



Economic Effects of Expanding Subsidized Child Care and Providing Universal Preschool

November 2021

Overview

H.R. 5376, the Build Back Better Act, as passed by the House of Representatives, would expand federal subsidies for child care and provide universal preschool at no cost for eligible children. Those provisions would increase federal deficits by \$381.5 billion from 2022 to 2031, the Congressional Budget Office estimates.¹

In addition to the effects on the federal budget, those provisions would affect child care workers (including preschool teachers) and families with children. This document describes the key channels through which those changes could affect the economy—answering some questions asked by Members of Congress. Understanding those channels would be important for identifying any potential effects on the agency’s economic forecast if those provisions were enacted. The document also describes channels through which short-term spending on child care and preschool could affect the labor market in the longer run and how those policies would interact with existing tax subsidies for child care.

If subsidies were expanded and preschool was universally provided, child care providers and preschools would hire more workers, boosting wages. Some parents would work more and some would work less, depending on the ages of their children, their income, their employment status, and their child care choices under current law. On average, parents’ employment would probably increase slightly under both programs.

This document does not examine effects that would arise from how the programs were financed.

¹ The cost estimate explains potential interactions with spending on the Head Start program as well as how provisions of the Budget Control Act of 2011 are addressed. See Congressional Budget Office, “Estimated Budgetary Effects of Title II, Committee on Education and Labor, H.R. 5376, the Build Back Better Act” (November 17, 2021), www.cbo.gov/publication/57622. That estimate applies to Rules Committee Print 117-18 incorporating a manager’s amendment by Congressman Yarmuth.

Federally Supported Child Care Under Current Law

Currently, federal support for the care of young children is available to low-income families and is provided in a few ways.

In 2019, the federal government provided the following funding:

- \$10 billion was provided through the Child Care Development Fund and Temporary Assistance for Needy Families; about 80 percent of recipients were single parents. Those programs provide subsidies to parents whose income is low, who are working or participating in work-related activities (such as job-training programs), and who have young children.
- \$10 billion was provided through the Head Start Program, which funds preschool for children from low-income families.

Taxpayers can claim the child and dependent care credit for qualified child care expenses for children under age 13. The credit amount is a share of qualified expenses, and that percentage decreases as income increases over a certain range.

Other Options for the Care of Young Children Under Current Law

Some parents, especially those in higher-income families, purchase unsubsidized child care.

Other parents, especially those in lower-income families, receive care that is subsidized by their state or local government or rely on informal care while they work. Informal care is unregulated care typically provided by family members (other than parents) or friends for little or no pay.

Other parents care for their children instead of having paid employment.

The hours parents and informal caregivers spend caring for children are not counted as working in the official employment statistics, nor are the hours parents spend caring for their own children. Similarly, the child care services provided during those hours are not included in the official measure of gross domestic product.

Expanded Subsidies for Child Care—Eligibility

Under H.R. 5376, families that met the following criteria would be eligible for subsidized child care.

- The children were age 5 or younger.
- The children were not attending kindergarten.
- The parents worked or participated in work-related activities, such as job training programs.
- The family's income was below 250 percent of the state median income.

Expanded Subsidies for Child Care—Benefits

The benefit amount would be sufficient to purchase care in a child care setting that met certain requirements.

Out-of-pocket costs would be capped at a modest percentage of a family's income regardless of the number of children enrolled in subsidized care.

As a result, the out-of-pocket costs of formal child care would be lower than under current law for most eligible families after accounting for the subsidies. If additional work increased a family's income, the subsidy it received would be reduced by an amount less than the increase in income. Even with that reduction, the cost of child care would still typically be smaller than under current law.

The benefits would be scheduled to expire after six years.

Universal Preschool—Eligibility

Children ages 3 or 4 on the date established by the state for kindergarten eligibility would be eligible for free preschool regardless of their family's income. (Preschool would serve children ages 3 to 5 because some children turn 5 before the end of the school year.)

Compared with child care for children at those same ages, preschools tend to operate for fewer hours, to have more highly trained staff, and to have curricula that more closely resemble kindergarten.

Universal Preschool—Benefits

The program would provide full-day (or at least 1,020 hours per year) preschool for eligible children, and their families would have no out-of-pocket costs.

The preschool would require teachers to have certain credentials and would need to meet other requirements.

Some families would need to supplement preschool with additional care—for example, before- or after-school care. Some of those families would be eligible to receive subsidies for that care.

The benefits would be scheduled to expire after six years.

How Child Care Providers Would Be Affected

Because it would cost them less, more families would use paid child care (including preschool). The additional paid child care would mostly replace existing informal care and care provided by parents. Employment in the child care industry would increase.

- Some people who currently work in other occupations would become child care workers.
- Some people who are currently out of the labor force would also become child care workers. That group would include some family members and friends who currently provide informal care and parents who care for their children on their own.

Wages for child care workers would increase to attract additional workers to meet the higher demand. (Recruiting and training those workers would take time.) Those higher wages could increase wages and reduce employment in other related industries.

Higher wages for child care workers would increase the cost of unsubsidized child care, so some families would use less paid child care. But that decrease would be smaller than the overall increase in demand for paid child care driven by the increased demand for subsidized child care and preschool.

Capital expenditures related to child care, such as building and upgrading child care centers, would increase. (Building that additional capacity would take time.)

How Parents' Employment Would Be Affected—Overview

Lower costs of child care would affect parents' employment decisions (whether to work, not work, or change their hours of work) in two opposing ways. Many parents would be subject to pressure in both directions.

- On the one hand, additional child care would cost less, which would encourage parents to work more by lowering the cost of work.
- On the other hand, some parents would work less because they would need to work fewer hours to maintain the same level of consumption of goods and services (other than child care).

Parents' decisions about whether to increase or decrease their work hours would differ depending on their eligibility for subsidized child care (including universal preschool), their current employment status, and their child care choices under current law.

On average, parents' employment would probably increase slightly under both policies. The employment increase for mothers would be greater because they are more likely to be the primary caretakers of children; having access to low-cost or free child care would allow them to work more.

How the Employment of Lower-Income Parents Would Be Affected

On average, both expanded subsidies for child care and universal preschool would probably increase employment of parents who would be eligible for subsidized child care on the basis of their income under current law.

Nonworking parents who *would have cared for their own children* (instead of having paid employment) would work more because of lower costs of additional work.

Working parents who *would have paid for child care* would also work more because additional work would cost less, but that effect would be partially offset by some parents' preference to work less because their income net of child care costs would be higher.

How the Employment of Lower-Income Parents Would Be Affected (Continued)

Working parents who *would have used informal care* under current law would respond differently depending on their preferences and whether they were eligible for universal preschool in addition to subsidized child care.

- Some parents would continue using informal care rather than subsidized formal care, so their employment would not change.
- Some parents would choose subsidized child care—in some cases, to supplement universal preschool—because its cost had declined relative to informal care. They would tend to work less because additional work would still cost more than when using informal care; that effect would be partially offset by some parents' preference to work more because their income net of child care costs would decline.
- Some parents would choose universal preschool without using subsidized child care as a supplement. Their employment would not change because the cost of working and income net of child care costs would be unchanged.

How the Employment of Higher-Income Parents With Children Under Age 3 Would Be Affected

Parents who would be ineligible for subsidized child care on the basis of their income under current law would probably work fewer hours while their children were not old enough to attend preschool, on average.

- Some working parents whose income was only modestly above the eligibility threshold and who would have used formal care would work fewer hours to become eligible for subsidized child care.
- Some working parents whose income was well above the threshold and who would have used formal care would work less because the higher costs of unsubsidized care would increase the cost of work. Some would work more because their income net of child care costs would be lower. Both effects would probably be small.
- Nonworking parents who would have used formal care would probably not start working. That is because the higher costs of unsubsidized care would discourage work.
- Nonworking parents who would have used informal care would be unlikely to start working because the cost of working and their income net of child care costs would not change.

How the Employment of Higher-Income Parents With Children Ages 3 to 5 Would Be Affected

Some children ages 3, 4, or 5 in families with incomes above the threshold for subsidized child care would be eligible for free preschool, and the employment of those parents would probably change little, on average. Some of them would work more because of the lower cost of working part time, but others would work less.

- Currently, higher-income families are more likely to pay for child care than lower-income families. With universal preschool, some of those families would probably use free preschool and purchase unsubsidized care that extended beyond the hours for preschool.
- The cost of additional child care for hours extended beyond preschool hours would not decrease for those families, so those parents would not work more.
- Some parents, however, might work less because free preschool would raise their income net of preschool costs.

How Families' Consumption Would Be Affected

Some people who do not currently work would start working in the child care sector because of higher demand, and some workers would be attracted to the child care sector because of higher pay. Those people would have higher earnings and, as a result, their families would have more income to spend on goods and services.

Overall, the consumption of goods and services (other than child care) for families who use child care would probably be higher. (Some families could face a decline in earnings from changes in employment, but that decline would be very small relative to the decrease in child care costs.)

- Most families who were eligible for the expanded child care subsidies would pay less for child care, which would allow them to spend more on other goods and services.
- Families who were ineligible for subsidized child care would have slightly less to spend on other goods and services because greater demand for child care would lead to higher costs of unsubsidized child care.
- Families who were eligible for universal preschool would have the same or more to spend on other goods and services.

How Parents Would Be Affected in the Longer Term

The earnings of parents receiving child care assistance would probably be higher in the long run.

- Because subsidized child care would, on average, increase employment, parents would gain more work experience, leading to higher wages and greater employment in the long run.
- Those effects would probably be stronger for women, who are more likely to leave the labor force to care for children under current law.

How Children Would Be Affected in the Longer Term

The effects of subsidized child care on earnings when the children grow up are uncertain. Those effects would depend on any changes in the quality of care, which in turn would depend on the program's rules, enforcement of those rules, and responses of child care providers and parents. If the quality of child care fell under the subsidies, the effects on earnings could be negative.

Universal preschool for children ages 3 to 5 could have a positive effect on their earnings as adults, but any effect would probably be smaller, on average, than what some studies have found for existing programs.

- Children from low-income families benefit the most from preschool but are less likely than children from higher-income families to attend preschool without financial assistance. Many of those children are served by Head Start under current law, so universal preschool would probably not change the future earnings of those children.
- The adult earnings of children from higher-income families are less affected by preschool attendance. Those children typically do not have access to federally subsidized preschool under current law, but many still attend preschool. Universal preschool would extend federal subsidies to children from those higher-income families, but it would probably not change their future earnings substantially.

How Tax Subsidies for Child Care Would Be Affected

The amount of expenses eligible for the child and dependent care tax credit would change for some families.

- The amount of the tax credit could decrease for people who paid less for child care.
- People who began paying for child care under the policy might become eligible to claim the tax credit.
- Working more might not change the credit amount, but in some cases the credit would increase or decrease.

This document does not consider potential changes to the current tax credit and the related tax exclusion for child care assistance provided by employers (such as flexible spending accounts), or to the tax credit for employers that provide child care.

Selected Studies on the Effects of Subsidized Child Care and Universal Preschool on Parents' Employment

Studies on the introduction of universal preschool:

- Hao Li, “The Effect of Universal Pre-Kindergarten Policy on Female Labor Force Participation—A Synthetic Control Approach,” *Southern Economic Journal*, vol. 87, no. 2 (October 2020), pp. 440–482, <https://doi.org/10.1002/soej.12459>.
- Rasheed Malik, *The Effects of Universal Preschool in Washington, D.C.: Children's Learning and Mother's Earnings* (Center for American Progress, September 2018), <https://tinyurl.com/6esydy9z>.
- Elizabeth U. Cascio and Diane Whitmore Schanzenbach, “The Impact of Expanding Access to High-Quality Preschool,” *Brookings Papers on Economic Activity* (Fall 2013), pp. 127–192, <https://tinyurl.com/3zzfvjuh>.
- Maria Donovan Fitzpatrick, “Preschoolers Enrolled and Mothers at Work? The Effects of Universal Prekindergarten,” *Journal of Labor Economics*, vol. 28, no. 1 (January 2010), pp. 51–85, <https://doi.org/10.1086/648666>.

Selected Studies on the Effects of Subsidized Child Care and Universal Preschool on Parents' Employment (Continued)

Studies on increases in child care subsidies for low-income parents:

- Charles Michalopoulos, *Effects of Reducing Child Care Subsidy Copayments in Washington State* (submitted by Manpower Defense Research Corporation to the Department of Health and Human Services, June 2010), <https://tinyurl.com/xfmknyjm>.
- Mark C. Berger and Dan A. Black, "Child Care Subsidies, Quality of Care, and the Labor Supply of Low-Income, Single Mothers," *The Review of Economics and Statistics*, vol. 74, no. 4 (November 1992), pp. 635–642, <https://www.jstor.org/stable/2109377>.

Reviews of studies from other countries:

- Mike Brewer and others, *Free Childcare and Parents' Labour Supply: Is More Better?* Discussion Paper 10415 (IZA Institute of Labor Economics, December 2016), pp. 3–6, <https://tinyurl.com/3bc6j8f5>.
- Michael Baker, "Universal Early Childhood Interventions: What is the Evidence Base?" *Canadian Journal of Economics*, vol. 44, no. 4 (November 2011), pp. 1069–1105, <https://doi.org/10.1111/j.1540-5982.2011.01668.x>.

About This Document

This document was prepared to enhance the transparency of the Congressional Budget Office's work and to encourage external review of that work. In keeping with CBO's mandate to provide objective, impartial analysis, the document makes no recommendations.

William Carrington, Justin Falk, and Rebecca Heller prepared the document with assistance from Julia Heinzl and guidance from Xiaotong Niu and Julie Topoleski. Comments were provided by Sheila Dacey, Molly Dahl, Elizabeth Cove Delisle, Sebastien Gay, Theresa Gullo, Edward Harris, Joseph Kile, John McClelland, Susanne Mehlman, Shannon Mok, Jaeger Nelson, Joseph Rosenberg, Sam Papenfuss, Naveen Singhal, Emily Stern, Jeffrey Werling, and Sree Yeluri (all of CBO), as well as David Blau (Ohio State University), Elizabeth Cascio (Dartmouth College), Janet Currie (Princeton University), Magne Mogstad (University of Chicago), and participants in the November 2021 meeting of CBO's Panel of Economic Advisers. The assistance of external reviewers implies no responsibility for the final product; that responsibility rests solely with CBO.

Mark Doms, Jeffrey Kling, and Robert Sunshine reviewed the document. Caitlin Verboon edited it and prepared the text for publication. The document is available on CBO's website at www.cbo.gov/publication/57630.

CBO seeks feedback to make its work as useful as possible. Please send comments to communications@cbo.gov.