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KAI Benefits and Credits

Working Tax Credit:

Take-up of Childcare Element

2008-09

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Working Tax Credit

Take-Up of Childcare Element 2008-09

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Summary of Main Findings

This publication estimates the numbers of families entitled to, but not claiming the childcare element of Working Tax Credit (WTC) and uses this information to calculate a take-up rate. Information is drawn from administrative data, from HMRC's Tax Credit and Child Benefit Study, and from other surveys such as the Family Resources Survey.

Childcare Element Take Up

- There were, on average, 448 thousand families who benefited from the childcare element of WTC in 2008-09.
- Using Tax Credit and Child Benefit Study survey data linked back to tax credits administrative records, we estimate around 52 thousand families already in receipt of tax credits were entitled to, but did not claim, the childcare element in 2008-09.
- Based on Family Resources Survey data, adjusted using similar methods to those in the main tax credit take-up rates publication, we estimate around 55 thousand families were entitled to childcare element but did not claim tax credits in 2008-09.
- Using the above figures, we therefore estimate that the caseload take-up rate for childcare element was around 81 per cent in 2008-09.

Childcare Element Ratio

- The proportion of tax credit recipients entitled to more than family element who claim the childcare element (sometimes known as the childcare element ratio) was 18 per cent in 2008-09. This ratio is occasionally used as a proxy measure of "take-up".
- The main reason the childcare element ratio is much lower than the take-up rate is because of the almost 2 million families in the denominator who are not eligible for childcare element. The three main reasons families are ineligible is because they are single-earner couples (33%); because they do not use any childcare (29%); or because they only use ineligible forms of childcare, such as family or friends (29%).

1. Introduction

Child Tax Credit (CTC) and Working Tax Credit (WTC) were introduced in April 2003 and replaced Working Families' Tax Credit, Disabled Person's Tax Credit and Children's Tax Credit, as well as some other forms of financial support for families with children. WTC also extended in-work financial support to families without children or a disability.

The main publication presents estimates of annual take-up rates for CTC and WTC, covering the 2008-09 financial year. More details about the eligibility criteria for tax credits, and the methodology used in the production of the take-up rates, are available in that publication.

This special supplement to the 2008-09 main publication looks in more detail at take-up of one specific element of tax credits, the childcare element of Working Tax Credit.

The origins of the childcare element can be traced back to the childcare disregard in Family Credit¹, which was introduced in October 1994, when childcare costs of £40 per week could be disregarded in the income calculation for Family Credit. The generosity of the disregard was increased at various stages until the disregard was replaced along with Family Credit itself when Working Families' Tax Credit (WFTC) was introduced in October 1999. From this date, WFTC contained a "childcare tax credit" worth up to 70% of eligible childcare costs up to maximum cost levels of £100 per week for one child in childcare, and £150 per week for two or more children in childcare. These limits rose to £135 and £200 respectively from June 2001.

After the introduction of Child and Working Tax Credit in April 2003, the childcare tax credit was renamed as the childcare element of Working Tax Credit, and the level of support was increased in subsequent years to 80% of eligible childcare costs, up to maximum cost levels of £175 per week for one child in childcare and £300 per week for two or more children in childcare². The 2010 Spending Review announced that the level of support will return to 70% of eligible childcare costs from 2011-12 onwards.

Although the childcare element may be viewed as simply one of many elements within the tax credits system, it has tended to attract more attention than others. The role of childcare in allowing parents, particularly lone parents, to move into work means it is of interest both in terms of improving work incentives and alleviating child poverty. There are also potential effects on child development outcomes which may result from children participating in formal childcare.

In recognition of the higher level of interest, this publication looks specifically at take-up of the childcare element: how a take-up rate can be defined, estimates of the groups which are entitled to it but do not claim, and what the level of the take-up rate is likely to be.

¹ A childcare disregard was also available from October 1994 in Disability Working Allowance, which was replaced by the childcare tax credit element of Disabled Person's Tax Credit in October 1999, before being subsumed into Working Tax Credit in April 2003.

² The increase in the limits took place from April 2005, whilst the rise in the percentage of costs covered to 80% took place from April 2006.

2. Definitions

Eligible childcare

The definition of eligible childcare is set out in the Tax Credits Manual (see: http://www.hmrc.gov.uk/manuals/ntcmanual/eligibility_childcare/ntc0260100.htm). Broadly, with a few exceptions, “eligible” childcare corresponds fairly closely with what is often termed as “formal” childcare – childcare typically provided by a carer who is registered with the appropriate authorities (eg. Ofsted in England). It encompasses group settings such as nurseries, playgroups and out-of-school clubs, and also care provided by registered childminders. Eligible childcare can also be provided within the child’s home, as long as the childcare provider is approved and is not a relative of the parent.

Claiming for eligible childcare costs

Childcare costs can be claimed for either during the initial tax credits claim process, or subsequently. For those claiming in their initial tax credits claim, the claim form asks whether each child is in eligible childcare, and separately, asks for details of childcare costs incurred and the details of the childcare providers who are supplying the childcare. Alternatively, the parent may claim tax credits without reporting any use of eligible childcare, but then report to the Tax Credits Helpline that they have started using eligible childcare during the year. A further possibility is that they report using childcare retrospectively after the year has ended, during the finalisation of their award. However entitlement to the childcare element can only be backdated up to three months from the date of claim or notification.

Due to the annual nature of the tax credits award, parents are asked to give childcare costs expressed as an average. Whether costs are weekly, monthly or paid at other frequencies, parents should work out how much they pay over the course of a year and divide by 52 to get a weekly average. Since April 2010, parents who only need childcare for short fixed periods (such as during the school holidays) can have their costs calculated and paid over the period they use the childcare instead.

Claimants benefiting from childcare element

Not all tax credit claimants can benefit from a higher tax credit award, even if they are using paid, eligible childcare and have claimed for childcare support. Only in-work tax credit recipients, whose award is higher than the family element of £545 per year, and who typically are on low or moderate incomes, will see an increase in their award. In 2008-09, there were around 5.7 million families with children benefiting from tax credits, of whom 2.5 million were in work and entitled to more than the family element. Of this group, around 448 thousand were benefiting from the childcare element; that is, they applied for childcare support through tax credits and were receiving a higher award as a result.

Take-up Rate

A take-up rate for the childcare element is based on the same definition as that used in the wider tax credits and Child Benefit take-up statistics: which is that, broadly, the take-up rate is defined as the number of families who receive support, dividing by the number of families who are eligible. Due to inaccuracies in measurement of the total eligible population using survey data, we estimate the eligible population to be the

number of recipients plus the number of entitled non-recipients. For the childcare element, the take-up rate is therefore defined as:

$$\frac{CC_A}{(CC_A + ENRCC_P + ENRTC_F)}$$

Where:

CC_A is the administrative caseload (the number of families benefiting from childcare element);

ENRCC_P is the number of childcare element entitled non-recipients who are already claiming tax credits, and is based on Tax Credits and Child Benefit Study data;

ENRTC_F is the number of tax credit entitled non-recipients who are also entitled to childcare element, and is based (primarily) on Family Resources Survey data.

The caseload term, CC_A, and the ENRTC_F term are broadly similar in definition to those we use in our standard tax credits take-up rates methodology (with some modest alterations and assumptions which will be described later). The key additional term is ENRCC_P. This measures the number of families who have already claimed tax credits, and are entitled to, but who have not claimed childcare element. It makes use of the Tax Credits and Child Benefit Study dataset, of which further details are given below.

3. Calculating the take-up rate

a/ The administrative caseload

The administrative caseload is the number of families benefiting from the childcare element in 2008-09, based on finalised tax credits award data.³ As noted earlier, there were around **448 thousand** families benefiting from the childcare element in 2008-09.

b/ Entitled Non-Recipients already claiming tax credits

In 2008, HMRC commissioned the National Centre for Social Research to conduct a large scale panel survey, the 'Tax Credits and Child Benefit Study', to contribute to a better understanding of different aspects of tax credits and Child Benefit. The first wave of this research took place between October 2008 and February 2009, and involved over 3,600 face to face interviews with current and previous tax credits recipients. The study was aimed at exploring people's experiences of a wide range of issues within the tax credit and Child Benefit systems.

In order to improve the quality of the data received, respondents to the survey were asked whether they consented to their survey responses being linked back to tax credits administrative data. This proved largely successful, and 82 per cent of families who participated in the survey agreed to have their details linked⁴.

Linked survey data allows us to accurately estimate **ENRCC_p**, the number of childcare element entitled non-recipients who are already claiming tax credits. We cannot normally estimate this group using administrative data, because HMRC data does not capture those using eligible childcare but not claiming for it. We also cannot use our conventional main data source for estimating entitled non-recipients, the Family Resources Survey, because it does not accurately estimate receipt (and therefore non-receipt) of childcare element amongst tax credit recipients. Only linked data provides the full information we require.

The panel study questions on childcare ask: "What are your usual arrangements for looking after [your child/your children]?" Separate questions are asked about childcare in school term-times and holidays where usage differs, but because the vast majority of the panel study fieldwork took place during term-time, we use term-time responses in order to measure childcare element eligibility. Where childcare was paid, registered (where applicable), and in one of the following categories, we considered that childcare (and by extension the family using it) to be "eligible" for childcare element:

- Nursery school, nursery class or reception class;
- Special day school or nursery or unit for children with special educational needs;
- Day nursery;
- Playgroup or pre-school;
- Childminder;

³ As set out in the finalised award statistics: <http://www.hmrc.gov.uk/statistics/fin-main-stats/cwtc-final-awards-may10.pdf>

⁴ The data was checked for possible bias arising from consent; the proportion of families modelled as eligible for childcare element in the panel was 13 per cent amongst those withholding consent, compared to 14 per cent for those who gave consent. We therefore concluded that consent bias was not a significant problem for this analysis.

- Nanny or au pair;
- Baby-sitter who came to the home;
- Breakfast club or after school club/ activities;
- Holiday club/scheme.

The panel study also records the work status of individuals within families. We used the survey data to identify working lone parents, dual earner couples and single earner couples who had an incapacitated partner, to ensure that families met the work eligibility conditions for childcare element⁵.

In order to estimate whether these parents were eligible non-recipients of the childcare element, we needed to establish a/ whether they could benefit financially from the childcare element, and b/ whether they were claiming childcare element already. Both these pieces of information were taken from tax credits administrative data. We restricted the analysis to those entitled to more than the family element in the interview month, which meant that they would see an increase in their award if they claimed childcare element. We also recorded whether they had claimed childcare element in the interview month⁶.

In the event, we found 28 sample cases who met all the criteria for being a childcare eligible non-recipient – families who were using eligible childcare, met the work and income conditions to receive and benefit financially from childcare element, but who were not claiming it.

To gross this figure up to the relevant population, these 28 cases represented 2.1% of the total sample who were in-work and benefiting by more than the family element of tax credits. As there were around 2.5 million families in this position in 2008-09, applying the 2.1% to this figure suggests that there were around **52 thousand** families who received tax credits and were eligible for, but did not receive childcare element in 2008-09.

c/ Entitled Non-Recipients not claiming tax credits

The estimate of **ENRTC_F** is arrived at using methodology similar to that used in the standard tax credits take-up rate analysis. We take as our starting point the number of tax credit entitled non-recipients who are also entitled to childcare element from the Family Resources Survey (FRS), then:

- Subtract cases who are modelled as entitled to tax credits and childcare element, but who are waiting for the outcome of a tax credit application;
- Increase the remaining cases by an adjustment factor, to account for the effect of the income disregard, estimated using British Household Panel Study (BHPS) data;
- Subtract an estimate of the number of childcare element “payments reduced to zero” cases, who are likely to say they are not receiving tax credits in the FRS.

All these estimates are made in exactly the same way as those in the main publication, with the exception of the BHPS disregard adjustment factor. The sample sizes in the BHPS for tax credit ENRs who are entitled to childcare element are too small to be reliable. We therefore estimated a number of “close substitutes”:

⁵ “Working” in this context means working 16 or more hours per week.

⁶ We also checked whether families who had not claimed in the interview month had claimed in another month covered by the panel survey period; only 1 sample case had done so.

- The adjustment factor for entitled non-recipients who were in work and entitled to more than family element was 1.30 (that is, the “true” number of entitled non-recipients is estimated to be 30% higher than the numbers implied by the FRS);
- The adjustment factor for entitled non-recipients entitled to more than family element who were single and dual earner couples with a child under 12 was 1.43;
- The adjustment factor for those entitled to childcare element (recipients and non-recipients alike) was 1.29.

In the event, we judged that the second of these was the closest to the “true” estimate. Although the last of the three specifically covers childcare element eligibility, recipients tend to have lower adjustment factors than entitled non-recipients⁷ - the adjustment factor for entitled non-recipients entitled to more than family element is just over 10% higher than for both recipients and non-recipients combined. Scaling up the third factor of 1.29 by this 10% gives us a factor of around 1.42, which is almost identical to the 1.43 estimate.

Taking all the above factors into account, we estimate that the number of families entitled to, but not receiving tax credits and who are also entitled to childcare element is around **55 thousand**.

d/ The take-up rate

We now have all the elements required to construct a take-up rate estimate. The estimate is:

448 thousand recipients;

Divided by;

448 thousand recipients *plus* 52 thousand entitled non-recipients claiming tax credits, *plus* 55 thousand entitled non-recipients not claiming tax credits;

Giving a caseload take-up rate for the childcare element in 2008-09 of around **81 per cent**.

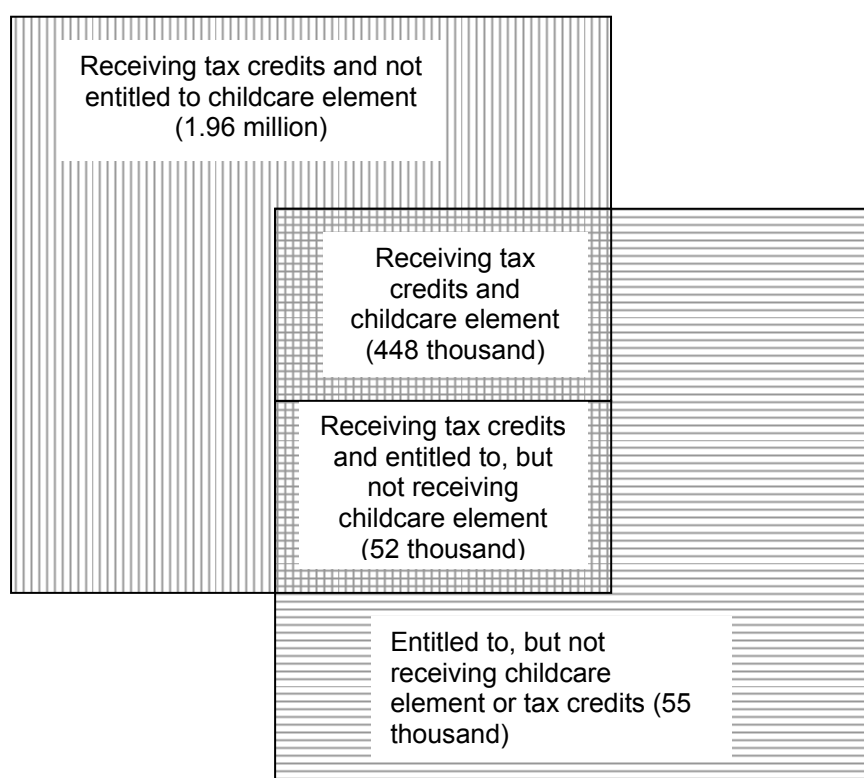
⁷ This is in line with common sense; as tax credit take-up is negatively related to income, those who have experienced bigger income increases – ie. who have a bigger “adjustment factor” – are less likely to claim and hence, more likely to be entitled non-recipients.

4. The Childcare Element Ratio and the relationship with the Take-up Rate

This section explores the relationship between two measures – the take-up rate already described, and the “childcare element ratio”, which is the proportion of tax credit recipients entitled to more than family element who claim the childcare element. In 2008-09, the childcare element ratio was calculated at around 18 per cent (448 thousand divided by 2.5 million). This latter measure is sometimes used as a proxy for “take-up”, although it is not the same as the take-up rate. For an example of where the childcare element ratio has been used, see indicator NI118 in <http://www.communities.gov.uk/documents/localgovernment/pdf/542429.pdf>

In both cases, the numerator of the calculation is the same – the number of families benefiting from the childcare element. However, the denominators of the take-up rate and childcare element ratio differ. Figure 1 shows the relationship between the two denominators.

Figure 1: relationship between the denominator of the childcare element take-up rate and the denominator of the childcare element ratio



The denominator of the childcare element ratio is the large box on the left, with vertical lines; it covers all those receiving tax credits who are entitled to more than the family element. In contrast, the denominator of the childcare element take-up rate is the large box on the right, with horizontal lines, and covers all those entitled to childcare element. Where the two boxes intersect (shown with mixed horizontal and vertical lines) these groups are present in both denominators.

The reason why the childcare element ratio, at 18 per cent, is so much lower than the childcare element take-up rate, at 81 per cent, can be easily seen from figure 1. In the calculation of the childcare element ratio, we exclude the relatively small number of tax credit entitled non-recipients (55 thousand) in the right hand box, but include a very large number of non-entitled families (1.96 million) in the left hand box. Including this large number in the denominator drags down the childcare element ratio.

Why are these 1.96 million families not entitled to childcare element? The Tax Credits and Child Benefit Study can be used to gain further insights into the characteristics of the group. We find that (grossing up results to the population entitled to more than the family element):

- Around 650 thousand (33%) are ineligible single earner couples, so irrespective of whether they use eligible childcare, they cannot claim childcare element;
- Around 140 thousand (7%) are families whose youngest child is aged 15+, who are therefore either unlikely to be eligible for childcare element, or are too old to require childcare in any case;
- Around 40 thousand (2%) are using eligible forms of childcare, but it is unpaid, so they do not require financial assistance to pay for it;
- Around 560 thousand (29%) are using only ineligible forms of childcare, such as relatives or friends;
- The remaining 570 thousand (29%) do not use any childcare – perhaps because their children are too old to need care, or the parent looks after the child themselves.

What then, does the childcare element ratio measure? To a small extent, changes in the ratio will reflect genuine changes in the take-up rate of the childcare element amongst eligible families. But with an already high take-up rate, the scope for this is limited; even with a 100% childcare element take-up rate, the 2008-09 childcare element ratio would only have reached 20%. For the ratio to increase above this level, it requires families to move into eligibility for childcare element; for example, by families using ineligible childcare to start using eligible care, or for the non-working partner in single earner couples to move into work. The childcare element ratio is therefore a better indicator of the extent of eligible childcare use amongst low income families receiving tax credits than it is of take-up, and it is for this purpose that it has been used in indicator NI118.