

To: Directors of Children's Services of
local authorities in England

16 August 2007

**EARLY YEARS FUNDING REFORMS:
Guidance on cost analysis and funding survey results**

Dear colleague.

Following the announcements made in June by Jim Knight, Minister for Schools and Learners on changes to the school, early years and 14-16 funding arrangements for 2008-11, this letter alerts local authorities to the publication of **guidance on the first stage of the reform of the early years element of the Dedicated Schools Grant - the need for local authorities to undertake an analysis of the cost of delivering the free entitlement in private voluntary and independent settings.**

The cost analysis is the first stage of a three part process of reform between now and 2011:

- Having carried out an analysis of PVI costs in their area, local authorities will need to and present it to their Schools Forum and relevant sub-group before setting budgets for 2008-11.
- From 2009-10 all local authorities will be required to introduce consistent pupil counting between the maintained and PVI sectors.
- By 2010-11 at the latest, local authorities will be required to develop and introduce a single local formula for funding early years provision in the maintained and PVI sectors
- Schools Forum membership will be broadened so that representatives of the early years PVI sector can be included

Full details of the announcements can be found at <http://www.teachernet.gov.uk/management/schoolfunding/schoolfunding2008to11/> the Department will also be publishing a more detailed explanatory note on all the decisions this autumn.

The guidance we are publishing today has been developed in partnership with the National Day Nursery Association and the Pre-School Learning Alliance. It contains practice examples from local authorities who have gone some way to completing a similar analysis. A copy of the guidance can be downloaded from the Every Child Matters website at www.everychildmatters.gov.uk/earlyyears

In addition, we are also publishing today the findings of our survey of local funding arrangements and schools forums membership. This survey was carried out between March – July 2007 when we asked all local authorities to complete a questionnaire detailing how they go about allocating and distributing free entitlement funding to maintained schools and PVI providers and about the membership of their Schools Forums. We have now published all questionnaires received online alongside a summary of the key findings.

We also intend to publish in the Education Benchmarking tables estimates of the level of funding local authorities allocated in 2006-07 to the free entitlement in private, voluntary and independent and maintained sector providers. These estimates will be available online in late August.

We hope these documents will, together, provide a resource for local authorities to share best practice, to 'benchmark' themselves and to use in reviews of their under 5s funding arrangements. I am sure you will want to discuss them at your Schools Forum and with your Schools Finance and Early Years teams.

Enquires about this letter, the questionnaire or the cost analysis guidance should be address to Claudine Menashe-Jones at claudine-menashe-jones@dcsf.gsi.gov.uk.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Graham Archer', is written above a horizontal line. A vertical line is positioned to the right of the signature.

Graham Archer
Deputy Director
Early Years, Extended Schools and Special Needs Group

Early Years Funding Reform: Analysing the costs of delivering the free entitlement to nursery education in the PVI Sector

department for
children, schools and families



Reforming the funding for the Free Entitlement to Early Education – guidance on analysing costs

The Department for Children, Schools and Families has announced the following changes to how the free entitlement to early learning and care for three and four year olds will be funded through local authorities (LAs).

- To support the extension to 15 hours and increasing flexibility of the free entitlement to high quality early years education and care, local authorities will be required to develop and introduce a **single local formula** for funding early years provision in the maintained and private, voluntary and independent (PVI) sectors¹ over the next two years and by 2010-11 at the latest.
- From 2009-10 all local authorities will be required to introduce **consistent pupil counting between the maintained and PVI sectors**. Changing the count from place-led to mainly participation-led funding in both sectors will need to be carefully managed, subject to an impact assessment and appropriate transition and protection mechanisms.
- In the short term local authorities will need to carry out **an analysis of PVI costs** in their area, and present this to their schools forum and relevant sub-group before setting budgets for 2008-11.

There are also a number of changes aimed at improving the representation of PVI providers on Schools Forums so that the views of all sectors are taken into account.

- Schools Forums' membership will be broadened to include non- school members from the early years sector so that they can play a full part in discussions on the development of the funding arrangements.
- Local authorities are also expected to establish a early years provider reference group, which will act as a sub-group to the Schools Forum feeding in views on the implementation of the new early years funding arrangements.
- The limit on non-school members will be raised from one fifth to one third to accommodate the broader membership.

Further details of the Schools, Early Years and 14-16 Funding announcements can be found at www.teachernet.gov.uk/management/schoolfunding

To support the delivery of the analysis of PVI costs described above, the DCSF has produced this guidance document with input from National Day Nurseries Association (NDNA) and The Pre-school Learning Alliance. It outlines a suggested process to follow when analysing the costs of delivering the free entitlement and gives some examples of local authorities that have already started this work. **It does not cover how local authorities should fund the free entitlement.** Although the cost of delivery will be a key consideration in local funding decisions, it is unlikely to be the only factor that local authorities take into account when setting local budgets and funding systems.

¹ Private, voluntary and independent providers include, for example, privately owned day nurseries, sessional playgroups run by voluntary sector organisations and nursery classes in Independent Schools.

Analysing the Costs of Delivering the Free entitlement in the PVI Sector

Objectives

Undertaking an analysis of the cost of delivering the free entitlement to nursery education for 3 and 4 year-olds in private voluntary and independent sector settings is a key staging post in the process of arriving at a single local formula for free entitlement funding by 2010, which will include the maintained sector. To complete the cost analysis process local authorities will be expected to produce a published document which has been presented to and discussed at your Schools Forums before budgets for 2008-11 have been set. The document should include:

- the key cost drivers taken into account for the analysis
- a description of the local PVI market of providers, highlighting the impact of different operating models on the cost of delivery
- an outline of the process and analysis undertaken by the authority, and,
- conclusions in the context of previous and planned spending on the free entitlement, child outcome measures, sufficiency and sustainability.

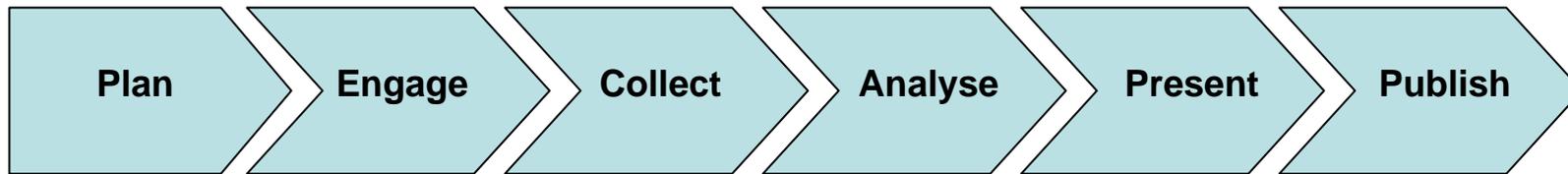
A collaborative approach with providers will be key to success. Carrying out this analysis will enable you to work with providers to get a better understanding of how the free entitlement is delivered in the PVI sector in your authority to support better facilitation of the childcare market. Authorities should also consider how this cost analysis will feed into the development of a single formula for the free entitlement by 2010. The analysis will also provide a firmer basis for discussions in Schools Forums on the allocation of resources to the free entitlement and PVI settings in particular – although it only covers the cost of delivery and not other factors in funding decisions that LAs will want to consider, such as the need to secure sufficient and diverse provision.

The DCSF will also be publishing a full implementation guide on the Schools, Early Years and 14-16 funding arrangements for 2008-11 in early September 2007. Authorities may also want to refer to the summary of current approaches to funding set out in this summary (www.everychildmatters.gov.uk/earlyyears)

Summary

This guidance sets out six key stages in the cost analysis process which we have drawn together in the light of feedback from local authorities who have already conducted the analysis. Case studies are also included here. The suggested process is designed to provide support and suggestions based on what other authorities have learnt.

The six key stages to the cost analysis process:



Key points to consider at each stage in the process are set out in the following sections.

1. Plan the activity in consultation with provider groups
2. Engage with a wider provider audience
3. Collect the data
4. Analyse the data
5. Present the analysis
6. Publish the conclusion



1. Plan the activity – working in partnership to establish your strategy

Early buy-in to the analysis from key stakeholders will be key to achieving the objectives. **Consult with your Schools Forum and local providers** on your approach to the process. The parameters of the exercise should be discussed and agreed with the Early Years Reference Group or early years sub-group to the Schools Forum, exploring key questions about how the exercise will be carried out and how will providers be fully involved. The group should provide input and agree the template of information required and the methodology.

It will also be important to ensure that all relevant parts of the LA are engaged at the planning stage, particularly finance, research and information services colleagues. Where possible, the analysis should be linked with wider work of the LA, especially the Childcare Sufficiency Assessment, which will involve surveys and assessments of the supply of childcare in the authority.

Authorities will want to ensure that their Early Years Reference Group is fully representative and has legitimacy and standing with other providers. To establish the group LAs should:

- Identify any existing networks/groups and whether they are inclusive to all providers and have wide membership that reflects the local provider market e.g. full day care settings, sessional providers and childminders
- Ensure that effort is invested in building new groups
- Consider how best to engage larger providers and representative organisations. National bodies such as NDNA and The Pre-school Learning Alliance may be in a position to offer support and access to a wider constituency of settings.
- The group should have simple Terms of Reference to make clear the responsibilities of all involved and ensure the group is legitimately representing providers
- Examine how spokespeople/representatives are chosen – they should have a proper mandate from group members and have systems in place to gather opinions to feed into the Schools Forum and to feedback to the sub-group
- Consider what support might be offered to members to overcome any barriers to engagement, e.g. training in representation and briefings on the assessment process and workings of the Schools Forum

What are the timescales?

Local authorities are required to complete the cost analysis and present the findings to their Schools Forum before budgets are set for 2008-09. The exact timing will vary in authorities from the autumn of 2007 through to the early part of next year. Given this timescale it is important that the remit and scope of the work are carefully thought through. The time needed, response rate and the quality of the information provided will vary depending on the method used.

What research methods will you use?

The most appropriate methods of collecting the required information will be different for each local authority, depending on the consultative structures that are currently in place, as well as the size of the authority and the nature of the local PVI sector. Questionnaires, telephone surveys and face-to-face interviews, network meetings and individual visits to settings by local authority officers, are likely to be the most effective methods for gathering the information you need. You might also consider a 2-stage process, where an initial questionnaire or telephone survey is used to collect information from large numbers of providers, and is followed up by telephone or face-to-face interviews where more detailed information is gained from a smaller sample of providers. Where providers are part of a larger operation the Nursery Manager may not be best placed to provide financial data – a short telephone survey to identify the right contact would be advisable. Dedicated resources and leadership from Early Years officers will be key to success.

What about confidentiality?

Consideration needs to be given to how authorities will build trust with providers so that they submit information with confidence that it will be used appropriately. Data seen by the Schools Forum and Early Years Reference group should be anonymised and should be used only for the purposes of this cost analysis, for example, by aggregating data so that individual providers cannot be identified. As well as agreeing these local terms of engagement, authorities should persuade providers of the benefits of investing the time in providing the information and ensuring that it is as full as possible in order to reform the funding system in the longer term.

Detailed advice on carrying out quantitative and qualitative research in childcare can be found at <http://www.everychildmatters.gov.uk/resources-and-practice/IG00195/> (This toolkit was designed in reference to the Childcare Sufficiency Assessment but has many relevant sections, as well as links to additional guidance on research techniques.)



2. Advertise the activity - engaging providers

Clear and consistent communications activity will help give the exercise a local identity that will be recognisable to providers. It can also help to increase providers' confidence that the communications received are official and the data they provide will be anonymised and used appropriately.

You will need to make sure **all providers** in your area are aware of the following:

- Why this is being done - that this analysis is part of an on-going process to reform the funding of the free entitlement, working towards the introduction of a single formula and a more consistent and transparent approach to funding the free entitlement across sectors
- What the process will involve, including relevant dates
- Who is on the Early Years Reference Group to represent different types of provision
- An indication of what they will need to provide, including the level of detail
- Where they can find additional information
- What you have already done – (i.e. consultation with Schools Forum and Provider Forum)
- How this agenda will be delivered in line with Government guidance

LAs who have completed this process have found that sharing information at the first available opportunity helped them to build a relationship of trust with the sector. **A mix of communication methods**, from direct mail shots and newsletters through to adverts in the local press and high profile events will help to secure maximum coverage. You may wish to consider:

- **Writing to all registered providers** using the CIS database as a source of information.
- **Hosting events and information sessions** as an opportunity to advertise the analysis, test out ideas for data collection and address providers' concerns. You will need to consider running events at times of day that make it easy for providers to attend.
- **Using existing networks and forums** - In many areas there are networks already set up, where childcare managers/owners meet in an informal way to discuss practice and business issues. These are ideal forums to meet a number of providers face to face to explain the rationale for the analysis, and explore its impact and opportunities.
- **Advertising through an Early Years newsletter or the LA website** – Publishing the strategy on the LA website, outlining clear and transparent ways of working, consultation and participation routes, will provide a useful resource that can be referenced in communications.

Whether at an event or in other communications, it will be important to outline:

- Those parts of the process that are **already predetermined** (e.g. the presentation to the Schools Forum and publication of the analysis, and the timescales) and
- The parts of the process that you are **seeking to determine** (e.g. how settings are categorised and the issues that they are facing, approaches to data collection and the factors to be considered, and the way in which the funding is distributed).

The Contestability Checklist process for PVI engagement in Children's Centres devised by NDNA on behalf of DCSF is a similar process to the above and will be a useful resource to local authorities here – see <http://www.surestart.gov.uk/publications/?Document=1848>

Case study: Rochdale MBC

Contact: Bob Adams

Between December 2006 and February 2007 Rochdale carried out a phone survey of PVI providers to gather fees information and looked at maintained sector costs in order to move from sector specific “flat rates” to differing rates according to cost of delivery. Although this does not cover PVI costs, their experience does highlight the importance of strong provider engagement.

Method and Analysis:

Firstly the authority phoned all PVI providers and asked for a full breakdown of all their charges (am rates, pm rates, daily rates, weekly rates, monthly rates etc) and what was included in that rate (lunches were often charged for in the am rate). This was used to calculate an average charge for each provider and an average charge for the borough. In the maintained sector, they compared actual school budgets (from formula funding) to the costs required to deliver. This was used to calculate funding for the extension of the free entitlement to 15 hours in maintained settings as part of the Pathfinder project: <http://www.everychildmatters.gov.uk/earlyyears/flexibleentitlement/>

Findings:

Rochdale used their pathfinder steering group to discuss the idea of sector specific rates that would reflect the different costs in different settings and help address sustainability concerns. They eventually arrived at different rates for childminders, playgroups and private day nurseries.

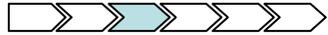
The authority then met with a representative sample of providers from each sector and compared the new proposed rate to their actual costs of delivery. This was then reported back to the various boroughwide associations and forums. All sectors agreed with the proposed changes..

Outcome:

Rochdale introduced individual sector hourly rates as opposed to a flat, all-sector, session rate. Additional funding was agreed through the Schools Forum to ensure that these rates could be maintained in future years. It took time to get providers on board, but now the borough has 126 of 132 eligible providers delivering the extended offer with more coming on board in September.

Lessons learned – Rochdale said:

“Even though some providers effectively took a cut on their hourly rate, there was no real opposition to the proposals we made. We had sought to be honest and open regarding the proposals, why we were doing it and how we had arrived at our findings. We had also been honest about this being a starting point and that there would be future reviews as the extended entitlement becomes reality. There was and is obviously concern about change, particularly where funding and the security it brings, are involved. We feel strongly that entering into an honest, open and transparent discussion goes some way to preventing and being seen to address fears and concerns in the process.”



3. Collect the data – developing the evidence base

Authorities will need to consult and work in partnership with providers to decide on the most appropriate categories to use when identifying the key cost drivers and headings for collecting the data. We would expect to see the following factors considered:

- Staffing costs (including recruitment and holiday pay)
- Administration and management costs
- Premises costs: Rent (or equivalent) and Business rates, where relevant
- Heat/lighting
- Equipment and materials (e.g. toys)
- Insurance / legal costs
- Contingency / reserves
- Registration Fees (e.g. Ofsted)
- Training (including staff cover)
- Outreach / marketing
- Telephone / Internet
- Refreshments / Food
- Consumables (e.g. cleaning, stationary)
- Maintenance
- Travel/transport (e.g. visits to out door play space)

The table below sets out the headings used in collecting cost information through the DCSF annual Providers Survey. This can be used by authorities as a starting point for developing a data collection template. The table sets out national averages in Full daycare and Sessional settings based on the 2005 survey results. We have also included figures collected by the department through a survey of individual settings in 9 local authorities across the country. This demonstrates the variation that exists at local level and highlights that the national averages are not necessarily representative. The 'other costs' category here is clearly quite broad and represents a significant proportion of the overall non-staff costs. LAs should therefore consult with providers on other, more specific categories to mitigate the risk of having a large 'other costs' category. A sample questionnaire, including an alternative formulation for cost heading, is attached at Annex A.

Things to consider when deciding on what cost categories to use:

- local authorities will need to consult with providers about how profit and surplus are included within the analysis. It may be useful to collect data on levels of profit / surplus that providers consider necessary to remain sustainable. A better view across the authority on 'normal' levels of profit will help inform local assumptions.
- Some surplus may be necessary for settings to ensure contingency resources are available to protect them from unexpected circumstances. In particular it will enable them to manage uneven occupancy levels over the course of the year - these should be regarded as legitimate costs of running a sustainable setting.
- Equally, in some small settings profits or surpluses may in fact represent staff costs.
- Capital costs should be included in the analysis – e.g. premises, items needed for effective delivery (such as toys) and equipment, including maintenance and replacement. Local authorities will need to ensure that when it comes to considering these costs in the context of funding the entitlement that the relevant rules on the use of capital and revenue grants are adhered to.

Table 1: Example cost headings

Annual expenditure	Full Daycare		Sessional	
	Providers Survey 2005 (excl zeros)	Average of LA analysis (excl zeros)	Providers Survey 2005 (excl zeros)	Average of LA analysis (excl zeros)
Cost of premises	11,800	17,232	3,900	5,300
Insurance	2,000	1,295	700	317
Toys, books etc	2,600	3,541	1,200	1,397
Business rates	4,200	14,633	1,400	0
Food	5,700	6,291	600	871
Other consumables	1,700	1,926	700	682
Professional fees	1,800	1,719	500	644
Transport	1,800	660	600	893
Other costs	13,200	13,632	6,600	1,927
Total non-staff costs	44,800	48,462	16,200	9,538
Total staff costs	128,650	128,377	25,800	26,675
TOTAL EXPENDITURE*	173,450	176,839	42,000	36,213

Provider characteristics

As well as deciding on relevant categories of provider type (e.g. Voluntary / Private/ Independent and Full daycare / sessional) authorities will also need to supplement data on the **characteristics of the setting** in order to develop a unit cost analysis for free provision, including:

- Number of free entitlement places available
- Average number of children attending (to help calculate an occupancy rate)
- Age ranges of provision offered
- Opening hours
- Number and type of full and part time staff employed
- Number of free entitlement hours/sessions booked this funding period
- Number of free entitlement hours/sessions delivered as a percentage of the overall business
- Meals provided free
- Meals provided at a reasonable additional charge
- Additional services provided for 3 and 4 year olds that are beyond the free entitlement and the remit of the EYFS (and so not eligible for free entitlement funding) e.g. specialised musical instrument tuition, professional dance or language tuition, etc.
- Receipt of other funding support e.g. sustainability funding, capital development, training
- Location – is the provider in a deprived or rural area?

It is realistic to assume that in sparsely populated areas the cost of provision is likely to be higher. Many of the costs associated with delivering the free entitlement are fixed (e.g. rents) or semi-fixed (e.g. staff costs) and so small changes in occupancy at certain thresholds can affect providers' sustainability.

Case study: Bracknell Forest Borough Council

Contact: David Allais.

In October 2006 Bracknell Forest collected cost and income data from PVI providers using a questionnaire to inform decisions on increasing funding for early education.

Method:

Following a provider meeting a questionnaire was sent to all providers to determine the extent of reported financial difficulties. The short questionnaire asked for details of all costs and income associated with the provision of the free entitlement. They were asked for the actual costs for Summer Term 2006 and the forecast costs for Autumn Term 2006. The data was analysed to determine average costs and income per setting and the extent to which settings were experiencing a shortfall in funding.

The authority has a good relationship with local providers, built on trust, and settings were therefore willing to take part in the exercise.

Outcome:

Bracknell Forest BC had previously increased funding annually by a cost of living increase aligned to teachers pay. While this was considered a good increase and well received by their Early Years providers, it only took staff costs into consideration and not all the other operating costs. The findings of the analysis were discussed by the Schools Forum and used as evidence in securing a 6.7% increase in the free entitlement funding for 2007/08, in line with the increase in the Dedicated Schools Grant.

This increase has been instrumental in reducing the number of requests for sustainability funding and the number of settings closing for financial reasons. The process and funding increase has also helped to demonstrate to PVI providers that the Local authority values their services and takes action when problems are identified.

Lessons learnt:

The main issues encountered were low rates of return on the survey within the deadline and variability in how the data was provided. 14 of 49 settings (4 private and 10 voluntary) responded in time and other responses after the deadline had to be excluded. Some figures were given as annual totals while others were termly and there were differing levels of detail - some providers went to great lengths to list every cost associated with running a setting, others only provided very basic information.

The authority will repeat the process to inform the next budget round. In order to incorporate the lessons learned, Bracknell Forest are planning to:

- a) Hold a provider meeting, to which all relevant staff are invited and encouraged to attend.
- b) Explain fully why they are collecting data, what it will be used for, who will have access to it, what benefits the exercise will have for the settings and what information (and in what format) they need to collect.
- c) Change the questionnaire to provide more guidance on the type and format of information required.
- d) Provide support to providers during the data collection (through the LA's development officers and finance officers), and
- e) To allow enough time for all settings to have a chance to provide the requested information and to be proactive in encouraging all settings to respond.

This section has outlined the range of factors that may affect the cost of delivering the free entitlement in different settings. However, it may not be possible or necessary to gain discreet data for each of these areas and local authorities will need to tailor the approach to local circumstances. Some local authorities have found it helpful to work at a similar level and in similar categories to the way in which providers publish their financial data.

If collecting termly data it is advisable to collect cost data for at least two funding periods/terms so that they can be compared and a yearly average can be derived. If annual cost data is being collected, data from the previous year can be used as a check. This analysis is part of a longer term process of reform and Authorities may want to repeat it in future years to ensure that costings are kept up to date. This should be made clear to local providers as it could help them streamline the provision of information in future years.

Some of the data received may not be complete or may be inconsistent or insufficiently detailed and therefore unreliable. Providers who fall into this group can either be removed from the sample or contacted again with a view to collecting further information. Larger authorities may want to consider selecting a representative sample of local providers for the purposes of the survey – in these cases it may be necessary to have a wider forum through which the results of the survey can be tested for accuracy. Some authorities have found that asking settings to provide copies of their accounts can help validate the data – this clearly needs to be agreed with providers and be subject to commitments to confidentiality.

Case study: *North Somerset*
Contact details: Louise Malik

North Somerset sent out a questionnaire at the beginning of May 2007 and providers were given until the end of May to respond. They collected data on setting characteristics, staff costs and non staff costs, each broken down into a number of smaller headings. The work was undertaken by a sub-group to the Schools Forum which was set up to look at the funding of the free entitlement in light of the consultation on Schools, Early years and 14-16 Funding 2008-11.

As a result of this work North Somerset are currently considering basing their funding model around staffing ratios in different settings and providing protection for rural providers.

Lessons learnt:

Some issues were encountered around the number of responses and the quality and consistency of the data received from providers. This meant at times it was difficult to identify similarities between different providers as the information provided was so variable, for example, some providers classified all of the leader's time as management and didn't reflect their time with the children.

- *Be clear about the type of information you want providers to supply (i.e. what to include under each heading, whether data should be hourly/weekly/termly etc.) to ensure consistency and enable comparisons to be made between settings*
- *Where possible plan in some leeway on deadlines to enable late responses to be included and to return to providers to 'sense check' data and iron out inconsistencies*
- *Carry out a data collection exercise on a face to face basis with a small representative group to really get underneath the cost drivers and the best way to estimate the costs associated with delivering the free entitlement*

Costs – not fees.

Some authorities have compared their funding rates to the fees which providers charge. This will not be considered sufficient for the analysis of the cost of provision that we are expecting all authorities to undertake. Our research suggests that provider fees are not always reflective of the cost of providing care for different aged children (instead they are often set to ensure revenue covers the costs of the setting as a whole). As staffing is the main cost driver for providers and staff:child ratios are lower for 3 and 4 year olds than for younger children it would be expected that fees would be significantly lower for this age group. We have found that this is not generally the case as many full day care settings in particular chose to have a 'flatter' fee structure across different age ranges. Therefore, it is more reliable for the analysis to be based on a bottom-up analysis of costs.

Why is the type of provider important?

Different types of providers tend to have different operating models and so their cost bases vary. For example, a childminder caring for a small number of children in his or her own home is likely to have a different cost base to a large private full daycare provider, in rented premises and providing group based care from 8am – 6pm. Some larger provider chains may benefit from economies of scale in the costs they incur which might be taken into account. Equally, some small sessional providers only offering the free entitlement will need to have more of their core costs taken into account. Some LAs have found it useful to categorise their providers based on these differences, or to categorise according to 'private' or 'voluntary' ownership in order to recognise business rates charges in the private sector.



4. Analyse the data – producing a unit cost

From the data received you will be looking to derive approximate costs for delivery of the free entitlement by different categories of providers. Arriving at an approximation for fixed costs (rent, business rates, heating, etc.) may be more straightforward, whereas age-variable costs (staffing, equipment, food, etc.) will require more detailed preliminary calculation.

Where settings only provide care for 3 and 4 year olds it will only be necessary to collect 'whole setting' cost data which can then be divided by the number of free entitlement hours delivered to get the approximate costs associated with providing care for one child for one hour or session.

Where settings provide childcare for a wider age range of children it will be important to identify the costs of providing care to 3 and 4 year olds as distinct from other age groups. The specific costs associated with 3 and 4 year olds can be derived by developing an 'activity based cost'. This involves weighting the providers' staff costs according to the number of children attending in the different age bands and by the staffing ratio requirements applicable to those bands. Other costs relevant to delivering the free entitlement – such as premises, food, equipment and administration – can be estimated as above by dividing the total cost by the proportion of free entitlement hours / sessions delivered.

Authorities will need to consider any changes that may result from the introduction of the Early Years Foundation Stage from September 2008, which will give PVI providers the option of operating at a 1:13 staff:child ratio where they have a graduate leader.

Case study: London Borough of Greenwich

Greenwich has done a unit cost analysis in the maintained sector which provides a useful example of a process that could be applied more widely. This was done early in the 2007 Spring term in order to compare the funding rates of the maintained and PVI sectors.

Method:
In Greenwich maintained nursery class allocations are based on an activity-led funding model, i.e. schools are funded on the basis of 1 x teacher & 1 x early years practitioner per class of 25 fte places. In addition to this, funding is allocated on a per place basis for management, variable premises costs (cleaning, water), and a range of delegated council services (for example, governor services, personnel services, etc). This funding model was converted into a cost per pupil per session using the following methodology;

Maintained nursery classes	Formula funding per class of 25 FTE (2006-07)	
staff funding	£77,085	
premises costs	£2,573	
curriculum resources	£2,172	
costs of delegated services	£812	
TOTAL COSTS PER CLASS	£82,642	A
No of sessions per year (190 school days x 2)	380	B
cost per session per class	£217.48	C (A / B)
staff cost per session per pupil	£8.70	D (C / 25)

Analysis:
The analysis highlighted that free entitlement in the maintained sector was marginally better funded than the Private & Voluntary Sector, which was being resourced at the rate of £8.00 per session.

Outcome:
To ensure equity of funding, and with the agreement of the Schools Forum, the unit rate for the PVI sector was increased from 1/4/07 to £9.00 per session (£8.70 + 3.5% inflation). This was at a cost of £165,000.



5. Present

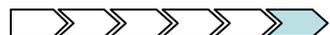
You will want to discuss and agree the draft findings of the analysis with the **Early Years Reference Group** (as well as with other relevant groups/networks) before they are finalised, so that their knowledge of the market and views are reflected in the analysis and conclusions. Full discussion with PVI providers will also help to ensure that the findings are accepted by the sector. The reference group may want to provide input to the conclusions for the benefit of the Schools Forum.

As set out previously, the findings of the analysis should then be presented to your **Schools Forum**. The purpose of the exercise is to promote local discussion as to the early years funding arrangements in the context of the early years funding reforms. Having been consulted early in the process – during the planning stage – they should be familiar with the rationale and aims. However, it will be important to ensure that the member who is presenting the proposals is given the support they need. At this stage it will be important to outline:

- the local authority's duty to ensure all 3 and 4 year olds have access to free early learning and care (see the current Code of Practice <http://www.surestart.gov.uk/publications/index.cfm?document=1747>).
- how this duty fits into the wider local authorities responsibilities – such as the sufficiency duty and targets to improve the outcomes for young children, and to narrow gaps in early achievement (see <http://www.dfes.gov.uk/consultations/conDetails.cfm?consultationId=1475>).
- the role the PVI sectors play in delivering the free entitlement
- the differences between the local PVI and maintained sector funding mechanisms (see <http://www.everychildmatters.gov.uk/resources-and-practice/IG00178/> and www.everychildmatters.gov.uk/earlyyears for the results of the DCSF national survey)
- the other funding available to support providers - capital and revenue funding is available from the General Sure Start Grant (the Sure Start, Early Years and Childcare Grant from 2008) to support providers to remain sustainable and to meet the needs of disabled children and those with SEN. That can include capital support for the extension of the free entitlement or to improve the quality of provision as well as dedicated resources for staff training and development through the new Graduate Leader Fund. Long term financial support for sustainability may only be justified in exceptional cases (see 'Securing Sufficient Childcare', paragraph 4.28 at <http://www.everychildmatters.gov.uk/earlyyears/sufficiency/>)

As set out above the presentation of the analysis should cover the following key points:

- identification of the key cost drivers taken into account for the analysis
- a description of the local PVI market of providers, highlighting different operating circumstances and how they might affect the cost of delivering the free entitlement in different types of settings
- an outline of the process and analysis undertaken by the authority (e.g. survey and consultation mechanisms used, response rates and assessments of how robust the data is) and,
- a conclusion which places the cost analysis in the context of previous and planned spending on the free entitlement, child outcome targets, sufficiency and sustainability.



6. Publish

The findings of the analysis should be published on the local authority website – with any financial data properly anonymised - alongside the terms of reference and the next steps to be taken and how this work will be progressed in line with Government guidance on funding reform.

Next steps

Carrying out this analysis of the costs of provision will underpin the future move to a single formula. It will enable authorities to consider how funding is distributed to providers (monthly, termly etc.) and the impact this and any claw back arrangements are having on providers' sustainability and ability to invest in the services they are providing. (Upfront payments can help ease cashflow problems for some providers). Local authorities may want to consider changing the level of funding for all or some providers (e.g. introducing a banded approach) in light of this analysis and other considerations and in advance of the introduction of the single formula. Consultation and partnership working with providers will be vital to the success of any funding reforms and should be undertaken with a view to the longer term changes over 2008-11. An explanatory note on the introduction of a single formula and the other changes to early years funding announced earlier this year will be published in autumn 2007.

For more information and support please contact:

At **DCSF**:
Childcare Division
Caxton House, 6-12 Tothill Street
London, SW1H 9NA
e: Childrens.learning@dcf.gsi.gov.uk
w: www.everychildmatters.gov.uk/earlyyears

At **The Pre-School Learning Alliance**
The Fitzpatrick Building
188 York Way, London N7 9AD
Tel: (020) 7697 2500
Fax: (020) 7700 1599
e: info@pre-school.org.uk
w: www.pre-school.org.uk

At the **National Day Nurseries Association (NDNA)**:
National Early Years Enterprise Centre, Longbow
Close, Huddersfield, HD2 1GQ
t: 0870 774 4244
f: 0870 774 4243
e: info@ndna.org.uk
w: www.ndna.org.uk

Annex A: Sample provider questionnaire

[Contact details and timescale for return of form]

		Information Required	Please Insert Responses referring to the Notes for Guidance as required			
1	Please insert the name of your organisation	Name of Provider Organisation				
2	Please enter the name of the person completing the survey	Name of Respondent				
3	Please enter the position held by the respondent (for example – owner, manager, supervisor)	Position of respondent in Provider Organisation				
4	Please indicate which sector your setting is in	Please tick the relevant box to indicate whether you are a Private (P), Voluntary (V) or Independent (I) setting		P	V	I
	And please indicate whether you offer only sessional care or full day care.	Please tick the relevant box to indicate whether you provide Sessional (S) or Full Day Care (F) provision	S		F	
5	Please indicate whether your organisation is:	Ownership Structure	<i>Please tick whichever applies</i>			
	- Privately owned and managed (typically a small business founded and run by the owner)	- Privately owned and managed				
	- A part of a larger private sector childcare group	- Voluntary sector				
	- A part of the voluntary (non-profit making) sector	- Member of larger privately-owned group (identify the total number of				
	- Any other form of ownership (please specify)					

		nurseries/settings in the group)	
		- Member of larger voluntary sector group (identify the total number of nurseries/settings in the group)	
		- Other form of ownership	

6	Please indicate when your organisation began to provide childcare at this setting	Date the provider began to provide childcare	
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7	Please specify the ages of children who attend by the three age bands specified	Age range attending (please tick all the boxes which apply)	0 to 2 years	2 to 3 years	3 and 4 years	Other
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8	Please provide details of average hours of care per week for children attending by age band	<p>We wish to identify the breakdown of hours of care per week by age band, where possible. We appreciate that this may be an estimate based on current attendance patterns.</p> <p>E.g. if you are a full daycare provider, with 15 children aged 2-3 who, on average, each attend for 9 hours per day, 4 days per week, you would enter 540 hours in this column (i.e. 15 x 9 x 4).</p> <p>E.g. if you are a morning sessional provider with 10 children aged 3-4 who, on average, each attend for 2.5 hours per day, 5 days per week, you would enter 125 hours in this column (i.e. 10 x 2.5 x 5).</p>	0 to 2 years	2 to 3 years	3 and 4 years	Other

9	Please set out the days of opening per week and the hours you open each day	Opening Hours	Mo	Tu	W	Th	Fr	Sa	Su	
		- Days of opening per week (please tick every day you are open)								
		- Opening/Closing Times (please use the 24 hour clock)								
		Please indicate whether you are closed: - At any particular times of day, for example over lunch	Number of weeks open per year e.g. 38 weeks, 50 weeks							
		Closure at particular times of day								

10	Please provide a breakdown of your costs based on your latest full year accounts, using the following headings if at all possible. Please round to the nearest pound Please indicate the accounting year that this relates to If you are unable to use this cost breakdown please use your own headings with an explanation of what is included under each heading	Costs (total for the business) based on your latest full year accounts or last full year of operation.	
		- Employees (including agency staff costs)	
		- Premises (including rent, rates, heating, lighting etc)	
		- Transport	
		- Supplies and Services (all bought in goods and services)	
		- Agency and Contracted Services (including all professional services such as legal and accounting)	
		- Recharges (including interest and payments for group services e.g. share of administration overhead if relevant)	
		- Other (please define)	
		- Total Costs	
		- Accounting Year	