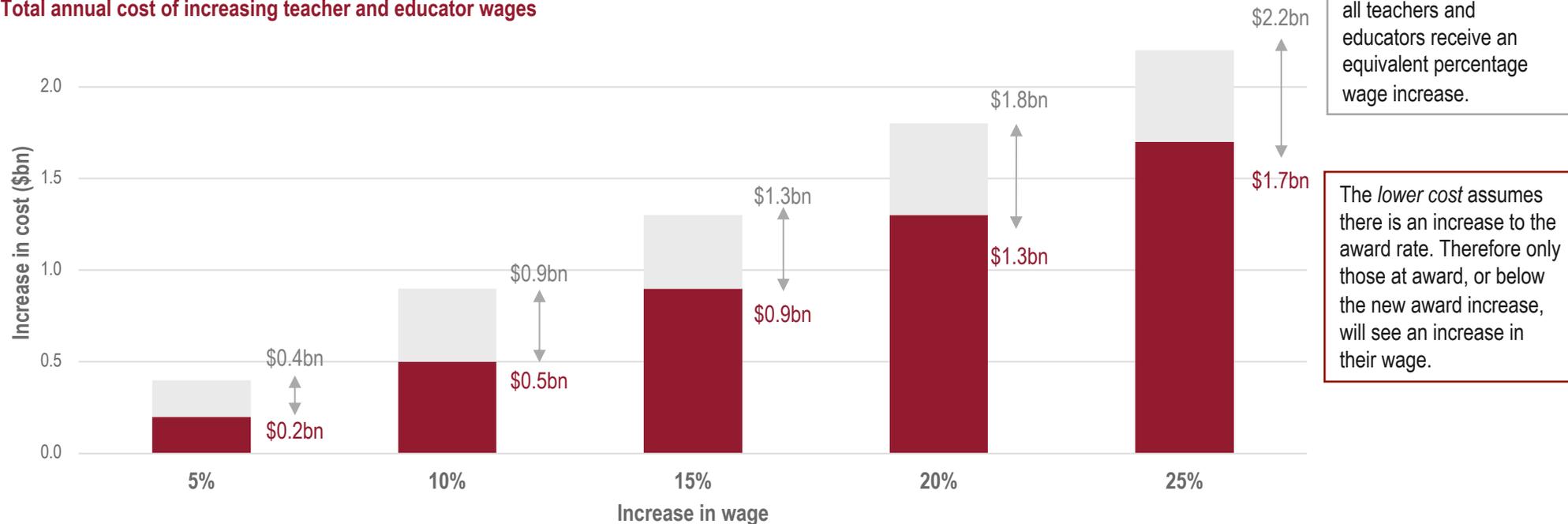
# The cost of a wage increase

We estimate that a cost of a 15% wage increase ranges from \$0.9 billion to \$1.3 billion. This represents 7-11% of the current expenditure on the CCS.

Our estimate of the total cost of a wage increase includes all teachers and educators currently employed in centre-based day care (CBDC) services, and includes the total employment cost (wages, superannuation, payroll tax where relevant, and long service leave loadings).

We test two different scenarios – an ‘across the board’ increase that lifts wages for all employees, and a more conservative increase in award rates only.

## Total annual cost of increasing teacher and educator wages



# Impact on fees

If a wage increase is unfunded, services will likely need to increase fees to cover the increased cost of delivery. Families living in major cities and in higher socio-economic areas would be most affected.

To fund the cost of a wage increase, services will need to increase their fees

Cost of delivery increases

Wages are the single largest cost category for services. If a wage increase is unfunded, the cost of delivery will increase substantially.

To meet this cost, services have three options:

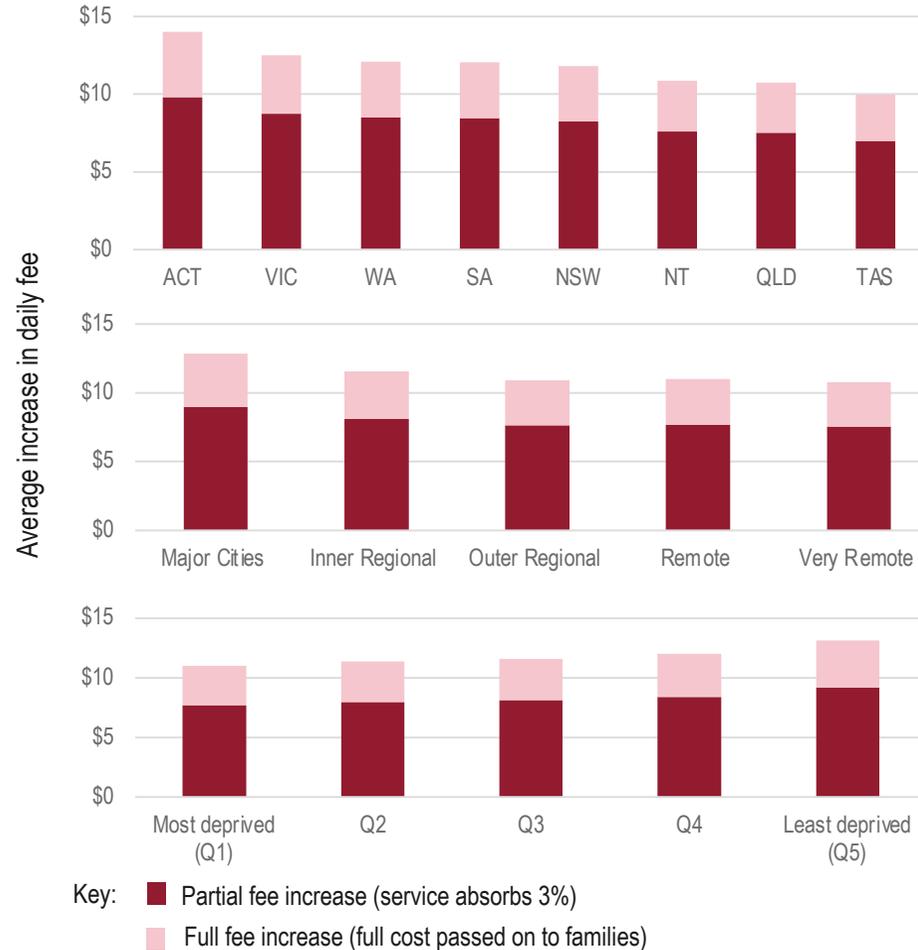
1. Absorb all the increased cost
2. Increase fees to cover the cost
3. A mix – absorbing some of the cost, and covering the rest through increased fees. Given operating margins are generally modest, we estimate that a maximum of 3% of the cost would be absorbed

We test the second and third scenarios to show the average size of the fee increase

Services need to increase revenue

Increase in fees for families

All fees will go up, but with greater impacts in some areas and contexts. For example, if fees increased by 11%...



There is an increase of up to \$12 to \$15 dollars a day in the ACT, Victoria, WA, SA and NSW. Even in low-fee Tasmania, the increase is up to \$10 a day.

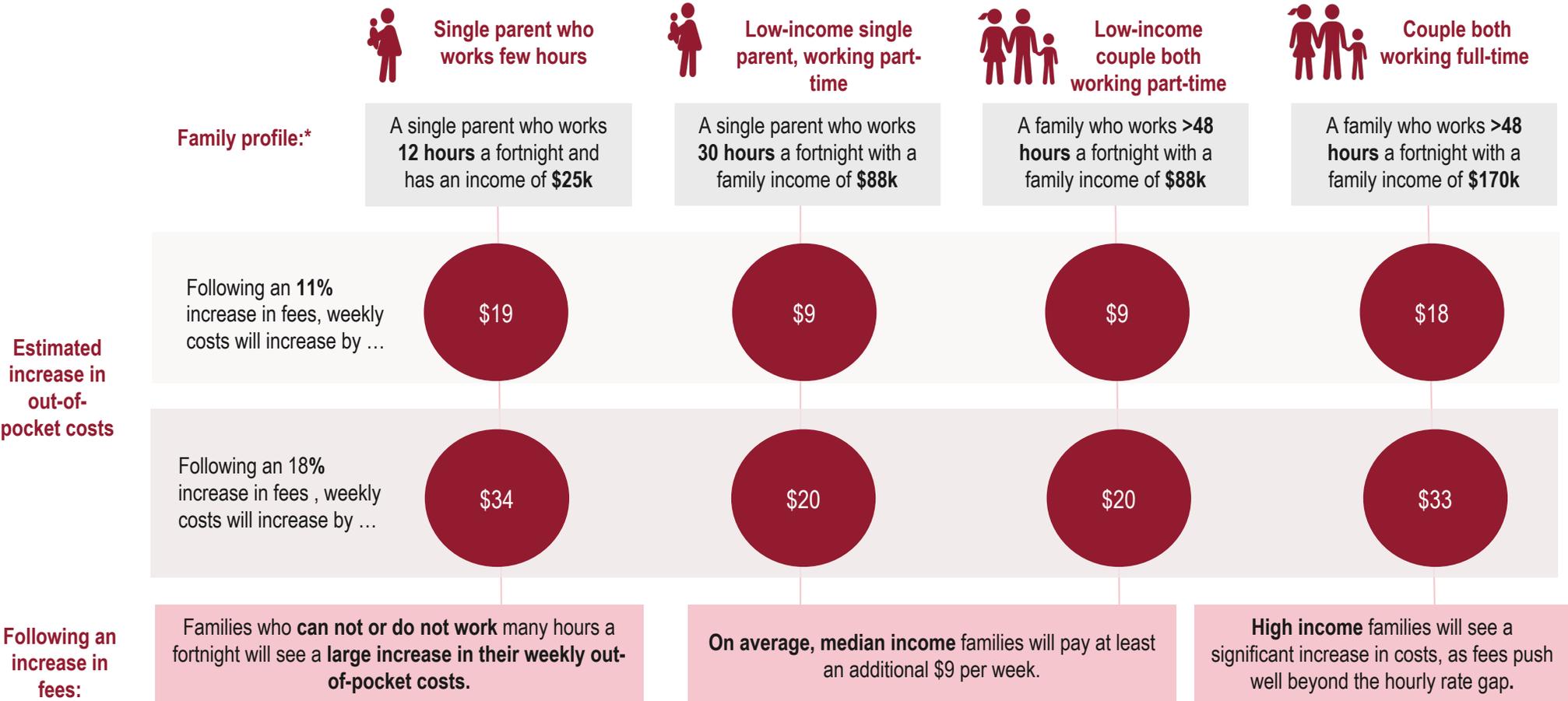
Families living in major cities will see the highest increase in fees.

The fee increase will be largest in higher socio-economic areas.

This analysis is based on an expected 11% increase in fees, following a 15% increase in wages (see slide 4 for reference). We estimate the impact on the average fee for each jurisdiction, ARIA classification and SEIFA quintile. Fee data is derived from Starting Blocks and Care for Kids.

# Impact on out-of-pocket costs

Fee increases will impact families in different ways, depending on their circumstances. Medium-income households are likely to see at least a \$60 increase in out-of-pocket costs



\* For each family, we assumed they have one child aged 3 years old, who attends a service for 3 days per week and 10 hours per day. The household income figures reflect the 10<sup>th</sup> percentile, median and 80<sup>th</sup> percentile – with \$25k reflecting the average Parenting Payment rate, \$88k the median household income, and \$170k a higher income household.

# Analysis of options to fund a wage increase

# Direct wage subsidy

A wage subsidy is a direct payment to services that covers the increase in their wages bill.

Wage subsidies are used across a range of sectors to supplement employee wages. We have reviewed key features of wage subsidy schemes in:

- Early childhood contexts (the Quality Fund, teacher supplement in Victoria, WAGE\$ in the US); and
- Other sectors (employment, social and community services, aged care).

## Case study: Aged Care Wage Increase

- The Fair Work Commission has ordered a 15% wage increase for aged care workers.
- Award rates will rise from June 2023 and the Commonwealth has agreed to fully fund the increase.
- The wage increase will be funded via a lift in the core funding to aged care services.
- There are currently concerns that the funding increase will not be passed on in full to employees.

## Case study: WAGE\$

- WAGE\$ is a United States wage subsidy provided direct to teachers and educators where their salary is below minimum thresholds.
- Subsidy levels are based on employee qualifications, and may consider geography, role, hours worked, age of children, type of program. Similar programs target ECEC programs operating in low SES communities.
- The total amount provided to teachers and educators is generally limited – only two states achieve pay parity with K-12 settings.
- Funding is provided to the employer retrospectively and in 6 month lump sums, and encourages a minimum 6-month commitment to the same employer.
- It's not built into ongoing funding, so is subject to budget and priority changes.

Wage subsidies differ in how they are organised and managed, but the design features appropriate for an Australian ECEC wage subsidy include:

- **Payments that cover the wage increase:** A payment to providers that is a percentage increase on their existing wages bill.
  - For example, if the annual total wages bill for a service is \$500,000 and the wage increase is 15%, the service would receive a \$75,000 subsidy.
- **Requirements to pass on the funding:** A wage subsidy is paid directly to the providers, with the requirement that it is passed on in full to educators and teachers. This means there is no administrative burden for educators and teachers.
- **Process and evidence requirements:** Wage subsidies can be paid monthly and retrospectively. Strong evidence requirements can mitigate the risk of fraud. For example:
  - Submitting annual audited financial statements confirming the total wages bill
  - Submitting payroll data confirming the wage increase has been passed on to educators and teachers
  - Periodic audits of a random sample of providers, and enhanced audit / evidence requirements for large providers

# Hourly rate cap increase

An HRC increase uses the existing CCS system to enable more revenue to flow through to services to meet the cost of a wage increase – with government and families sharing the cost of the increase.

Increasing the HRC is a way of enabling services to increase their fees without the full cost of the fee increase being passed on to families.

It means that the cost of any fee increase is shared between families and government – with the size of that share depending on the amount of subsidy a family is entitled to and what fees they are already paying.

## What is the hourly rate cap?

The HRC is a design feature of the CCS system. It sets an approximate benchmark for the hourly fee. Services can choose to charge more than the hourly rate cap, but families only receive subsidies up to the rate cap. For example:

- A family on the maximum subsidy level receives a subsidy of 85% of the hourly rate cap (currently \$12.74 per hour).
  - If fees were set at the HRC level, they would pay \$1.08 an hour, and government pays the remaining \$11.66.
  - If fees were \$15 per hour - \$2.26 above the HRC - they would pay \$3.34 an hour (\$1.08 + \$2.26) and government would continue to pay the remaining \$11.66.
  - If fees are below the HRC, they receive 85% of the actual fee.

A family's subsidy level depends on their household income and level of activity.

**Increasing the HRC means services can increase fees (gaining more revenue to fund wages) – but families don't pay the full cost.**

In this approach, the full cost of the wage increase can be shared between providers, families and government.

The HRC is built into the design of the CCS system. An HRC increase can be:

- Executed through the Ministers Rules rather than legislative change
- Changed in the CCS IT system without significant additional effort, as it is designed to change annually in line with inflation

However, it is important to note that this is a less direct funding mechanism than a wage subsidy.

This is because the CCS is a complex funding model, operating in a diverse and dynamic market, and because there is not a simple relationship between HRC levels and service revenue.

There are a range of factors that will determine the way that the increased cost is shared between providers, government and families. For example:

- **There is variability in whether / how much services can increase fees:** Up to 40% services already charge below the HRC<sup>1</sup> – most likely because their families cannot afford to pay more or because of significant competitive pressure. Increasing the HRC will not benefit these services.
- **Some services do not receive much revenue via the CCS:** Some services have a high proportion of families on low subsidy levels (because they are higher income earners) – in these circumstances, families would bear most of the additional cost.

These factors are outlined in more detail in the analysis on pages 19 - 24.

<sup>1</sup> AIFS Child care package evaluation: Final report February 2022 (Section 4.3)

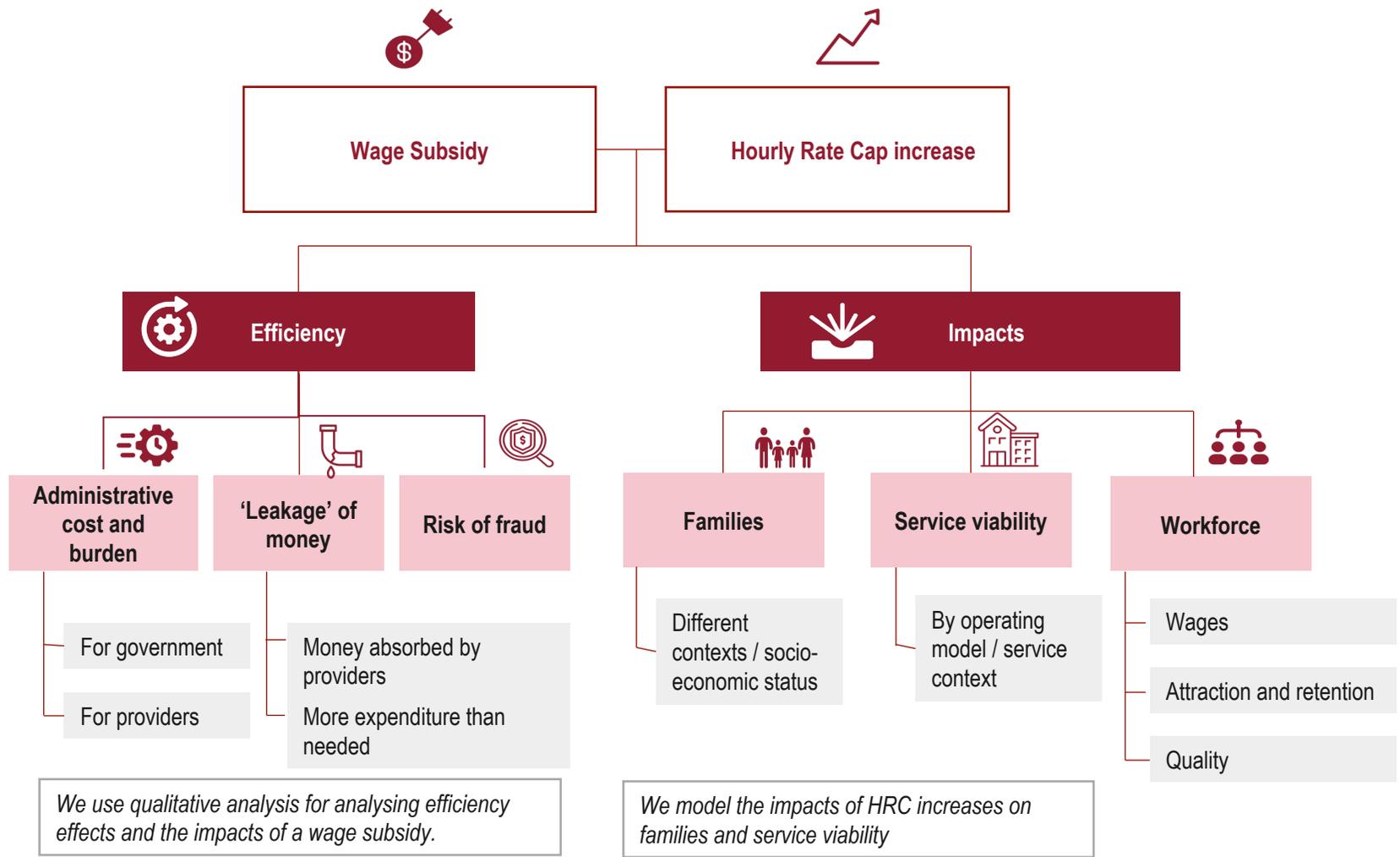
# Assessing the options

We assess each of the options, considering both the efficiency of the approach and the impact on families, service viability and the workforce.

We consider two options for funding a wage increase – and test the impact of an unfunded wage increase

We assess how efficient they are and what impact they're likely to have

To do this, we systematically consider a range of variables



*We use qualitative analysis for analysing efficiency effects and the impacts of a wage subsidy.*

*We model the impacts of HRC increases on families and service viability*

# Direct wage subsidy

A wage subsidy involves additional cost and administrative burden but is otherwise efficient to operate. Its results in no additional out-of-pocket costs to families, supports service viability and promotes attraction and retention of the workforce.

## Efficiency

 Administrative cost and burden **Moderate**

The administrative costs of a direct wage subsidy are considerably higher than an HRC change.

- **For government:** A wage subsidy requires the development and operation of a new system for processing payments to services. Using the cost of administering JobKeeper as a proxy, the administrative cost of a wage subsidy would be around \$7.5m annually.<sup>1</sup> This is less than 1% of the total cost of the CCS, but considerably more than an HRC increase.
- **For providers:** There is also administrative burden for providers, in managing and documenting the subsidy.

 'Leakage' of money through the system **Low**

'Leakage' refers to inefficient movement of money through the system – and in this context, captures the dual risks of providers using the increased revenue for something other than wages, and of government needing to spend more than is strictly needed.

Because a direct wage subsidy can be designed with high requirements for evidence and audit, there are strong mechanisms for ensuring:

- Any investment in wages is passed directly to employees
- No excessive / unnecessary funding is provided.

 Risk of fraud **Low**

A wage subsidy can be designed with strong accountability mechanisms, including evidence requirements and routine auditing. This means the risk of fraud is low.

## Impact

 Families **Positive**

There is no risk of increased out-of-pocket costs for families, as the increased cost of delivery is met through the wage subsidy.

There are potential positive impacts for families, if services are no longer closing rooms and restricting numbers. Continuity of teacher/educator relationships is also important for children's wellbeing and learning.

 Service viability **Positive**

Risks to service viability are significantly mitigated. There are unlikely to be differential effects on providers with different operating models. For example, services that have comparatively high wages bills because they staff over-ratio, already pay above-Award or hire more qualified teachers and educators would not be penalised.

 Workforce **Positive**

A wage subsidy is more likely to guarantee all teachers and educators benefit from a wage increase.

Wages are important for workforce wellbeing and recognition, and will contribute to attraction and retention in the workforce. Higher wages will contribute to a more professional and high-quality workforce.

<sup>1</sup> The ANAO reports that the total cost of administering JobKeeper was \$286m. This is the equivalent of \$63 per worker per year, applied to the nearly 120,000 CBDC workers with an ECEC qualification.

# Increasing the HRC

Increasing HRCs is comparatively easy to implement, but its effects are highly variable, inequitable and inefficient.

## Efficiency

### Administrative cost and burden Low

The administrative cost of an HRC increase is relatively low, because it leverages existing features of the CCS system.

- **For government:** There are establishment costs for government in processing a change to the Minister's Rules and changing CCS ITS settings, but these are likely to be able to be absorbed within existing resourcing. The largest cost is likely to be in communicating the change to families. There are no ongoing administrative costs.
- **For providers:** There are no establishment or ongoing costs for providers, beyond supporting communication of the change to families.

### 'Leakage' of money through the system High

'Leakage' refers to inefficient movement of money through the system – and in this context, captures the dual risks of providers using the increased revenue for something other than wages, and of government needing to spend more than is strictly needed.

The risk of leakage is high because:

- There are no mechanisms to ensure increased revenue is directed to wages – there is scope for providers to channel the additional revenue into profit or to cover other costs. This risk would be mitigated if Award rates compelled high wages.
- It is likely that government expenditure will be more than is required to meet the wage increase. As the analysis on Page 21 highlights, a 15% wage increase could require a 25% increase in HRCs to ensure services in all circumstances were able to increase revenue sufficiently.

### Risk of fraud Low

The risk of deliberate fraud is not high. However, as noted previously, is mechanism does not ensure that wage increases are passed on to the workforce.

## Impact

### Families Negative

The only way in which an HRC increase leads to increased revenue for services is via a fee increase. Although families will not bear the full cost of the increase, this mechanism does result in higher out-of-pocket costs.

The magnitude of the increase depends on:

- How much subsidy a family is eligible for – but families on lower subsidy rates are most exposed (i.e. those who receive less than 50% subsidy)
- How much fees increase by and how close their current fees are to the HRC

*See page 13 for full analysis*

### Service viability Variable

There is significant variability in operating models in the ECEC sector and an HRC increase will not have a consistent effect across the whole sector as a result. Our analysis shows that:

- Services unable to increase fees do not benefit at all from an HRC increase
- Services with high employment costs (as a proportion of total costs) are the most exposed
- Services with low employment costs (as a proportion of total costs) and the ability to increase fees are likely to experience substantial windfall gains.

*See pages 19-21 for full analysis*

### Workforce Variable

An HRC increase does not ensure or enable all services to increase wages. Some employees will benefit, but services that are already investing significantly in their workforce are the most disadvantaged by an HRC increase.

# Impact of an HRC increase on out-of-pocket costs

Increasing the HRC can enable some services to increase fees paid by families. Family out-of-pocket costs depend on whether a service is able to increase their fees, how current fees compare with the HRC, and the amount of CCS a family receives.

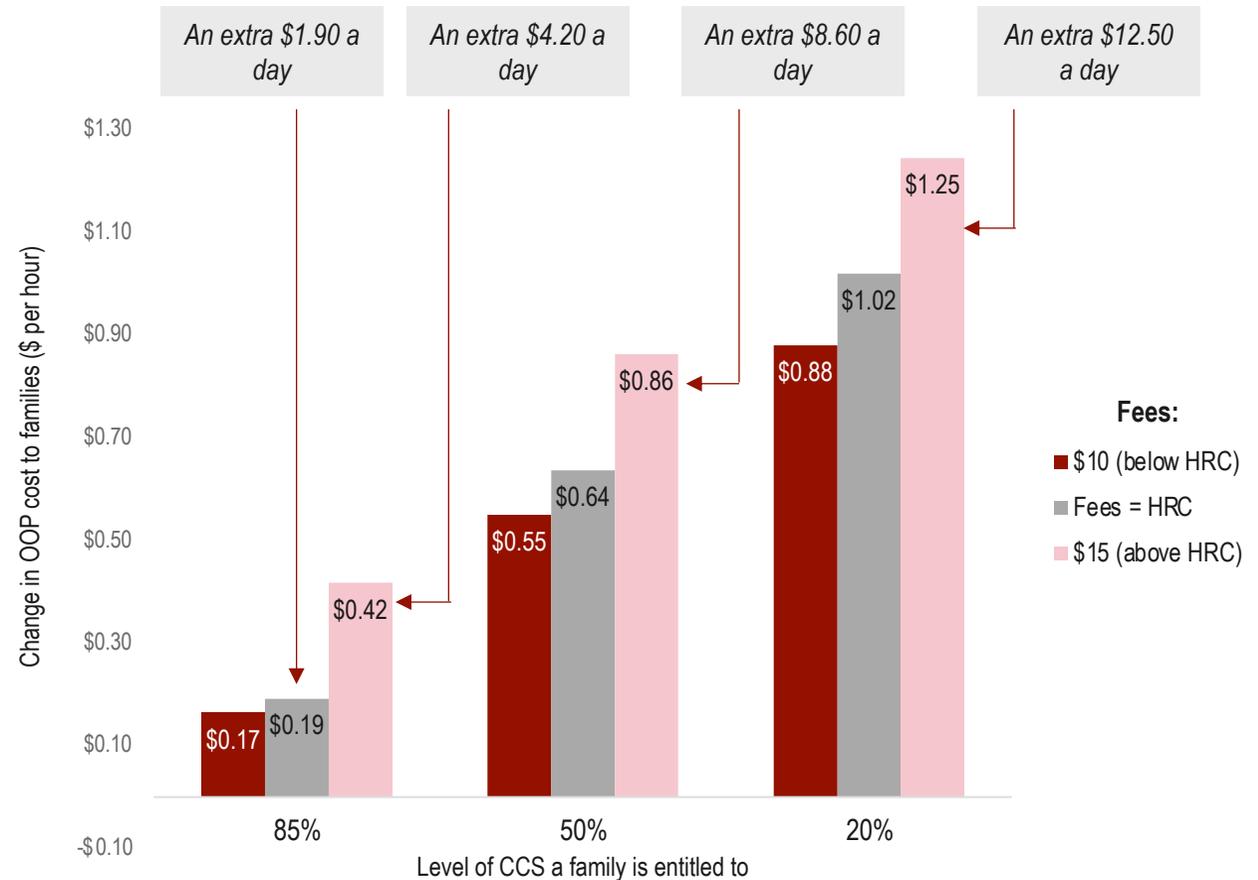
Increasing the HRC is intended to enable services to increase fees (and therefore revenue) without the full cost of that increase being borne by families.

However, the amount families will pay depends on their circumstances.

Our analysis shows that, even with HRC increases:

- **Out-of-pocket costs will increase for all families**
- **The increase is smallest for low-income families paying fees at or below the current HRC**
  - Families on 85% subsidy paying low-to-medium fees would need to pay up to an extra \$1.90 a day
- **The increase is largest for families paying fees above the HRC**
  - A low-income family in a high-fee service could need to pay an extra \$4.20 a day, and high-income families could pay more than \$12 a day
  - The sharp increase for families in high-fee services is because they are already above the HRC – so all the additional cost is borne by the family.

**The impact on out-of-pocket costs depends on the amount each family currently receives in CCS and whether current fees are below, at or above HRC\***



\* This analysis assumes a 15% fee increase and 10 hour daily sessions

# HRC increase and service ability to increase fees

There are a range of factors that shape whether, and to what extent, services increase fees.

Following an increase in the HRC, not all services will be able to fully increase fees and revenue. We model three scenarios:

## Service does not increase fees

This is more likely for services with highly price-sensitive families, for example:

- Services in low SES areas with families who have no capacity to pay additional fees
- Services operating in highly competitive markets where there's a risk that fee increases will prompt families to move services – therefore resulting in no net revenue

## Service partially increases fees

This is more likely for services:

- In communities where families are sensitive to price increases
- With a large proportion of families on higher incomes who only receive a small proportion of subsidy and therefore bear more of the increased costs
- Operating in moderately competitive local markets where there is some risk of losing families

## Services passes on the full increase

This is more likely for services:

- With higher income families who have the capacity to pay additional fees
- Operating in markets with low levels of competition on price, or where all local services are likely to increase fees to the same extent.

*\* We do not have any data on the proportion of services who fit each of these categories (wage costs and capacity to meet fees). For the purpose of modelling the effects of these different scenarios, we assume an equal distribution of all services into these categories.*

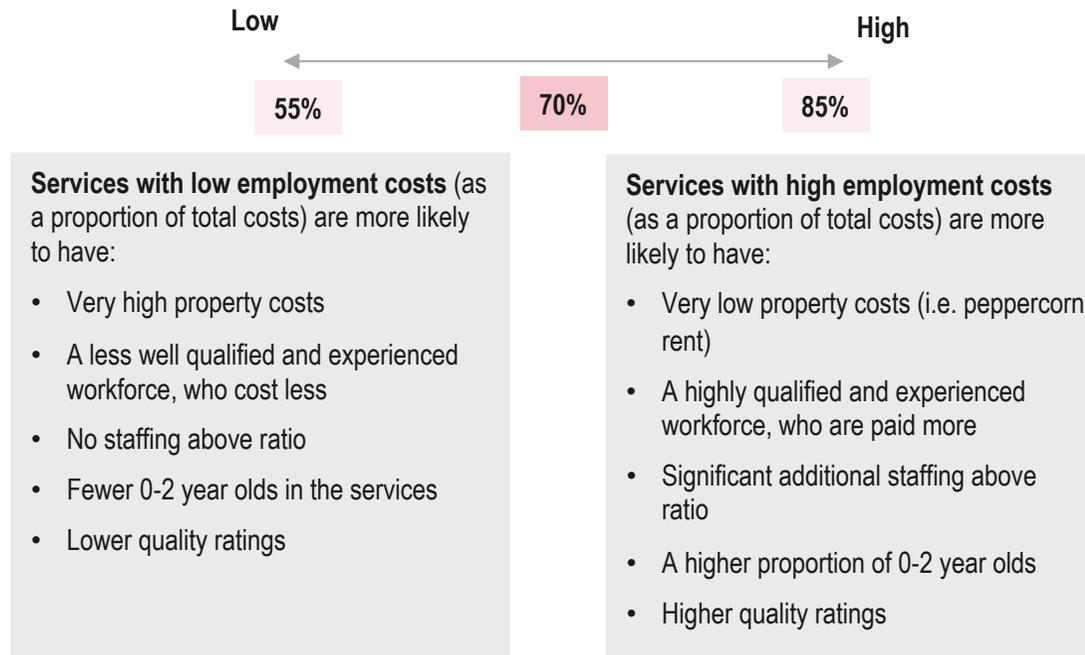
# HRC increase and service wage costs

Services with high employment costs (as a proportion of their total costs) will need more revenue to cover a wage increase.

There is significant variability in wage bills across the sector. As a proportion of total costs, wages vary between 55% and 85% with a median of 70%.\*

The differences in employment costs reflect differences in operating context:

## Wages as a proportion of total cost:



A wage increase will cost more for services with high employment costs – and they will need to increase their revenue by more.

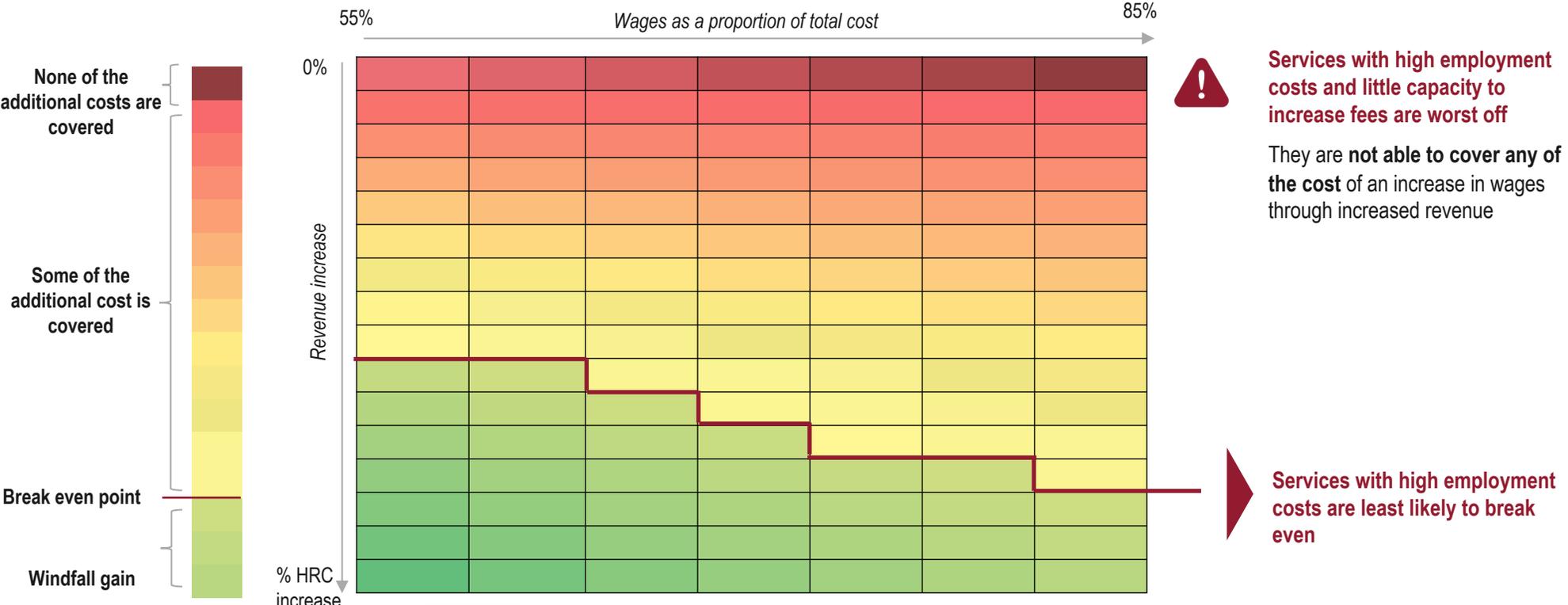
\* We do not have any data on the proportion of services who fit each of these categories (wage costs and capacity to meet fees). For the purpose of modelling the effects of these different scenarios, we assume an equal distribution of all services into these categories.

# Adequacy of an HRC increase

An HRC increase has highly variable and inequitable effects. Services with higher employment costs and limited ability to increase fees are significantly exposed, while others are likely to benefit from windfall gains.

We modelled the circumstances in which an HRC increase will allow services to increase their revenue enough to meet the cost of a wage increase. The model assumes the HRC increase matches the wage increase and takes into account the two key variables that influence whether or not services will break even – their ability to increase fees and whether they have high or low employment cost.

This heat map shows how much of the total cost of a wage increase is covered by an equivalent increase in the Hourly Rate Cap



Services with high employment costs and little capacity to increase fees are worst off. They are not able to cover any of the cost of an increase in wages through increased revenue.



Services with high employment costs are least likely to break even.



Services with low employment costs and the ability to increase fees are likely to receive windfall gains. They will receive more than enough revenue to cover the increased costs.

Note: We do not have data on the number of services in each of these scenarios and therefore cannot estimate the proportion of services likely to be out of pocket. For the purpose of this model, we have assumed an equal distribution of services into each category.

# Size of the HRC increase needed

It is difficult to set an HRC that is adequate for all services. If wages increase by 15%, you need to increase HRCs by 25% to ensure all services who can *partially* or *fully* increase fees can break even – and at this point, some services would be receiving a significant windfall gain. Services who cannot increase fees do not benefit from an HRC increase in any scenario.

We modelled the circumstances in which an HRC increase would enable services to generate enough revenue to meet the cost of a 15% wage increase.

To cover the cost of a 15% wage increase ....

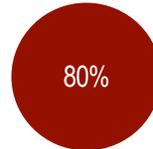
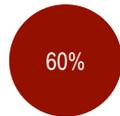
The HRC is increased by the same amount as the wage increase (15%)

The HRC is increased by a bit more than the wage increase (20%)

The HRC is increased by a lot more than the wage increase (25%)

## Service A: High employment costs and can partially increase fees

*This service staffs over-ratio, is already paying staff above-award rates and is on peppercorn rent*



HRC needs to increase by at least 25% for this service to break even

## Service B: Low employment costs and can fully increase fees

*This service is paying at award rates, has a high reliance on casual staff, and tends to employ less experienced teachers and educators*



But at a 25% HRC increase, this service gets a windfall gain of 3x the *additional* revenue they need

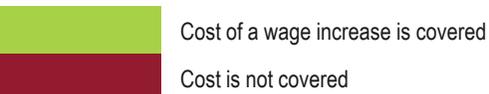
## Service C: Cannot increase fees

*This service could have high or low employment costs, but its families are extremely price sensitive and it cannot increase fees*



A service that cannot increase fees does not benefit from an HRC increase in any scenario

Proportion of the wage increase that is covered by the HRC increase

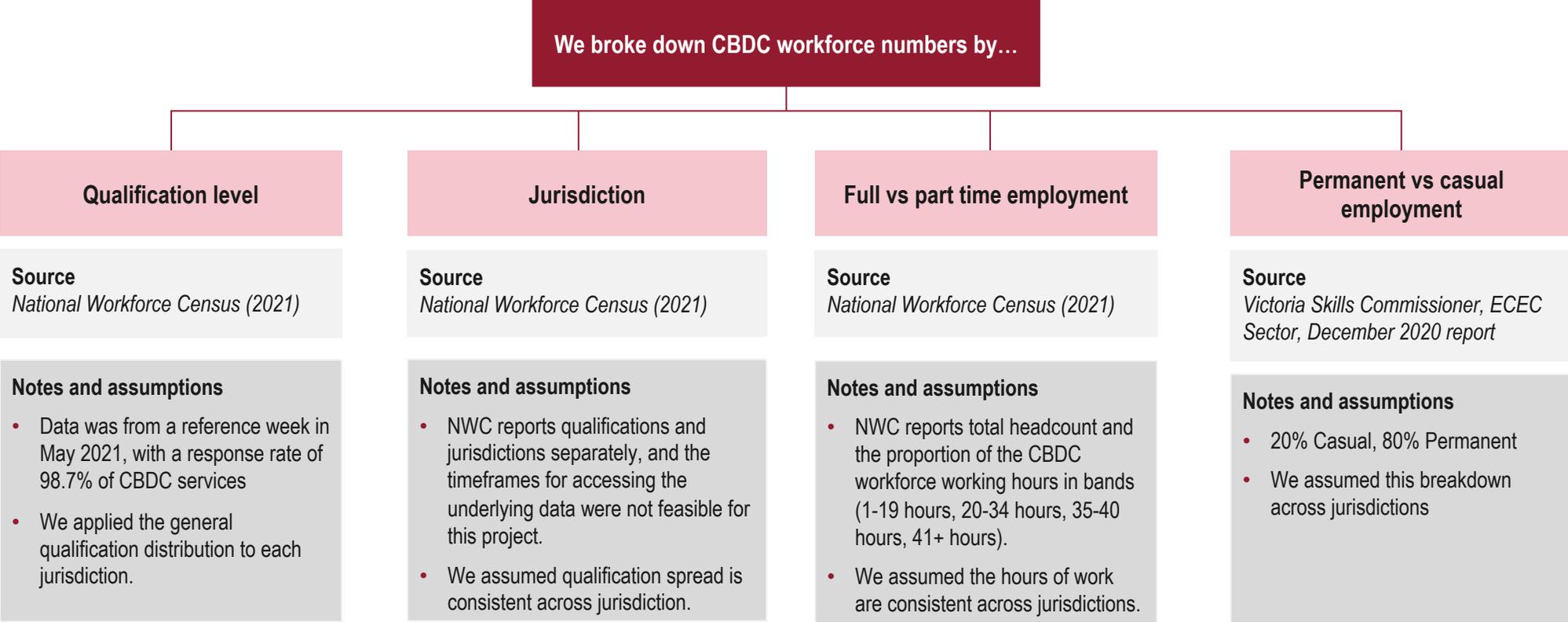


# Appendices

## Appendix 1 – Modelling the cost of a wage increase

# 1. Built a profile of the CBDC workforce

By getting a deeper understanding of the CBDC workforce profile we were able to more accurately measure the impact of wage increases.



## 2. Matched workforce profile with average wage rates and costs

Using our profile of the CBDC workforce, we matched the workforce according to award rate, considering qualification, experience and employment type.

**We determined current average wage rates**

### Average award wage by qualification level / level of experience

#### Source

*Propose: Children's Services Award (Educators), Educational Services Award (Teachers)*

#### Notes and assumptions

Breakdown of wages by level → Mapping levels to qualifications → Using NWC years of experience data to apportion workers to sub-levels.

Levels don't map precisely to qualifications.

We assumed the same proportion of the workforce in each sub-level across jurisdiction.

We assumed 75% of Centre Directors are under the Children's Services Award – and estimated one director and assistant director per CBDC service.

### Percentage at or above award

#### Source

*National Workforce Census (2021)*

#### Notes and assumptions

NWC data on the proportion of the workforce with wages above the award is not broken down by qualification or experience (although it does account for setting).

We applied the proportion above award rates equally across all qualifications.

### Permanent vs casual employment

#### Source

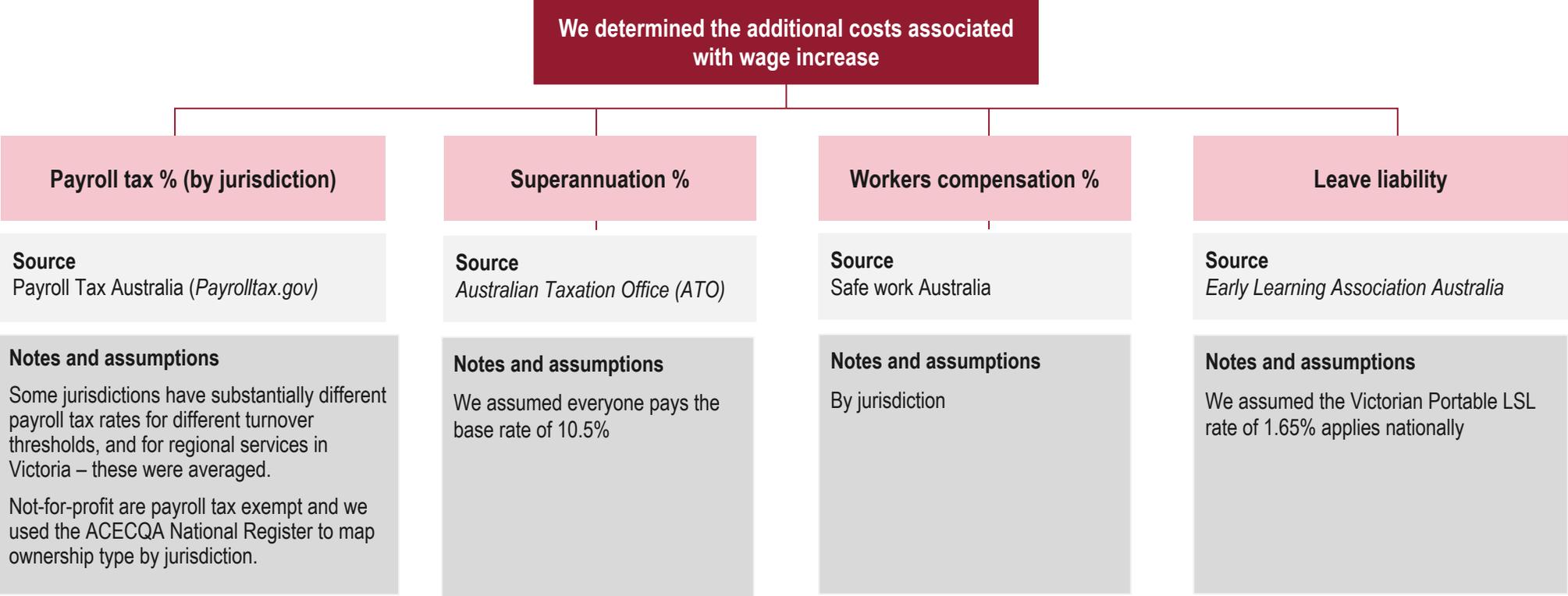
*Children's Services Award  
Educational Services (Teachers) Award*

#### Notes and assumptions

A casual employee must be paid the hourly rate payable for a full-time employee plus a casual loading of 25% for each ordinary hour worked.

## 2. Matched workforce profile with average wage rates and costs

We also considered the cost to the employer of increasing employee wages.



### 3. Applied a proportionate wage increase

There are a two different ways to apply a wage increase – a percentage increase on the total wages bill or lifting base rates in the Award.

**We then calculated the total cost of a wage increase. Depending on the policy objective, we calculated both:**

1

#### **A percentage increase across the board**

We applied a percentage increase to the total wages bill in the sector. This assumed **all** employees receive a percentage increase in their wage.

2

#### **Lifting wages to a minimum threshold**

This approach lifted the base rates across the board so that no employee would earn less than a certain amount. There's no guarantee that this would be passed onto any employee earning over the Award, however.



## Appendix 2 – Wage subsidy design

# Wage subsidies in other industries

Model	Sector	Key details
<p><b>Workforce Australia Wage Subsidy</b></p> <p><a href="https://www.workforceaustralia.gov.au/businesses/about/how-to/user-guides/wage-subsidy">https://www.workforceaustralia.gov.au/businesses/about/how-to/user-guides/wage-subsidy</a></p>	Employment for target cohorts	<ul style="list-style-type: none"> <li>• \$10k per worker that meets the criteria</li> <li>• Duration depends on how long the employee has been unemployed</li> <li>• Requires employee and employer to enter into a wage subsidy agreement</li> <li>• Both employer and employee validate the employment relationship and accuracy of payment details</li> <li>• Managed through a Workforce Australia portal, with employers signing up for an employer profile</li> </ul>
<p><b>Jobs Victoria wage subsidy</b></p> <p><a href="https://business.vic.gov.au/__data/assets/pdf_file/0008/2039345/Jobs-Victoria-Fund-Guidelines-updated.pdf">https://business.vic.gov.au/__data/assets/pdf_file/0008/2039345/Jobs-Victoria-Fund-Guidelines-updated.pdf</a></p>	Employment for target cohorts	<ul style="list-style-type: none"> <li>• Varying amounts, depending on context</li> <li>• Provided for up to 12 months</li> <li>• Managed via a grant agreement between the employer and the relevant department, requiring consent from the employee, and a statutory declaration that conditions are met</li> <li>• Employers must provide ongoing evidence that the employee is still employed on the terms stipulated in the agreement, and employers receiving more than \$200k have an additional level of financial scrutiny</li> <li>• Independent audits are conducted to ensure compliance / reduce fraud</li> </ul>
<p><b>Disability Employment Services (DES) Wage Subsidy Scheme</b></p>	Employment for people with disability	<ul style="list-style-type: none"> <li>• Rate is negotiated between the employer and the disability employment service provider</li> <li>• Time limited – provided for the first 13 weeks</li> <li>• Disability employment providers act as brokers between the employee and employer</li> <li>• Requires an agreement between employer and employee, and the disability employment service</li> </ul>
<p><b>Social and Community Services (SaCS) Award – supplementary funding</b></p> <p><a href="https://www.dss.gov.au/our-responsibilities/communities-and-vulnerable-people/grants-funding/fair-pay-for-social-and-community-services-workers/sacs-funding-supplementation-frequently-asked-questions">https://www.dss.gov.au/our-responsibilities/communities-and-vulnerable-people/grants-funding/fair-pay-for-social-and-community-services-workers/sacs-funding-supplementation-frequently-asked-questions</a></p>	Social and community services	<ul style="list-style-type: none"> <li>• Funding calculated using a formula - program funding amount x % SACS wage component x SACS ERO increase^ (i.e. not per employee)</li> <li>• Organisations can only use supplementation funding to cover costs arising from the Equal Remuneration Order (ERO) – including staff wages directly affected by the ERO and on-costs (i.e. superannuation and leave entitlements) that have increased because of the ERO</li> <li>• Employers who already pay above award are not required to increase wages proportionately, but may choose to do so (or may choose to use that money in any other way they choose, consistent with their grant requirements)</li> <li>• Acquitted via existing agreement accountability processes, although organisations need to complete a financial declaration and provide a financial acquittal to confirm the funding was used to meet wage costs</li> <li>• Only provided for established programs, not new programs (as this will be factored in, going forward)</li> </ul>
<p><b>Aged care wage increase</b></p> <p><a href="https://www.fwc.gov.au/hearings-decisions/major-cases/work-value-case-aged-care-industry">https://www.fwc.gov.au/hearings-decisions/major-cases/work-value-case-aged-care-industry</a></p>	Aged Care	<ul style="list-style-type: none"> <li>• The Fair Work Commission has ordered a 15% wage increase for aged care workers. The Commonwealth has agreed to fully fund the increase.</li> <li>• The Commonwealth will increase core funding to aged care services, but there are currently concerns that employers will not pass the full increase on to employees.</li> </ul>

# Wage subsidies in ECEC contexts

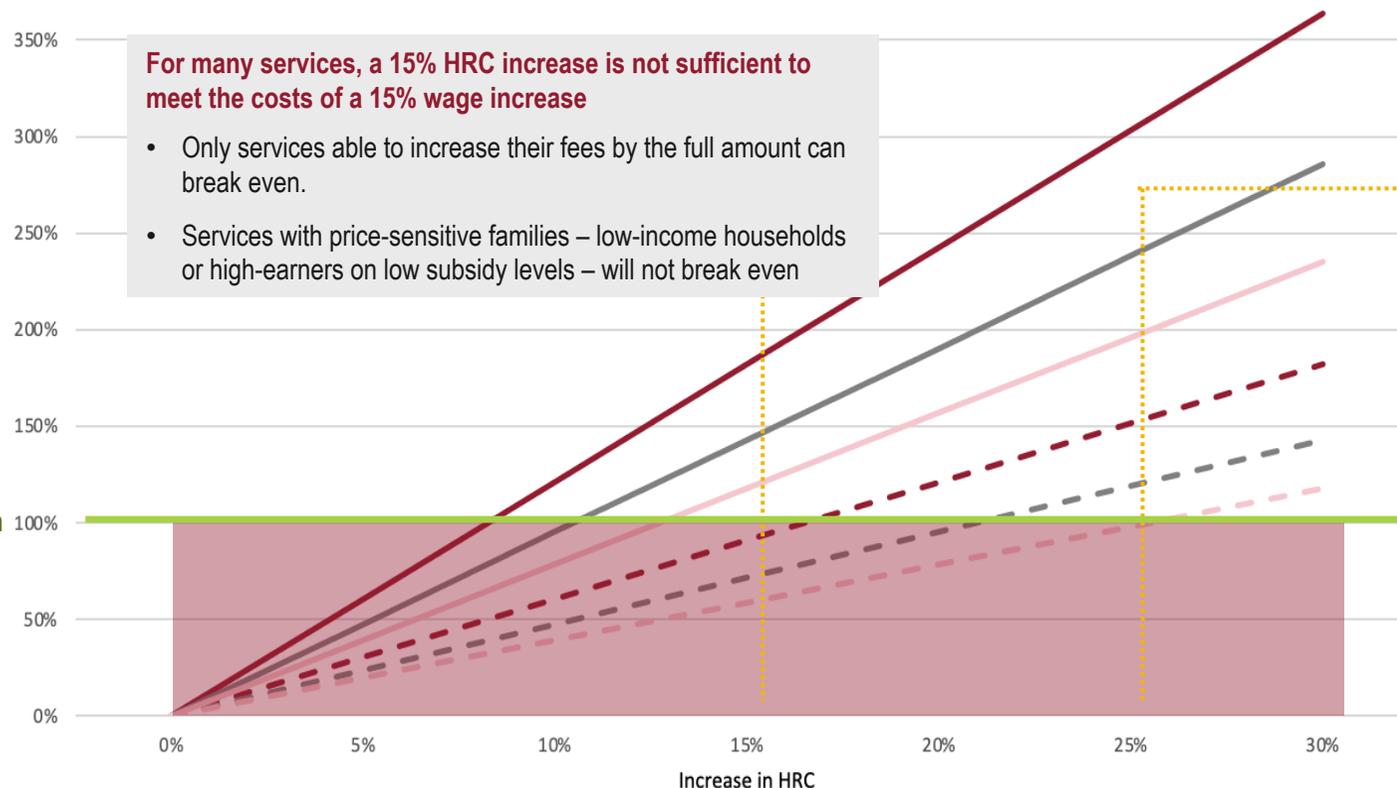
Model	Sector	Key details
<p><b>US Early Childhood Wage Subsidy (i.e. North Carolina, Florida, New Mexico, Nebraska, Tennessee)</b></p> <p><a href="https://www.childcareservices.org/programs/wage-s/">https://www.childcareservices.org/programs/wage-s/</a></p> <p><a href="https://cscce.berkeley.edu/wp-content/uploads/2022/04/6-Compensation-Strategies.pdf">https://cscce.berkeley.edu/wp-content/uploads/2022/04/6-Compensation-Strategies.pdf</a></p>	ECEC	<ul style="list-style-type: none"> <li>• Provided direct to teachers and educators where their salary is below minimum thresholds</li> <li>• Employees submit an application form and provide evidence in the form of a payslip, proof of qualification level and financial statements from employers</li> <li>• Subsidy levels are based on employee qualifications, on a sliding scale from vocational qualifications to postgraduate degrees, and may take into account geography, role, hours worked, age of children, type of program. Similar programs target ECEC programs operating in low SES communities.</li> <li>• The total amount provided to teachers and educators is generally relatively limited (estimated at \$100-\$6,500pa) – only two states achieve pay parity with K-12 settings.</li> <li>• Funding is provided to the employer retrospectively and in 6 months lump sums, and encourages minimum of 6 month commitment to the same employer</li> <li>• Employers are not allowed to use the funding in lieu of normal wage increases.</li> <li>• Not built into ongoing funding, so subject to budget and priority changes</li> </ul>
<p><b>Early Years Quality Fund Special Account</b></p> <p><a href="https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/bd/bd1213a/13bd133">https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/bd/bd1213a/13bd133</a></p> <p><a href="https://www.anao.gov.au/work/performance-audit/administration-early-years-quality-fund">https://www.anao.gov.au/work/performance-audit/administration-early-years-quality-fund</a></p>	ECEC	<ul style="list-style-type: none"> <li>• Established to support the introduction of new teacher requirements under the NQS, and provided a dedicated financial commitment (i.e. not out of Consolidated Revenue)</li> <li>• Supported wage increases of ~\$3-6/hr up to a cap of \$300m (under a demand-driven, first-in-first-served basis – although with half hypothecated for small providers and half for large providers)</li> <li>• Eligibility was limited to LDCs and providers were required to demonstrate they were limiting fee increases to 'actual' operating cost increases and instituting enterprise bargaining agreements.</li> <li>• Limited to a two-year period without ongoing funding.</li> <li>• Applications submitted on a provider basis, but each service assessed separately</li> <li>• Employers required to demonstrate they had an EBA that matched the required pay conditions</li> <li>• ANAO report pointed to significant deficiencies in the efficiency, equity and appropriateness of the design of the subsidy</li> </ul>
<p><b>Early Childhood Teacher Supplement (Victoria)</b></p>	ECEC	<ul style="list-style-type: none"> <li>• Loading paid to cover the cost of employing a teacher, paid as a single annual grant in addition to core / recurrent funding</li> <li>• Applied for annually on the basis of employment relations at the time</li> <li>• Calculated per enrolment and by the experience level of the teacher</li> <li>• Providers reported that administrative requirements were onerous (annual cycle of applications and did not fully cover the employment costs)</li> </ul>

## Appendix 3 – HRC increase

# Increasing the HRC - Covering wage costs across services

If wages increase by 15%, the HRC would need to increase by 25% to ensure services who could partially or full increase fees are able to break even – and at this point, some services would be receiving a significant windfall gain.

**This graph shows how much of the cost of a 15% wage increase is covered by an HRC increase**



**For many services, a 15% HRC increase is not sufficient to meet the costs of a 15% wage increase**

- Only services able to increase their fees by the full amount can break even.
- Services with price-sensitive families – low-income households or high-earners on low subsidy levels – will not break even

**To ensure services in most scenarios would have sufficient revenue to cover a 15% wage increase using the HRC, the HRC would need to increase by 25%**

- At this point, some services would be getting a windfall gain - 3x the amount of revenue they needed to cover the cost of the wage increase
- These are more likely to be services under-investing in their workforce

**Service scenarios**

- Wages are 55% of total cost  
Service can partially increase revenue
- Wages are 55% of total cost  
Service can increase revenue fully
- Wages are 70% of total cost  
Service can partially increase revenue
- Wages are 70% of total cost  
Service can increase revenue fully
- Wages are 85% of total cost  
Service can partially increase revenue
- Wages are 85% of total cost  
Service can increase revenue fully

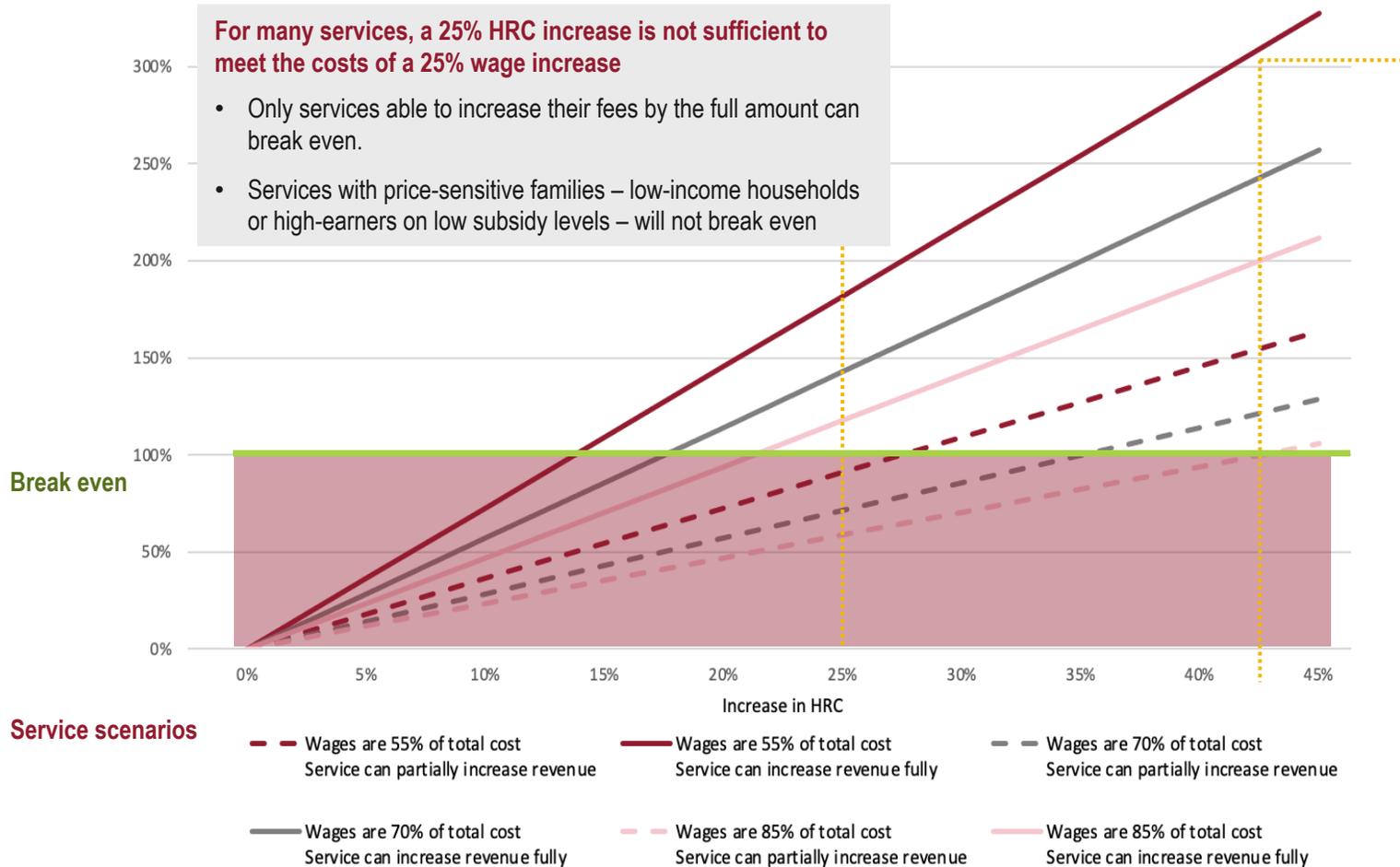
**There are some services who can't increase their fees and therefore don't receive increased revenue from an increase in the HRC**

Note: We did not have data on the number of services in each of these scenarios and therefore did not estimate the proportion of services likely to be out of pocket. For the purpose of this model, assumed an equal distribution of services into each category.

# Increasing the HRC - Covering wage costs across services

If wages increase by 25%, the HRC would need to increase by approx. 42% to ensure services who could partially or full increase fees are able to break even – and at this point, some services would be receiving a significant windfall gain.

This graph shows how much of the cost of a 25% wage increase is covered by an HRC increase



To ensure services in most scenarios would have sufficient revenue to cover a 25% wage increase using the HRC, the HRC would need to increase by approx. 42%

- At this point, some services would be getting a windfall gain - 3x the amount of revenue they needed to cover the cost of the wage increase
- These are more likely to be services under-investing in their workforce

There are some services who can't increase their fees and therefore don't receive increased revenue from an increase in the HRC

Note: We did not have data on the number of services in each of these scenarios and therefore did not estimate the proportion of services likely to be out of pocket. For the purpose of this model, assumed an equal distribution of services into each category.