Smarter Funding, Stronger System:

Targeting long day care funding to need

the FrontProject | The Investment Dialogue for Australia's Children

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About the Front Project

The Front Project is a national, philanthropically funded organisation that puts children and families at the centre. We work with the early childhood sector, government and business leaders to ensure the early childhood system lives up to what children and families want from it.

Our vision is of an early childhood system that delivers quality and access for families and supports children's agency and voice, early development, and future outcomes.

We believe in matching the quality of our nation's early childhood system with the high expectations we hold for all children.

We want all families to have the opportunity to thrive, regardless of the challenges they face.

The Front Project works systematically to develop evidence-based, meaningful, and pragmatic policy solutions that create deep, sustained, and long-term change for greater impact.

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Summary

Every child deserves a fair go at a good start in life, no matter their postcode or their family circumstances. Young children are shaped by the environments and relationships around them. They arrive at long day care services from a variety of backgrounds, and with a variety of needs that change over time. Children may arrive needing help to develop their oral language skills or manage their feelings, or come from backgrounds where they have experienced family violence or trauma. Sometimes, the help children need can stem from unequal access to the support that helps other children thrive. Sometimes, the help children need is part of normal variation in developmental progress. Evidence tells us that when children arrive at early learning requiring additional help, they benefit greatly when it is provided.

For many children who may benefit from additional support, a long day care service is their first step into an intentional teaching and learning environment, but it is not the last. In schools and universities, dedicated funding is embedded in the systems, providing additional support allocated on the basis of need. This funding provides children with extra help, so they are more likely to have the same opportunity as their peers to thrive.

Key points

- Needs-based funding exists in many other education systems in Australia and overseas, but is a gap in the current long day care funding system.
- Providing targeted funding based on need could better support children and families, improve quality, relieve pressure on the educator workforce, and help better manage the system.
- It could help address current challenges in the system, including that services in disadvantaged communities are generally less well-resourced and lower quality than more advantaged areas.
- There are some important design choices for government – such as how need is measured, how funding is allocated, and how services are supported to use it. But the lessons from other systems show that there are multiple good ways to answer these questions, and that needs-based funding can be successfully implemented in Australia's long day care system.

This is known as needs-based funding, and is now an accepted, permanent part of the school education system in Australia. It is also a part of the university system in Australia, a part of many states' preschool systems, and a part of the ECEC systems in many other countries such as England and Aotearoa New Zealand. Its purpose is to provide for equality of opportunity for all children, by enriching the experience of those children who experience forms of disadvantage.

But long day care services in Australia do not receive this kind of needs-based funding.

The purpose of this report is to consider how a needs-based funding system could be designed to achieve better and more equitable outcomes for children, by directing additional support and resources to long day care services.

The report considers the challenges in the current system that a needs-based funding system could address, and how needs-based funding could work either alongside existing parts of the system, such as the Inclusion Support Program and the Child Care Subsidy, or form part of a different future funding system. It outlines the benefits a needs-based funding system could have to children's outcomes, and improving the ECEC system more broadly, including to support quality improvement and the workforce.

> "Targeted investment in disadvantaged students is the most cost-efficient way to improve the overall equity of educational outcomes being achieved
>
> *David Gonski AC and other authors in their Review of School Funding*[1]

The report then considers how a needs-based funding system could work – how services could use the additional funding and supports, different ways to measure need and allocate funding to address it, and the 'last mile' system of supports, resources and rules needed to maximise the impact of needs-based funding.

The power of properly-resourced, high quality ECEC to counteract disadvantage is well documented in Australian and worldwide evidence, but the Australian long day care system does not take advantage of this opportunity in its system and funding design. Unlike in other systems such as schools, almost all funding in the long day care system is linked to parent fees, so services' funding is determined by the ability and willingness of parents to pay fees, not by the needs of the children attending the service. This means, perversely, that better-off children typically attend better-funded and higher quality services, while children from disadvantaged backgrounds typically attend services that are of lower quality and not as well-resourced to help them. This is not the way an education and care system should work. Australia is missing an opportunity to act early and help children get the best start in life.

In 2024, nearly one in four Australian children (23.5 per cent) arrived at school developmentally vulnerable on at least one domain, and one in eight (12.5 per cent) were developmentally vulnerable on two or more domains. Rates were higher for First Nations children and children in socioeconomically disadvantaged areas. However, developmental vulnerability and disadvantage can be found across all communities in Australia - it is not isolated to a few communities or services. Even in the top 20 per cent most advantaged areas, nearly one in six children (16.2 per cent) were developmentally vulnerable on at least one domain. Since data collection began in 2009, most of these developmental vulnerability results have not improved, and many measures have gotten worse.[2] Consultations held in preparing this report indicate that children's level of need and complexity in long day care services is only increasing.

Recent reforms and government investment have focussed on other important areas, including improving access and affordability, for example through increasing the Child

Care Subsidy rates, relaxing the activity test and investing in new services. But it is the experience of children when they are attending a service that is most important in improving their outcomes.

Introducing needs-based funding in Australian long day care services could be the next significant early childhood reform. It is a missing piece that could both complement and enhance reforms already underway, and was a key recommendation of the recent Productivity Commission inquiry into the ECEC system.

If done well, a range of benefits could be delivered, including higher quality across the system, workforce retention improvements, and a more sophisticated, stewarded early childhood system, giving governments better management of the system to deliver the outcomes the community expects. It would mean the children and families who need it most would be better supported, and children would have a fairer chance at successful lifelong learning.

There are a range of different, effective uses for needs-based funding, depending on the level of funding, the nature of the need of the children, and the existing capability of the staff. By better resourcing and supporting services, they would be better able to invest in things like capability building, specialist resources and staff, additional staff, and family engagement and service integration. By intervening early with children and families, the need for expensive, later in life interventions in schools and other services can be reduced.

The experience from other systems demonstrates that needs-based funding can be successfully implemented, and there are many good options available to choose from. Every system is different, but lessons from existing needs-based funding systems provide valuable insights for the design and implementation of a needs-based funding system for long day care services in Australia – how to best set it up to realise the potential benefits, and avoid the key risks in the context of the Australian long day care system. This report draws on these lessons, research and other consultation to outline how such a system could operate.

The most important of the lessons to be learnt is that simply providing more money is not sufficient to do the things needed to improve children's outcomes; there needs to be a thoughtfully designed system of supports, accountability, and learning and evaluation to ensure additional resources reach the children and services intended, in the ways intended, to drive the system change needed.

In considering the detailed design of a needs-based funding system, this report outlines the three key design questions:

1. **How can need be measured?**

   A needs-based funding system requires a way to measure need, to form the basis of allocating funding. There are a range of different ways to measure need, including with child, family or community data, or a combination of measures considered at a service-level.

2. **How can funding be allocated according to need?**

   This includes how a fixed funding amount could be allocated with different emphases on spread and concentration, and whether to set minimum and maximum per service amounts.

3. **What is the 'last mile' of supports, rules and accountability mechanisms needed to ensure funding allocated to services is used effectively to improve children's outcomes?**

   This could include a planning and acquittal system for services, as well as direct support and a menu of evidence-based interventions to help them know how best to use the funds.

For each of these questions, the report outlines different options and analyses their different implications and trade-offs. As this report outlines, there are a number of different ways a needs-based funding system could be established. For example, it could:

- be added to the current funding system alongside existing funding streams like the Inclusion Support Program and Child Care Subsidy, or embedded in a new funding system.
- be demand-driven, or with a fixed annual funding allocation distributed proportionately according to need.
- be delivered to every service, or be more targeted.
- be managed by the Commonwealth, states and territories, sector bodies or a combination of these groups.

These questions and options are outlined to provide a roadmap for government to develop a needs-based funding approach for Australia's long day care system.

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About this report

Work on this report commenced in April 2026. It originally considered 'equity loadings', but it has become clear that the term 'needs-based funding' is better understood in Australia, while the term 'equity' often means different things to different people or in different contexts.

As part of the development of this report, existing evidence and research was reviewed, including looking at needs-based funding approaches in other jurisdictions and systems. Consultations were held with sector leaders and peak bodies, academic experts, educators and service leaders, national, state and territory government officials, thought leaders, and experts in other systems. This included people with diverse experience and perspectives from across Australia, including in regional and remote communities, First Nations communities, and disadvantaged communities. In order to encourage candour, all consultations occurred on a 'Chatham House' basis, so individuals are not named and their comments are not attributed. The time and thoughtfulness of those who shared their experience and wisdom is greatly appreciated.

In addition to this report, a more detailed technical report has been produced and shared with project sponsors and the Commonwealth Department of Education. Work is also being undertaken by the e61 Institute to analyse newly available data about the incidence and distribution of need in long day care services in Australia to further inform understanding of needs-based funding. This will be released at a later date.

Why should needs-based funding be introduced to long day care services?

Needs-based funding is what it says it is - a dedicated stream of funding targeted to need. In the context of long day care services, it recognises that while there are some core costs of delivery that will apply in every service – for example, educator and teacher wages to meet National Quality Standard requirements, rent, or food – some costs will vary depending on the needs of the children in any individual service. While significant investment is made to help children participate in early childhood education and care (ECEC) by helping with the cost of access (most notably, the Child Care Subsidy and Additional Child Care Subsidy), it is just as important that the education and care they receive while attending is high quality and able to meet their needs.

Some children need more help to thrive – for example, because they haven't yet had the same access to support as other children, experienced challenges such as family violence, or grew up in a home where English was not the main language spoken. The extra help these children need often takes the form of more people (for example, an additional educator or a speech therapist), or better equipping people to meet their needs (for example, specific training). This comes at additional cost.

Key Points

- Some children in long day care services need more help than others to thrive.
- But the current system largely allocates funding according to parent fees, not need.
- A needs-based funding approach would address this, better resourcing services where there is greater need.
- Needs-based funding approaches in other systems and jurisdictions provide important lessons to inform design.

The purpose of a needs-based funding system is to provide funding to enrich the learning experience and provide more support for children whose circumstances mean they need it most.

This approach is well accepted and understood around the world, and needs-based funding is a common part of education systems. In Australia, there is needs-based funding in schools, and the Government has introduced needs-based funding in universities.

However, the long day care system is not currently adequately meeting these children's needs. The most recent Australian Early Development Census (AEDC) in 2024 showed a significant increase in developmental vulnerability across all domains assessed - children's physical health and wellbeing; social competence; language and cognitive skills; emotional maturity; and communication skills and general knowledge.[3] Services and staff

consistently report an increase in the prevalence and complexity of need and children displaying challenging behaviours, leading to the workforce feeling stretched and stressed. While there are specific funding streams and programs for the small proportion of children with intensive needs (such as the Inclusion Support Program), and a new program being introduced for children with developmental delay and autism (Thriving Kids), there is no funding stream or program focused on children with other additional needs or at risk of developmental vulnerability.

The current system

Perversely, the current system in many ways is the opposite of needs-based funding – the amount of money a long day care service can spend is based on how much it can raise in fees from families. Historically, many considered the purpose of government's support for ECEC to primarily be about supporting parental workforce participation. While this remains one purpose, there is growing acceptance that ECEC should also provide a high quality and enriching age-appropriate education experience for young children. However, some policy and funding settings have not been recalibrated to support this.

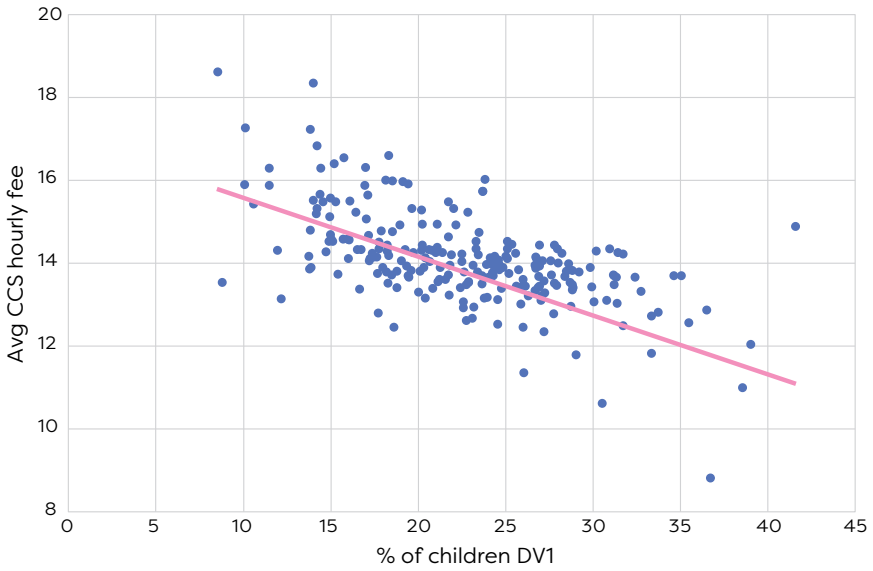
> **Governments do not have to choose between a universal or targeted approach. The best approach is one where every child receives a baseline level of quality early childhood education, and disadvantaged and vulnerable children and their families receive additional support. This is consistent with the concept of needs-based funding in schools – some children require more resources and support to achieve the desired outcome.**
>
> *Susan Pascoe AM and Professor Deborah Brennan in Lifting Our Game*[4]

Despite the means-tested Child Care Subsidy, families who are able and willing to pay higher fees (and who are generally more advantaged) have children at better resourced and higher quality services, while children in less-advantaged families go to lower quality services. In this way, rather than counteract disadvantage, the ECEC system can compound it.

These challenges are shown in the two graphs below.

Figure 1 shows the correlation between average long day care fees and AEDC results in individual communities. It shows areas with higher average fees generally also have better AEDC results, with a lower proportion of developmentally vulnerable children. There are multiple factors contributing to this, including that costs are higher in some areas. But it is consistent with more children likely to be developmentally vulnerable attending services with fewer resources to help them, while children less likely to be developmentally vulnerable attend better resourced services.

Figure 1: **Average hourly fees and proportion of children developmentally vulnerable on one or more domain, by SA3 (Victoria, New South Wales and Queensland)[5]**



The correlation between disadvantage and resourcing can also be seen in service quality data. Figure 2 shows that services in advantaged areas are more likely to Exceed the National Quality Standard (NQS), and are less likely to be Working Towards the NQS (i.e. not meeting it). In disadvantaged areas, the opposite is true – services are more likely to be Working Towards the NQS, and less likely to Exceed it. Average quality follows a clear social gradient. This is important because we know that Exceeding the NQS is the level that maximises the impact of ECEC on improving developmental outcomes for children.[6]

Figure 2: **Proportion of long day care places rated Exceeding or Working Towards the National Quality Standard, by SEIFA decile[7]**



Precedents for a needs-based funding system for long day care services

Needs-based funding already exists in some early childhood systems. Victoria (School Readiness Funding), Queensland (Kindy Uplift) and South Australia (Preschool Boost) have all added needs-based funding to their preschool system in recent years. Other countries also have needs-based funding in their early childhood systems, including Aotearoa New Zealand (Equity Funding) and England (Early Years Pupil Premium).[8] This report is informed by the experience of governments and services in these jurisdictions. Further detail on how the state systems work is in the Appendix.

These examples provide valuable evidence to demonstrate that such a system can be designed and delivered in Australian long day care services.[a] And while these are in their early stages of implementation, there are positive signs of their impact. For example, in Victoria, early analysis of reading results for Prep children who attended a preschool receiving School Readiness Funding showed they were 1.4 times more likely to achieve at or above the expected level than the cohort of children who attended the same preschool before School Readiness Funding. More than 75 per cent of preschools reported that it had led to an improved capacity for services and staff to respond to the needs of children, and a majority of preschool teachers reported it helped them identify, assess and respond to child vulnerability, and to tailor supports to the needs of children and families.[9]

> Nationally, there are growing calls for a needs-based funding model that recognises the need for higher levels of funding in areas of disadvantage. … Needs-based funding supports inclusion through funding interventions such as lower ratios, increased planning, professional learning and connection to other services, as well as outreach and engagement… Rather than relying on funding applications for individual children (as per the current Inclusion Support Program), needs-based funding would provide services with resourcing on the basis of what is required to make a difference in outcomes for the children they serve.
>
> *The Hon. Julia Gillard AC in the Final Report of the South Australian Royal Commission into Early Childhood Education and Care*[10]

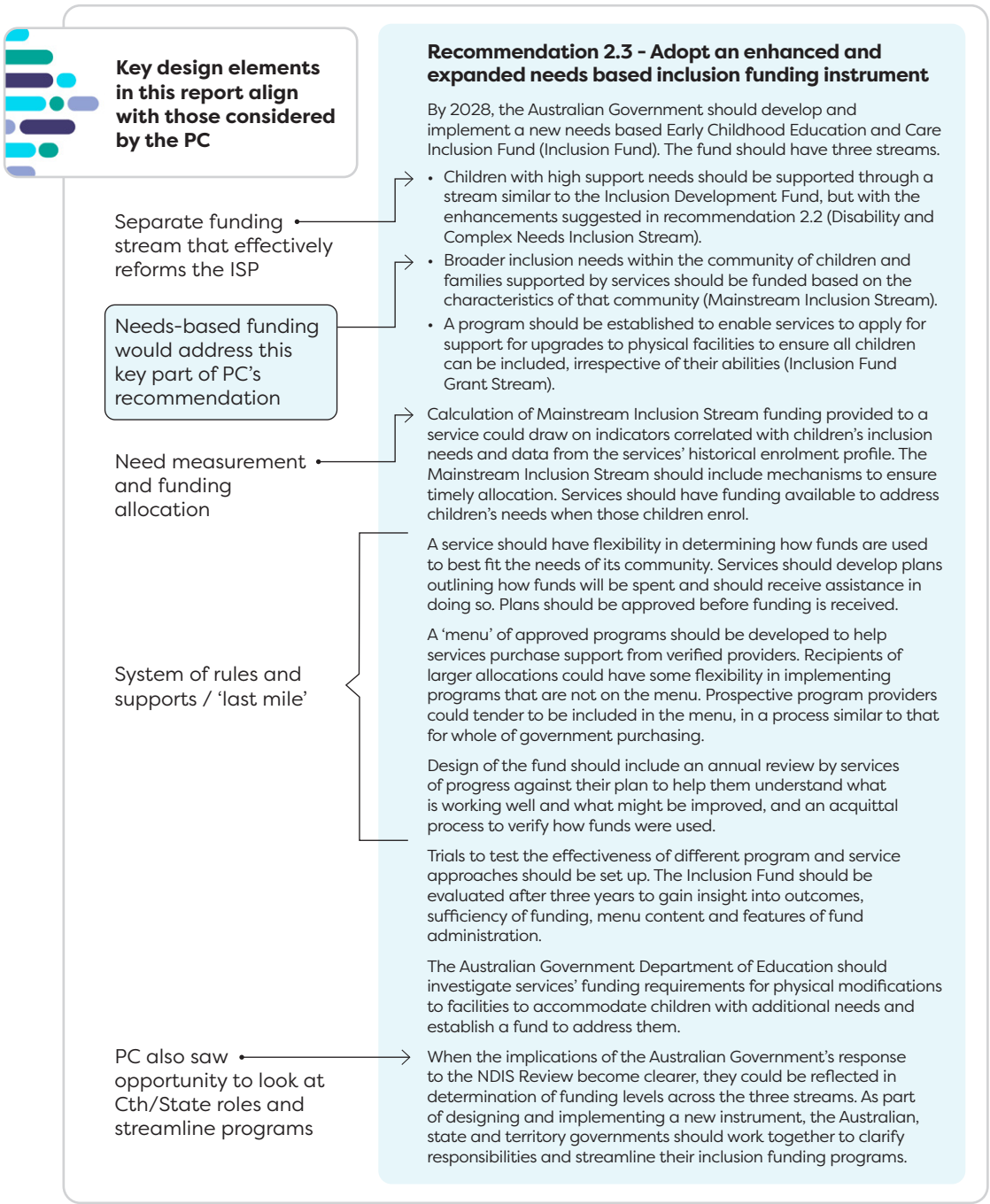
These other systems also provide important lessons for the design of a needs-based funding system. A clear one is that government cannot just add money to the system and expect the impact to simply follow – the right supports and guidance need to be provided too. When the NSW Centre for Education Statistics and Evaluation looked at the initial impact of needs-based funding reform in NSW government schools, it found student outcomes had not improved, and school staff wanted more guidance to help them make evidence-based decisions.[11] The system has since adapted to incorporate this lesson. In Victoria, when the Schools Mental Health Fund was established in response to the recommendations of the Royal Commission into Mental Health, it also provided a menu of evidence-based programs and initiatives that schools had to use their funding on.[12]

[a] Each of School Readiness Funding, Kindy Uplift and Preschool Boost operate in both standalone preschools and long day care services that offer a preschool program. However, they cover only children at a long day care service enrolled in a preschool program, and not all children, all their time in a service, or all long day care services. The needs-based funding system considered in this report would operate alongside these preschool systems, not replace them.

In England, when the Pupil Premium was introduced, the government also established the Education Endowment Fund to provide evidence-based advice on what interventions had strong evidence of impact.[13]

The idea of needs-based funding in Australian long day care services is not new. Many have suggested it over the years,[14] and what is proposed in this report is similar to the Mainstream Inclusion Stream part of the ECEC Inclusion Fund that the Productivity Commission recommended in 2024.[15] Figure 3 shows how this report's considerations align with the Productivity Commission's recommendation, including how need could be measured; funding controls and supports (including a "menu"); and the opportunity to look at how the role of Commonwealth, state and territory governments could be clarified and funding arrangements streamlined.

Figure 3: Alignment between the Productivity Commission's (PC's) 2024 recommendation and this report



Insights from consultations

Input from the consultations has informed all aspects of this report. Some key, overarching themes stood out:

- **Children, and long day care services and staff, need more help.**

  The number of children and families arriving with more and more complex needs is increasing. The sector and its staff want to help, but lack the resources to do so consistently. This is not the only challenge facing the ECEC system, but it is a big one, and it is having an impact across the system – on children's outcomes, on staff retention, and on the ability of the system overall to meet the community's expectations of it. The funding system has not kept up with changing needs and rising costs.

- **Need looks different in different communities, and even in different services within the same community.**

  Services can often serve a particular part of the community, and the communities' needs may differ – need will look different in a service in an area with lower incomes and higher rates of family violence, compared to a service in an area with a larger number of recent migrants where English is less likely to be spoken at home. Common conceptions about need can be wrong – there can be pockets of significant disadvantage even in very affluent areas, and in many areas there can be a significant difference in need even between nearby services.[b]

- **Needs-based funding would make a real difference.**

  Targeted, additional funding would be welcomed by the sector, and people with experience in other systems with needs-based funding talked about the difference it can make to the system, and the children and families in it.

- **It is not enough to simply put more money into the system, how it is used is vitally important.**

  In addition to appropriate funding rules and accountability, many services and educators will need support and guidance to make the most of any additional funding, and it will take time for all parts of the system to adjust to a new approach. These are important lessons learned from other needs-based funding systems.

[b] This can happen for several reasons, including families usually choosing to use a service close to home, services seeking to attract particular parts of the community (similar to many non-government schools), services developing a reputation for being highly inclusive of particular communities and attracting more families as a result, and because some services may operate soft exclusion policies that direct some families to other services or implement different approaches to pricing. Some of this stratification can be seen in existing data – for example, only about half of long day care services are assisted by the Inclusion Support Program's additional educator subsidy or innovative solutions program. (see: Correspondence between Senator Hodgins-May and Secretary, Department of Education regarding Budget Estimates, (29 May 2026)).

What could be the benefits of needs-based funding?

A needs-based funding system, if it is well-designed, could help the ECEC system in Australia in several ways.

Child outcomes

Most importantly, needs-based funding can better target funding to need, directing more money to things that will make the greatest impact on children's outcomes, giving children the same opportunity as their peers to thrive. The ability for ECEC to help counteract disadvantage and intervene early in children's lives is well understood. In addition to the work of services and educators, ECEC allows an opportunity for greater integration and connection with other services and systems. Intervening early is better for children and their families, as it makes their lives better, sooner, and can lead to better long-term outcomes across a range of areas. It is also better for governments and the broader community, as early intervention reduces the need for more costly, later interventions, relieving some of the cost and burden currently falling on schools and other service systems.[16]

Quality

Quality is vitally important for a child to benefit from attending a long day care service. A needs-based funding system can also contribute to broader quality improvement in the ECEC system, helping all children. The program can have a strong focus on capability uplift and support, and much of the improvement should be retained in the sector (for example, as an individual educator's capacity improves, or as service leaders learn to better understand and respond to the needs of the children).

Additional resources can also improve quality by enabling partnerships with health, allied health, family support and community organisations. These connections deepen educators' understanding of children's circumstances, support more responsive teaching, and strengthen the ability of services to respond early.

Workforce support and retention

Needs-based funding can help address workforce wellbeing and retention. A key driver of workforce frustration and burnout is supporting an increasing number of children and families without adequate resourcing. Needs-based funding could help address this by better supporting and equipping staff to work with more complex groups of children and families. Improved workforce retention also contributes to building and sustaining a safe and higher-quality system for children.

System-building

Needs-based funding can also be implemented in a way that would contribute to the building of a better ECEC system in Australia.

It is regularly observed that the ECEC system in Australia is fragmented and complex, including concerns about government funding not achieving desired outcomes, and different levels of government with overlapping roles in some places and gaps left in other places.[17] A needs-based funding system can help resolve these issues.

A needs-based funding system provides a template for how a more sophisticated funding system can work, including increasing accountability on providers for the effectiveness of how they use funding, and sending a strong signal about government's expectations about how funding is used. It can also build a deeper relationship between government and services by having staff work directly with services, increasing governments' understanding of the system, of individual providers' capability, and of children's needs.

The system described in this report also provides a template for future system improvements to improve integration and reduce duplication. For example, state and territory governments could support and oversee services in a planning and acquittal process for needs-based funding. In states where preschool needs-based funding systems also operate in some long day care services, those planning and acquittal processes could be combined into one process, effectively pooling the funding for greater impact. This could then be a model for better integrating or coordinating other funding streams, such as different inclusion supports. While this would take work and some time, it provides a path forward to resolve some long-standing challenges in the system such as overlapping roles and funding streams, and the administrative burden involved for families and services.

Needs-based funding could also be introduced as part of broader reforms that move towards a more sophisticated Multi Tiered System of Supports (MTSS). An MTSS approach typically involves three tiers of coordinated supports of increasing intensity – universal, evidence-based practices for all children; targeted supports for those with additional needs such as small groups; and intensive, highly individualised supports. Ongoing evaluation, capability building and system building is an important part of an MTSS. This is a commonly supported approach in schools and can also be applied to ECEC.[18]

What could a needs-based funding system cover?

A needs-based funding approach provides additional resources in proportion to the needs of the children enrolled at the service or in their community, to help the service better meet these needs and set all children up for success.

This report considers needs-based funding options as a new addition to, not instead of, other parts of the funding system. The report assumes that existing funding streams would continue, including those that provide funding for the core delivery of ECEC and address where cost can be a barrier to access (such as the Child Care Subsidy), help keep services viable in thin markets (such as the Community Child Care Fund), or where an individual child requires specific additional support (such as the Inclusion Support Program).[19]

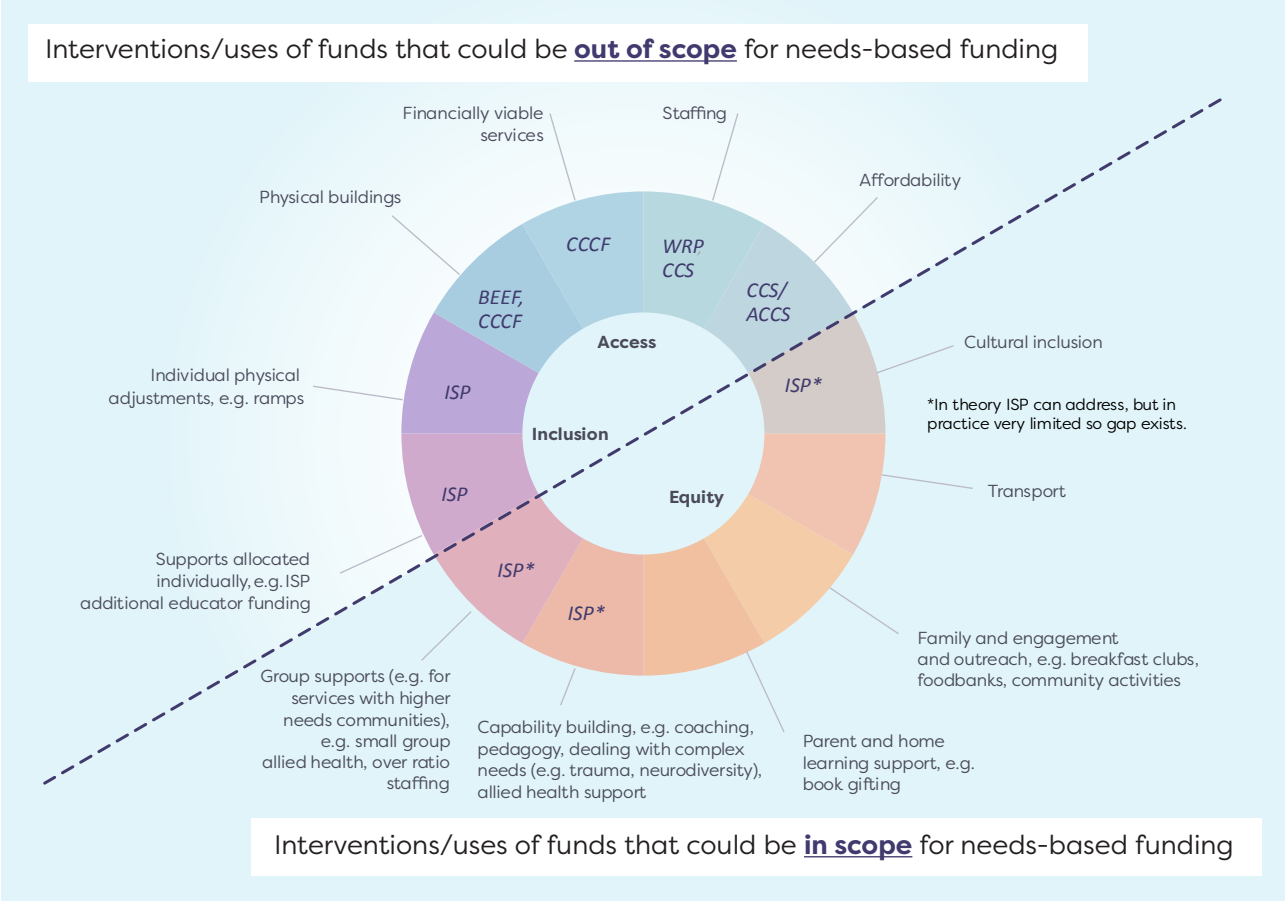
If a different funding system were introduced, some existing funding streams may change, but it is likely that some combination of different funding streams would still be needed for different purposes in any system, which a needs-based stream would operate alongside. For example, the Schooling Resource Standard has base per student funding, plus different loadings for socio-educational disadvantage, disability, and schools located in regional areas (among others). State preschool systems with needs-based funding also provide separate funding streams for individualised disability inclusion as well as core service delivery.

Key points

- Needs-based funding could be used for a range of purposes, including capability building, specialist resources and staff, additional staff, and family engagement and service integration.
- It could operate alongside existing funding streams such as the Inclusion Support Program and Child Care Subsidy, or as part of a new funding system.

One way to think about this is that different costs and needs in a system can relate to access, equity or inclusion, and that while there are several existing programs and funding streams addressing access and inclusion, as there is no instrument that addresses most equity needs. As shown in Figure 4 below, the distinction between different costs and needs can be blurry – for example, is the need for a physical ramp for a child with mobility challenges required for access or for inclusion? In practice, the classification does not matter; what matters is that there is *something* in the system that provides the ramp. The diagram offers a possible drawing of these boundaries for a needs-based funding system in the context of existing funding streams, but in any design the interaction with the other parts of the system is an important consideration.

Figure 4: Illustration of possible in and out of scope uses of needs-based funding



Note: ISP = Inclusion Support Program; CCS = Child Care Subsidy; ACCS = Additional Child Care Subsidy; CCCF = Community Child Care Fund; BEEF = Building Early Education Fund; WRP = Worker Retention Payment.

These possible uses cover a variety of contexts, including things that can help children while in a service (such as an additional educator, or capability building for an existing educator), help bring children to a service (such as transport or family engagement), or build connections between the long day care service and other services (such as allied health). This recognises that a long day care service is only one part of the service system, and that children will benefit the most when different services are supported to better integrate their work. This integration helps children to access different services as needed, and for educators to broaden or deepen their skills, better equipping them to work with children with different needs.

This report considers only long day care services. Other parts of the ECEC system, such as outside school hours care or family day care, may also benefit from some form of needs-based funding. However, the design of such a system would need to be different, and long day care is the part of the ECEC system that has the most children in it for the most time, and therefore the greatest opportunity for impact. According to Child Care Subsidy data, total long day care usage was more than three times total family day care and outside school hours care usage combined.[20]

This report also does not consider funding arrangements for Aboriginal Community Controlled Organisations (ACCOs). Significant work has been undertaken to consider appropriate funding approaches for ACCOs through the development of *Funding Model Options for ACCO Integrated Early Years Services*[21] and this does not seek to replace that.

Relationship with other ongoing reforms

At the same time as this report was being prepared, the Commonwealth Government was undertaking a Service Delivery Prices project to better understand the cost of ECEC delivery in Australia. It is not known what, if any, changes the government may make to the ECEC funding system in response. This report has therefore tried to consider how to design a needs-based funding system for different future states – to provide guidance on system design that could fit within current funding and policy settings, or inform the design of a new or different ECEC funding system.

The roll out of Thriving Kids, and associated changes to the NDIS, were also happening at the same time as this report was being prepared, and will continue for some time after its release. While there is considerable detail still to come about how Thriving Kids will work in practice, a needs-based funding system in long day care services would have a broader focus, reaching more children as it is not specifically focused on children with mild to moderate developmental delay and autism. Thriving Kids may interact with the long day care system, but how is likely to vary, and it is unclear if there will be an interface in every jurisdiction. The scale of the interaction is also unclear, and committed funding for Thriving Kids' operation in long day care services is quite modest - $139.7 million over five years to facilitate Thriving Kids services for children in ECEC.[22] This is less than a fifth of the current Inclusion Support Program spending.[23] There would be opportunities for needs-based funding and Thriving Kids to work together and complement each other as they are delivered.

How much funding should be needs-based?

There is no single answer to how much funding should be dedicated to supporting equitable access to opportunity for children. The Service Delivery Prices project is concurrently undertaking detailed analysis of current expenditure and costs, and should provide a rich source of information to inform detailed consideration.

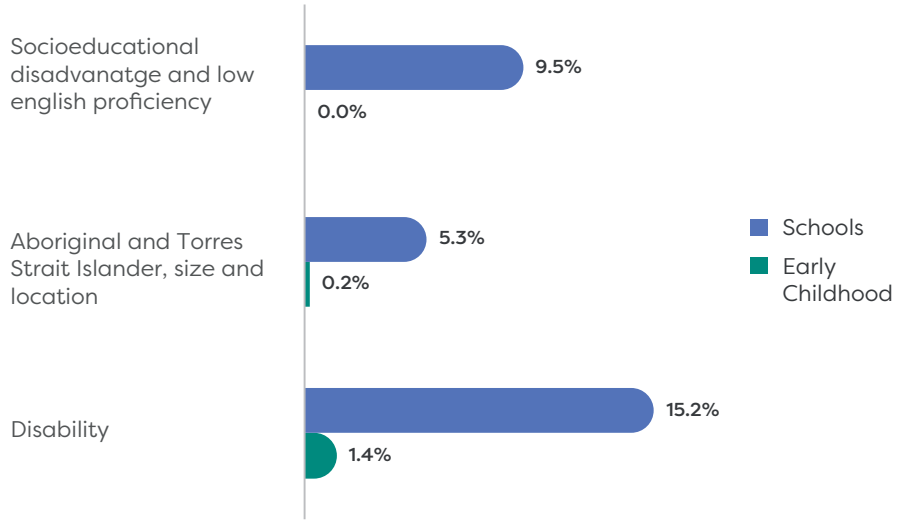
However, to understand what it could look like, it may be helpful context to consider the Schooling Resource Standard (SRS) that the Commonwealth Government uses to determine how it funds school systems in Australia, shown below in Figure 5.

Under the SRS, a large minority of the Commonwealth Government's funding (30 per cent) is used to address different forms of additional need or costs. These loadings are for socio-educational disadvantage (9.3 per cent or $3.1b, the closest analogue to ECEC needs-based funding considered in this report), low English proficiency (0.2 per cent), school location (2 per cent), Aboriginal and Torres Strait Islander students (1.9 per cent), school size (1.4 per cent), and disability (15.2 per cent, or about $5.1b).[24]

In contrast, in ECEC less than 2 per cent of overall system funding is currently allocated to these forms of need or cost, primarily disability through the Inclusion Support Program (1.4 per cent, or about $247m), and the Community Child Care Fund which supports some regional and remote services and First Nations communities (0.2 per cent).

Applying the schools comparator to long day care, 9 per cent of Commonwealth government funding would equate to over $1 billion per year. While this may sound like a lot of money, it is spread through a large system, with about 10,000 long day care services, and about 800,000 children who attend a long day care service each week.

Figure 5: Share of Commonwealth spending on schools and ECEC on additional needs or costs[25]



What kinds of things could needs-based funding be spent on?

There are a range of different, effective uses for needs-based funding, depending on the level of funding, the nature of the need of the children, and the existing capability of the staff. The list below provides some illustrative examples, but is not an exhaustive list.

Capability Building

- Training for staff to improve cultural safety of First Nations children and families.
- The cost of staff backfill so that existing staff can access additional non-contact time to attend specialised professional development. In some cases, this is as simple as increasing another staff member's hours, but in some remote communities additional staff may have to be provided with travel and accommodation.
- Training should be specific to the needs of the children, for example trauma informed practice and behaviour guidance, family support including responding to family violence and working with child protection and foster care systems, or language training for staff to build language-rich environments for children and families from non-English speaking backgrounds.
- Regular coaching from skilled educators or other professionals who can help embed practice change and promote professional reflection and development.
- A speech pathologist who spends time in a service to work with educators, to give them strategies and techniques they can use in their day-to-day work with children.

Specialist supports and resources

- Employment of local mentors for trainees in regional or remote communities, providing additional support and cultural safety.
- Small-group allied health sessions, such as an occupational therapist visiting a service once a week to work with a group of children.
- Clinical supervision with a psychologist can provide support to educators and teachers working with children with complex needs, helping them improve their practice and better manage the mental and emotional load that can lead to burnout and turnover.

Additional staff

- An additional early childhood teacher (above ratio) could provide additional pedagogical leadership and support for a service, and more direct attention for children. More intensive staffing is an evidence-based intervention for highly disadvantaged children.

Family engagement and service integration

- Programs for families to help them support their children develop a love of learning and prepare for school. A program can be delivered through home visits with families, group facilitation, individual consultation, and professional support.
- Employment of a cultural support worker to help build relationships with families and help other staff understand and create a more welcoming environment for culturally diverse families. This can include engaging local Elders, community leaders and/or community organisations to support inclusive practices such as language translation, cultural protocols training, incorporating culture into education program development and creating inclusive environments.
- Providing take home meals for children and their families, supporting nutrition and encouraging attendance and engagement, in contexts of poverty and food insecurity.
- Employment of a family support worker or 'linker' to actively engage with children and families, support enrollment and participation, connection with other services, and support educators to develop further skills in working with families and children that have complex life circumstances.
- Flexible brokerage funding to address small, practical barriers to access – for example, a family may need a car seat to transport their child, or new clothes and a backpack so they feel comfortable taking their child to a service.

How could a needs-based funding system work?

Key points

- Designing a needs-based funding system includes a range of choices around how need is measured, how funds are allocated, and how services are supported and accountable in their use of funds.
- A range of good options exist with different strengths and limitations that a government can choose between.

There is no single way to design and operate a needs-based funding system. Different options and configurations exist that can deliver significant benefit.

This section outlines the key design choices any government would face in establishing a system, and provides a framework for decisions that need to be made for any future needs-based funding system.

Design principles

Some key principles could underpin any needs-based funding system:

- **Clarity of purpose**. It should be clear what a needs-based funding system is trying to achieve - what problems or gaps in the current system it is trying to solve, and what it is not trying to do. This helps inform detailed design, including setting rules for how funding can be used, and clarifying its role in the broader funding system. This report operates on presumption that the purpose is to provide for equality of opportunity for all children, by enriching the experience of those children who experience forms of disadvantage.
- **Flexibility.** Needs vary service to service, so services should be able to use needs-based funding in different ways that respond to different local needs.
- **Additionality.** A needs-based funding system should ensure that additional funds are used to provide additional benefit. It should not be a substitute used to pay for the existing, core costs of ECEC delivery, or stop other investments in equity, capability building or quality.
- **Accountability and assurance**. Needs-based funding is taxpayer funds, and even if it were not, it would still be desirable that appropriate mechanisms are in place to ensure it is being used efficiently and effectively for its intended purpose. Services in receipt of needs-based funding, and external suppliers who may provide services funded by it, should be subject to reasonable rules and controls, but also provided guidance and supports.
- **Proportionality.** The allocation of needs-based funding should be proportionate to children's needs and what is required to meet them. The administration of the overall system, and the administrative and compliance burden placed on services and suppliers, should also be proportionate and risk-based.

- **Improvement driven**. A needs-based funding system should support ongoing improvement in the system. This includes supporting ongoing capability uplift and skill development of the workforce. In addition, the needs-based funding system should be a learning system, collecting data and improving its operation over time.
- **Sustainable and reliable.** A needs-based funding system should be sustainable for government to operate over the longer-term, and should provide services with enough certainty to be able to plan how to best use funds.

With these principles in mind, any needs-based funding system involves decisions about three key elements:

1. An approach to measuring need
2. An approach to allocating funds
3. A system of supports, rules and accountability to ensure the funding is used effectively.



1. Measuring need

In order to enrich the experience of children who experience forms of disadvantage, a needs-based funding system requires a way to identify and measure this disadvantage, to form the basis of allocating funding.

There are a range of different ways to measure need, including with a variety of child data (for example, Aboriginal and/or Torres Strait Islander children, non-English speaking background, or results of a formative assessment tool), family data (for example, parent education and occupation, or eligibility for family tax benefits), or community data (for example, the SEIFA decile of where the service is located, or the prior AEDC results of the community). Different measures may also measure different types of need – for example, some focus on economic disadvantage, while others are proxies for the quality of the home learning environment.

It is also possible to use multiple measures – for example, combining several measures to create a needs 'score' or 'index' for each service. This recognises that no single measure will be perfect, and allows for different types of need to be captured.

In considering these data options, some important considerations are:

- **Predictive power.** How accurate is the data in predicting whether the child or children will need additional help? No measure is determinative, but existing research, including to inform school funding systems[26] and recent analysis of early childhood data[27] can help understand what is and is not predictive of need.
- **Data timing.** Some data sources are only updated periodically – for example, SEIFA is updated every five years, and AEDC is collected every three years. This can provide stability to a funding system, but may also mean it is slower to detect changing circumstances.
- **Burden of collection.** Using an existing measure, or an existing system (such as the Services Australia data system) to link data sets, can reduce the administrative burden on families and services in establishing a needs-based funding system. However, collecting new data may not be a significant burden and involve only a small, one-off change (for example, to enrolment forms).
- **Precision.** Child or family measures can be more precise, as they are specific to the child and family. Community measures are not specific to the children in a service, and some

(such as SEIFA) reflect the whole population, and are not specific to children. Using only community measures also risks missing significant variation within them. For example, nearly half of all SA2 statistical areas contain smaller areas (SA1s) across 7 or more SEIFA deciles, showing even that within a single community or area, there is often a wide range of advantage and disadvantage.[28] And in consultations undertaken for the project, providers reported significant variation in need between nearby services.

Different measures will have different strengths and limitations, as outlined in Figure 6.

Figure 6: Overview of different measurement options

	Strengths	Limitations
Child or family data	• Precision - specific to children in a service. • Strong predictive power for specific measures. • May incentivise services to enrol children who would attract needs-based funding.	• May involve some additional collection burden. • Would likely need to use multiple measures to capture different forms of need.
Community data	• No collection burden on services or families. • Easy to understand. • May incentivise services to open in disadvantaged areas. • Can factor in higher costs, for example in regional and remote areas. • Can support a focus on supporting participation of children not previously attending (but funding is not contingent on it, and does not address all barriers, e.g. fees).	• Not precise, as not linked to specific children enrolled. • Service enrolments may not reflect community it operates in, and families may travel to other communities for ECEC. • Even small areas can have significant variation, so pockets of disadvantage may be missed. • Data is more likely to be lagged, so risks being out of date.
Service data or index	• Allows for mix of measures, recognising no single measure will be perfect, and allowing multiple different types of disadvantage to be captured, and capturing different benefits from different measures. • Takes comprehensive view of a service's need. • May incentivise services to open in areas, or enrol children, who would attract needs-based funding.	• May be more opaque for services or families.

The impact of concentration of disadvantage

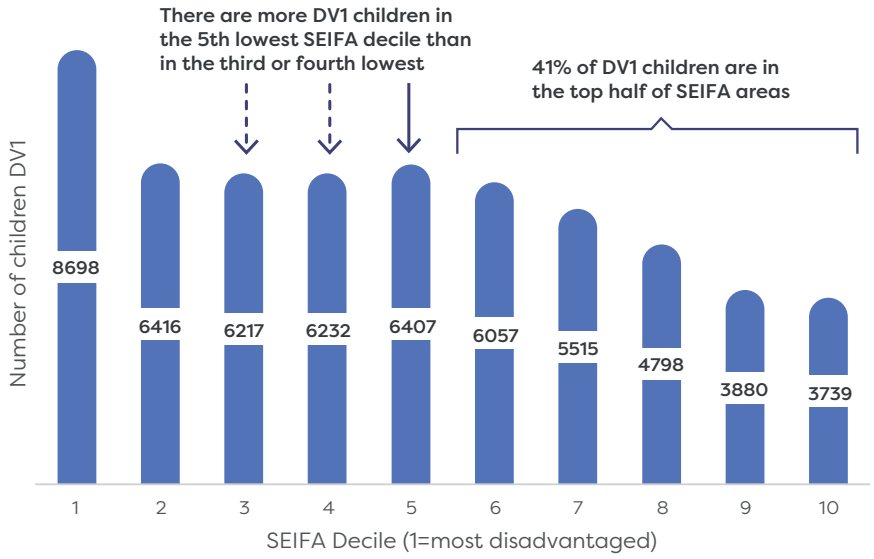
Another factor to consider (and this can be included as part of an index) is how a measure of need can reflect the cumulative impact of the level of need in a service. While one option is a simpler 'per child' funding approach, many funding systems factor in the degree to which disadvantage is concentrated in a service. This recognises that services with a higher proportion of children with needs will face disproportionately greater complexity, and that funding could increase exponentially rather than linearly to more effectively meet this need. It also recognises the increased integration and coordination effort required when services support larger concentrations of children and families experiencing vulnerability.

If the distribution of need in the system is highly stratified, as many in the sector report, the impact of the concentration of disadvantage is likely to be greater, increasing the likely benefits of factoring this into a funding approach.

Granularity and spread of disadvantage

Using an index and factoring in concentration of disadvantage also allows greater overall granularity in a needs-based funding system. This can provide greater nuance in funding allocation, and can prevent steep funding 'cliffs' where small changes in underlying data can lead to large changes in the funding allocated, or where setting thresholds can exclude a large number of children or services from the system. For example, while there is a strong socioeconomic gradient in AEDC results (where children in more disadvantaged areas are more likely to be developmentally vulnerable), there is still a broad spread of need – more than 40 per cent of *all* children developmentally vulnerable on one or more domain are in the more advantaged areas of Australia, and there are more in the fifth lowest SEIFA decile than in either the third or fourth lowest (see Figure 7 below). Focusing only on the most disadvantaged areas would mean many of these children would be missed.

Figure 7: Number of children developmentally vulnerable on one or more domain (DV1) by SEIFA decile.[29]



Averaging and forecasting

Irrespective of which measure(s) are used, some form of averaging or forecasting may be needed – for example, providing services a funding allocation for the year based on the previous year(s) enrolment. This would provide some notice and predictability for services about how much needs-based funding they have been allocated each year, and prevent significant swings in funding. Consultations highlighted that funding variability can be a real concern for services and may limit the effective use of funding. Specific mechanisms can be used for special circumstances, such as where new services open, or a service experiences a significant unexpected change in its enrolment profile.

Using averaging or forecasting could create a risk that funding does not reflect the needs of the current cohort of children in a service. However, advice from project consultations, based on provider experience and the current preschool systems, is that the level of disadvantage in a service generally does not significantly change year to year. This is likely due to several factors, including that children usually stay in the same service for several years, and services typically serve small catchment areas, so it is the same community being served year to year. Work underway by the e61 Institute may provide some empirical support for this.

Summary

Whichever measure or combination of measures is chosen will likely involve a trade-off between the factors discussed above. Any measure will be imperfect, and the aim should be to get as close as is practicable. Recognising this imperfection, it will be important that the other parts of a needs-based funding system give services enough resources, flexibility and support to make decisions about how to best use the funds to meet the specific needs of the children in their service.

2. Allocating funding

Another key step in system design is to consider how funding could be allocated and distributed through the system. Two options are considered below.

A set price, informed by the Service Delivery Prices project

One option has the Service Delivery Prices project help set 'prices' on different forms and levels of need. This can relate to both an individual child's characteristics, and the combination of children in a service. This can then be used for a demand-driven funding allocation, where funding rises and falls each year according to the level of need in the system. This is similar to the approach used in calculating the Schooling Resource Standard.

This approach may be relatively transparent and easy for services to understand, but does not provide government with cost certainty, as funding would increase or decrease as the level of need and number of children in the system changes over time. It is also technically complex to set the 'prices', as analysis may only reflect current expenditure patterns, rather than the true costs of meeting need. It would also need to be monitored and reviewed over time to ensure 'prices' set remained accurate.

A fixed annual funding allocation

An alternative approach would be to set an annual funding allocation, to be distributed proportionately according to measured need. This may be needed where calculating an exact 'price' for different needs is not possible or practical in the long day care system. It may also be preferable where government prefers to have certainty of expenditure, or to provide government with greater flexibility to change funding allocations over time as new information becomes available. It could be adjusted over time, for example to increase funding as utilisation increases (for example, more children attending long day care services, or for more days per week).

If a fixed annual allocation is used, the next design question is how the funding could be spread through the system.

There will, to some degree, be a trade-off between spreading funding across the system, and concentrating it in the highest need services. How this is resolved will depend on how the system wants services to use funding and the overall size of the funding pool. Later in this section, four different possible allocation approaches are outlined to illustrate some of these trade-offs. If the system wants services to be able to increase staffing levels and their qualifications mix to meet additional needs, they will need a larger amount of funding. This could mean greater emphasis would need to be given to the concentration of disadvantage in a service. Alternatively, if the aim is to drive practice change and quality improvement throughout the system, the funding would be spread more broadly. In practice, this can become a question of degrees and balance, not a binary choice.

Unlike in schools, where attendance is standard across the country (e.g. five days per week for forty weeks each year), utilisation of long day care varies, with some children attending a day or two each week, and some attending five. A long day care allocation approach could be based on the days or hours per week children are enrolled, rather than a simpler 'per child' basis.

Minimum and maximum funding levels for each service

A related issue to consider is whether to build in minimum and maximum funding levels for each service each year. This can help ensure that funding is deliberately spread throughout the system, that no service is provided too little or too much funding than it can usefully spend, and that unexpected anomalies in the funding formula do not lead to unintended results.

Having a system-wide minimum funding level, where every service receives a guaranteed minimum allocation, could have a number of benefits.

- It means that every service would be part of the system, and have to consider the needs of the children in the service, and how the service can better meet them. It would also support some additional capability uplift in every service, spreading the benefits broadly through the system.
- It prevents services moving in and out of the needs-based funding system from year to year, which can create additional complexity and administrative burden.
- It prevents services receiving unhelpfully small amounts of funding that provide little benefit to the service but creates an additional administrative burden.
- It recognises that need can be anywhere, and any measures used to allocate funding will be imperfect.

Likely for these reasons, Victoria, Queensland and South Australia have all instituted guaranteed minimum funding for every service participating in their preschool needs-based funding programs.

Providing a guaranteed minimum level of funding for each service can be seen to distort the integrity of a needs-based funding approach. However, noting that any measure of need is imperfect, it would be a very small part of the overall cost that could deliver significant system-building benefits. In one possible allocation approach considered for this report (see below), a guaranteed minimum $5000 of needs-based funding per service, that went to the 10 per cent *most* advantaged services in the system, would represent only 0.5 per cent of an overall $1 billion funding allocation. This could be considered a relatively small price to pay for the benefits it would be expected to deliver.

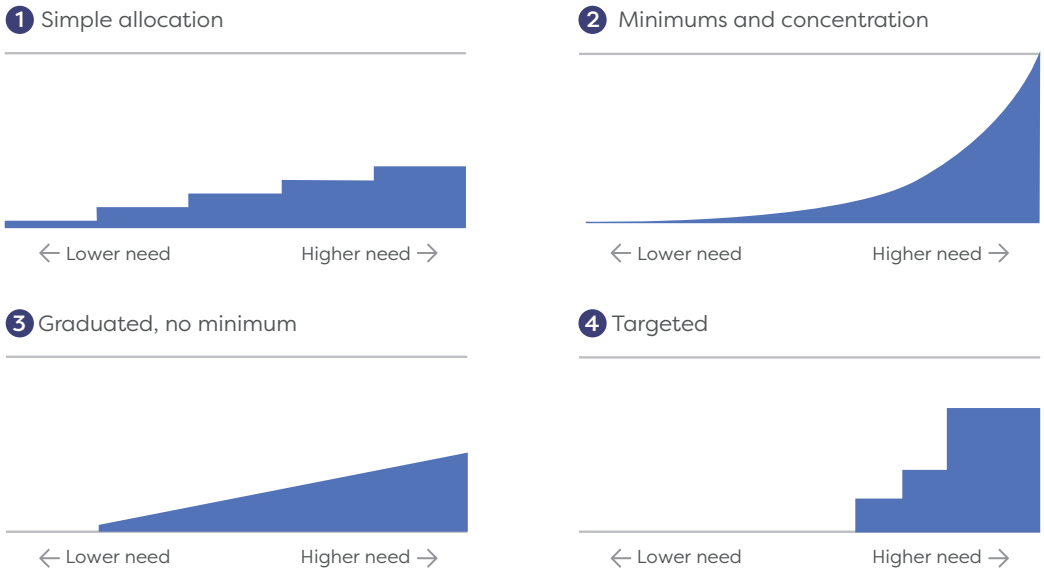
Illustrative examples – different allocation approaches

For the purposes of illustrating the implications of different approaches to allocation, four hypothetical approaches have been considered:

1. A simple allocation approach, that funds each service at a per child rate based on the SEIFA quintile of a service, with no additional funding for concentration of disadvantage.
2. A more sophisticated approach, that provides a minimum funding level for each service, with funding increases based on the level and concentration of disadvantage in a service. This could be based on child and family level measures or an index.
3. A graduated funding approach, that provides funding to most services, gradually increases funding for higher needs, but has no minimum funding guarantee. This could be based on child and family level measures or an index.
4. A targeted approach that only funds a small proportion of services with higher per-service funding levels, with some stepped funding levels. This could be based on child and family measures, community measures or an index.

For each approach, a fixed $1 billion funding allocation was simulated, showing the amount each long day care service would receive. The graphs in Figure 8 show the hypothetical funding allocation of each service, with lower need services on the left and higher needs services receiving the greater funding level on the right. Figure 9 then provides an overview of how each approach leads to different distributions of funding.[c]

Figure 8: Hypothetical allocation approaches



These approaches can provide different funding outcomes for services, and the system overall. A comparison of the different strengths and limitations of the different approaches is in Figure 10 below. In addition to the question of whether all services would receive some funding, key differences include whether there are funding 'cliffs' or gradual changes in funding levels, and how much funding the highest-funded services receive.

[c] Each of these approaches assumes a fixed $1 billion funding allocation is distributed across a system with 10,000 long day care services. To simplify the analysis, it assumes that each service has the same number of children enrolled for the same number of hours; only the need in each service varies. It does not consider cost variation, for example if costs are higher in regional and remote areas. The graphs are all drawn to the same scale to aid comparison. These hypothetical approaches have been developed for this report to illustrate the implications of different possible approaches, and do not use real data. In practice, an infinite number of permutations are possible.

Figure 9: Implications of different possible funding approaches for services

	1. Simple allocation	2. Minimums and concentration	3. Graduated, no minimum	4. Targeted
Average funding (of services receiving funding)	$100,000	$100,000	$125,000	$250,000
Services with no funding	Nil	Nil	2,000	6,000
Minimum funding per service	$20,000	$5000	Nil	Nil
Maximum funding per service	$180,000	$516,431	$230,000	$360,000
Funding distribution				
Most disadvantaged 10% of services	18%	40%	22%	36%
Most disadvantaged 20% of services	36%	65%	41%	72%
Most advantaged 20% of services	4%	1.2%	Nil	Nil
Most advantaged 10% of services	2%	0.5%	Nil	Nil

To give the individual service allocations context, the cost of some possible uses of funds has been investigated to provide illustrative examples of how a needs-based funding allocation may be used by a service.[d]

- **$2000** could fund a three-day training course for an educator on particular teaching strategies.
- **$5000** could fund cultural understanding training for a group of staff, to build confidence in engaging with First Nations families.
- **$10,000** could fund a one day, in-person workshop for seven educators to improve their support for neurodiverse children, including backfill costs.
- **$20,000** could fund two hours per week of coaching for eight educators to embed practice change and promote professional development.
- **$50,000** could fund a speech pathologist attending a service one day a week for six months, to work with educators to build capability in creating language-rich environments.
- **$100,000** could fund a part-time family support worker to engage with families and coach and mentor educators in how they work with families experiencing vulnerability; or an additional educator to provide additional pedagogical leadership and support, as well as more direct attention to children.

[d] These are illustrative examples with indicative costs drawn from public sources. A wide range of different uses of funds is possible.

At all funding levels, but particularly at higher levels, services would be expected to use their funds on a package of different uses, for example both employing additional staff and supporting the development of a range of existing staff. The typical long day care service operates 50-55 hours per week, with 17 staff supporting 84 children across multiple rooms and different days of attendance. Reaching most or all of the children requires approaches that extend across many staff members or rooms, rather than a single additional staff member or a few staff completing a training course.[30]

Figure 10: Strengths and limitations of different funding allocation approaches

Option	Strengths	Limitations / risks
1. Simple allocation	• Funding spread more evenly through system, and all services receive an allocation. • Some progressivity. • Relatively simple and easy to understand.	• Highest-need services receive less than other approaches. • Limited granularity in allocation, many services treated similarly. • Relatively large funding changes if move between tiers.
2. Minimums and concentration	• Funding spread throughout the system and relatively strongly targeted to need. • Graduated approach with no funding cliffs. • Highest need services receive substantially more funding.	• Large variation in funding allocation; funding rules need to accommodate this. • More granular funding distribution likely requires more data collection and is more opaque. • Large funding allocation to individual services can create risk, may need closer management.
3. Graduated, no minimum	• Similar to #2 (above), but with greater investment in 'middle need' services and less on higher and low need services.	• Similar to #2 (above), but some services and children miss out on funding. • Creates an 'in or out' funding cliff.
4. Targeted	• Funding is highly targeted to need. • Highest need services receive substantially more funding. • Relatively simple and easy to understand (depending on measures used).	• Most services and children miss out on funding, narrowing impact to only parts of the system. • Large funding cliffs for small changes in services' needs. • Greater delivery challenges, as need is spread across the country (but with fewer services in the system to provide scale and efficiency), and larger allocations may need closer management.

3. System of supports, rules and accountability (the 'last mile')

For a needs-based funding system in long day care services to deliver its intended benefits requires more than simply giving long day care services the funding. It must be accompanied by a system of supports, rules and accountabilities to ensure that funding is well-used. This can be considered the 'last mile' of the system – the crucial part that makes sure the funding benefits children and families.

> "While funding arrangements play a critical role in improving equity in educational outcomes, allocating the right level of resources in the right places is only part of the challenge. Of equal importance is ensuring that additional resources are used in the most educationally effective ways.
>
> *David Gonski AC and other authors in their Review of School Funding*[31]

A last mile system is needed, in part, because it is the use of taxpayer funds, and because of the nature of the long day care system in Australia, where most services are operated as for-profit businesses. But it also reflects lessons from other systems, including school funding – that you cannot just give services new money to undertake new activities and expect them to immediately know how best to use it; you need to give services guidance and practical support.

Services will need – and many will appreciate – guidance and support for the use of needs-based funding. Services will also likely learn and adapt their uses of funding over time. This has been reinforced by the experience of Victoria, Queensland and South Australia in their preschool systems, where each has established a system of supports, rules and accountability. In Victoria and South Australia, this has included government staff working directly with services. The last mile of a needs-based funding system in Australian long day care services could have three key elements.

1. There needs to be a general set of **program rules** that outlines how funds can be used (and what uses of funds are not permitted). Program rules could ensure that funding is spent on evidence-based interventions associated with the objectives of the funding, and that services are not using funds to substitute for other expenditure or other purposes. Within this, services would still have significant choice as to how funds are best spent in their local contexts, so they can tailor spending to meet the specific needs of the children in their service.
2. Requiring services to create **plans** for how they will use their needs-based funding, approved early in the year, with an **acquittal** process at the end of the year to demonstrate how funds were spent. Plans could be amended with agreement during the year, to accommodate changed circumstances. This provides both an important accountability mechanism and a process for the service to deliberately consider the needs of their children and the specific steps it can take to better meet those needs. This process could also help collect data to understand how services are using funds,

and the impact of different uses, contributing to a continuously learning system. A small part of the funding allocation could be used to cover some staff time costs for the preparation of the plans.

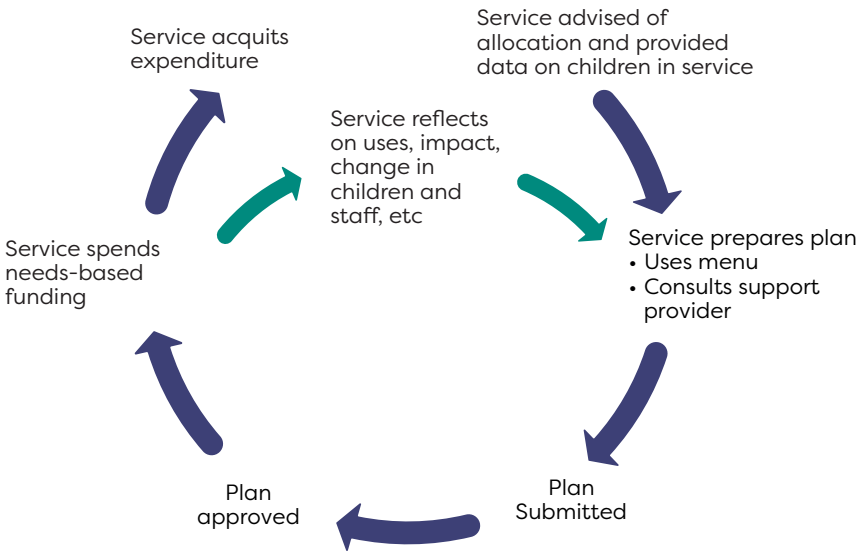
3. Services could be provided practical **support** to understand their cohorts' needs and how best to meet them. This could include:
   - **data sharing**, for example, providing tailored reports on the characteristics of the children in a service and the broader community it serves;
   - **one on one advice** with trained experts working with services to plan the best use of their funding; and
   - a pre-screened **menu of evidence-based uses of funds** that provides a list of different services and supports that can be used. Use of the menu could be compulsory (where services must spend needs-based funding only on items approved on the menu), optional (where the menu is a guide and broader program rules govern spending) or a combination (for example, where approved services can spend up to 25 per cent of the funding on off-menu items). Because some services or providers may only be available in some areas, different versions of the menu may be needed in each state and territory.

While described as discrete elements, these elements should be considered and developed together, as a coherent and mutually reinforcing system. This will both enhance the effectiveness of how needs-based funding is used by services, and provide an effective system to prevent funding being exploited.

There should be no separate application process for needs-based funding, with funding allocated automatically each year.

An overview of how an annual planning and acquittal cycle may work is in Figure 11.

Figure 11: Potential annual planning and acquittal cycle



Several additional design elements could also be considered to aid implementation of needs-based funding.

Central procurement of services

To ensure services have access to some services and achieve economies of scale, some activities or interventions could be centrally procured in bulk for the system (for example, as some allied health services are in Victoria's School Readiness Funding program). Services could then use some of their needs-based funding on these pre-purchased arrangements. This also allows government to help the supplier market - stimulating supply, imposing quality standards and building capability, for example ensuring that professionals are suitable and have relevant expertise to work with young children. Similar to the development of a menu, in many cases this may need to occur in localised ways (for example, separate arrangements made for each state and territory).

Pooling funding

While this report generally talks about funding being provided to services, in many instances it makes sense for services to be permitted to pool their needs-based funding. This could occur in several contexts:

- Within providers. Many services are owned by the same provider. It may be more efficient, for example, for a provider to hire a full-time employee to work across five services than for five services to each hire a person for one day per week.
- Geographic area. Services in an area could collaborate. This can be particularly beneficial where services are working with the same community with common challenges, or operate in regional or remote areas so travel and transport costs can be shared between providers. An example of place-based collaboration is The Hive in Mount Druitt (see case study on following page).
- Common form of need. Services dealing with a common need – for example, children from a particular cultural background, or with specific forms of neurodiversity - may not be geographically close, but could benefit from working together to collaborate on tailored capability building for educators, or to employ a bicultural worker who can work across multiple services.

The Hive case study

The Hive is a place-based, early years Collective Impact Initiative in Mt Druitt, a highly disadvantaged area of Western Sydney. The Hive was established in 2015 as an initiative of United Way Australia, to bring together residents, local services, ECEC providers and systems to collaboratively address the complex needs families and children were facing. Its early years initiatives include:

- Investing in in educator and leadership capability through coaching, mentoring, and bimonthly learning networks. This has included funding backfill so staff can participate in activities.
- 'Linkers' that work with families to navigate early education and child health services and overcome barriers. The Hive's Linkers have supported educators to understand these barriers, so educators can now help families with this too.
- Working with the local health district to embed child and family health nurses into services for developmental checks.
- Engaging occupational and speech therapists to work with educators – modelling strategies for them to use with children, helping the educators use them themselves.

The Early Childhood Educators' Network was evaluated by Western Sydney University through the period 2020-2025. The evaluation found strong evidence of impact in 12 of 15 areas examined, including centres being better equipped to support children with special educational needs, and supporting educator confidence and wellbeing. It concluded that it 'is lifting the quality of early childhood education right across one of the most disadvantaged postcodes in NSW and could be a model for consideration for similar contexts.'

A decade of quality investment work with ECEC services has resulted in significant increases in quality ratings. In 2017 only 43 per cent of services were rated as 'meeting' or 'exceeding' the National Quality Standard, in 2026 this has increased to 90 per cent. Preschool participation rates have also increased.

This work has been supported by philanthropic and some government funding, but a needs-based funding system would enable approaches like this to occur throughout the system.[32]

Pooling would be expected to have a number of benefits, including achieving economies of scale, and improved administrative efficiency for both services and government. If pooling were to be permitted, it would still require oversight, and while some flexibility could be permitted, there would still be a need for funding to be proportionately allocated according to need within the participating services. Even where pooling does not occur, some coordination could be helpful – for example, an allied health practitioner visiting a community can schedule multiple services on one visit, spreading travel costs.

Risk-based management

The oversight and operation of needs-based funding could be risk-based. Risk could be thought of in a number of ways – for example, the amount of funding a service receives, a service's compliance history, capability and willingness to engage meaningfully in the planning process, or the risk of different uses of needs-based funding. The risk of some suppliers should also be considered, as additional government investment in any system can sometimes lead to unscrupulous behaviour. Traditional assurance measures such as random and risk-based audits and cross-checking data against other sources could form part of this.

Over time, this approach can evolve into a broader, earned autonomy model, where some services are given greater flexibility on how funding is used and less intensive oversight, while others are provided more support or subjected to tighter scrutiny.

Other changes that could be considered as the system evolves is moving to longer funding cycles (for example, a two-year funding, planning and acquittal cycle rather than one year) and integrating the planning process into services' existing processes such as the Quality Improvement Plan or Strategic Inclusion Plan.

Complementary reforms

While outside the direct scope of a needs-based funding system, a number of other reforms could also be introduced to enhance the effectiveness of a needs-based funding system or support a similar cohort of children. These are:

- **Priority of access rules** to require services to enrol, or where places are limited to give priority to, children from specified disadvantaged backgrounds. These used to exist in the child care system, but were removed in 2018.
- Some children will have significantly higher needs, for reasons unrelated to factors that would come under the Inclusion Support Program (such as a diagnosed disability)– for example, parental drug or alcohol issues, family violence, housing instability, contact with child protection system or trauma. Different models of **intensive ECEC** such as Parkville Institute's Early Years Education Program have been shown to be of significant benefit for these children.[33] However, these programs are not able to be funded through Inclusion Support Program or the mainstream Child Care Subsidy system, and would still be unlikely to be in even a generous needs-based funding system. Consideration could be given to a different commissioning approach, or how it could be included in broader future funding reforms.
- The **Inclusion Support Program** requires reform and investment to ensure it is able to meet the needs of all the children who need it.[34]

- The provision of sufficient and nutritional **food** in long day care services was an issue that arose in consultations for this report. While it may not be a suitable use of needs-based funding (due to risks around additionality and substitution), it should be considered a core part of every long day care service's offering. This could be addressed through changes to the National Quality Standard, or as a condition of government funding.

Who could run the system?

Who is performing the different functions described above is an important question. The different roles could be performed by a number of different bodies.

The **Commonwealth Government** is the funder and steward of the long day care system in Australia, and would need to operate many parts of a needs-based funding system like collecting data, allocating funds, establishing IT systems, and setting overall program and spending rules. However, it may not be the natural home for many other functions – such as working one on one with services to support their planning, procuring panels of providers in each state and territory, or determining what evidence-based uses of funding are approved on the menu.

A number of other options exist:

State and territory governments. Some state and territory governments already have local teams working directly with early childhood services, including Victoria and South Australia to support their preschool needs-based funding systems. Other jurisdictions have school-based regional structures that could be built on for early childhood. Local teams can help with local knowledge, for example to apply risk-based management of the system.

Involving state and territory governments would have a number of valuable system building benefits, helping to create a 'middle layer' of the system between the Commonwealth Government and providers, allowing for better understanding and closer management of the system in the future.

It would also provide a platform for better integration between national and state-based ECEC systems and funding approaches, reducing administrative burden on services and allowing better coordination of different funding streams (including preschool needs-based funding streams), for example through combined planning and acquittal processes. This could also be a first step in untangling the complex split of roles and responsibilities of different levels of government in the broader early childhood system. It would also support greater integration between the long day care system and other early childhood services and programs operated by the states and territories, including preschool programs, family and child health services and Thriving Kids. Better connection and integration would make it easier for families to access different services, and see more children have their needs met sooner.

Existing sector bodies such as **inclusion agencies, peak bodies, or trusted providers** could also play a role in the system. This would involve expanding their current role, but could draw on existing models such as Queensland's Kindy Uplift, where some trusted providers as designated and funded to be advisory support bodies, providing support and guidance to other services. The operation of different inclusion agencies in each state and territory as part of the Inclusion Support Program also provides a model for this approach. Peak bodies, such as SNAICC or Early Childhood Australia, already perform some similar roles in parts of the system, and this could be expanded on.

Governments are currently considering the establishment of a new, national **Early Education and Care Commission**. If established, and depending on its specific role and functions, a Commission could play a role in a needs-based funding system. This could include data collection and sharing, or having a role in maintaining the menu of evidence-based uses of funds (if, for example, the Commission were to take on some of the Australian Education Research Organisation's early childhood functions).

Not every function in the system needs to be undertaken by the same body – different expertise and systems may be appropriate for different functions, for example to maintain the menu or to monitor services' financial acquittals.

The system may also be different in different states and territories. In some jurisdictions, state governments may be both well-placed and willing to perform a larger role in the system, but in some jurisdictions the history of the system will be different, so sector bodies may be better placed to perform some roles.

Learning system and evaluation

A robust monitoring and evaluation process for needs-based funding should be built in from the beginning. It could provide important feedback on how the system is being implemented and used, and to understand its impact over the longer-term. This should include establishing a clear program logic and data collection systems from the outset, and utilising and sharing data to improve the operation of the needs-based funding system over time.[35]

The system should be a learning one – able to learn quickly what is and is not working, and adapting to new information. This is likely to be particularly important in the early years, when government, services, educators and suppliers are likely to experience a learning curve in a new system and approach.

There will also be significant opportunities to link data with other systems to improve government and sector understanding of children's needs and the effectiveness of different interventions.

All these things will be made easier and more efficient if the right systems and data collection are in place from the beginning, embedded in the system. Good systems will also make the administration of the system simpler and easier for government, services, and suppliers, and help reduce implementation and integrity risks.

How might needs-based funding compare to the Schooling Resource Standard?[36]

	Schooling Resource Standard (socio-educational disadvantage loading)	Possible needs-based funding for long day care services
Place in broader funding system	One of six loadings in system, including for disability, the proportion of Aboriginal and Torres Strait Islander students, and school size and location.	Dedicated stream of funding to provide equality of opportunity for all children, by enriching the experience of children who experience some form of disadvantage.
Measurement	The loading amount is based on the percentage of students in the lowest two quartiles of socio-educational advantage, which measures the occupational and educational status of students' parents. The greater the percentage of a school's students in each of the bottom 2 quartiles, the higher the loading.	A range or combination of different child, family and community measures could be used. This could also factor in concentration of disadvantage in a service.
Allocation	A demand-driven system based on a notional 'cost'.	A demand-driven or fixed annual allocation of funding could be allocated in different ways, including minimum and maximum amounts for each service.
Supports, rules and accountability	Funding is allocated to school systems (e.g. state governments) who largely administer their own systems, or to independent schools, with some reporting requirements to the Commonwealth Government.	Services could be supported to plan and acquit funding, with rules set on permitted uses and a menu of evidence-based options provided.
Fund individual adjustments for children with a disability?	No. A separate loading for students with a disability is provided, based on individual student data.	No. The separate Inclusion Support Program would continue.

Conclusion

This report provides an overview of how needs-based funding could be introduced in the Australian long day care system.

The current long day care funding system does not direct additional resources to services according to the needs of the children they support. This is a significant gap that a needs-based funding system would fix.

The different options outlined provide a roadmap for government to make key design decisions, and include a number of ways to manage key risks, including the possibility of a fixed funding allocation to provide cost certainty, and a system of supports, rules and accountability to ensure funding is used in evidence-based ways to support children and families.

Detailed design of the system can be informed by lessons from other systems and jurisdictions, and needs-based funding can be tailored to fit in either the current system, or in an alternative, future funding system.

A needs-based funding system could deliver real benefits, improving children's learning and development, providing support to educators, and helping build a higher-quality and more responsive early childhood system.

Appendix – overview of preschool needs-based funding systems

	School Readiness Funding (Vic)	Kindy Uplift (Qld)	Preschool Boost (SA)
Commenced	2019 (25/79 LGAs); 2020 (32/79 LGAs) 2021 (statewide)	2022 (pilot) 2023 (statewide)	2026 (statewide as services begin to offer 3yo preschool, but at reduced funding)
Planning and funding cycle	Two years	One year	One year
Need measurement	'Informed by' parental occupation and education. Also understood to include First Nations.	Similar to Schools (SRS) - SEIFA Education and Occupation index (child's address), First Nations, and non-English speaking background.	Service SEIFA quintile
Allocation approach	Based on need measurement and level of need in a service (e.g. concentration of disadvantage)	Based on need measurement and level of need in a service (e.g. concentration of disadvantage)	Per child rate (by SEIFA), with loading for outer regional, remote and very remote (for 2027)
Minimum per service	$2000 (over two-year cycle)	$5395	$10,000: Major Cities, Inner Regional $20,000 Outer Regional $25,000 Remote $30,000 Very Remote (for 2027; is $7500 for all services in 2026)
Maximum per service	No maximum, some receive over $400,000 (over two-year cycle)	$100,000	$150,000 (for 2027)
Curated menu or permitted uses?	Menu and rules	Rules, no menu	Menu and rules
Provider management and support	Department of Education staff	Advisory Support bodies (e.g. C&K, Gowrie Qld)	Office for Early Childhood Development staff
Allied health approach	Services with over $10,000 (2y) have a portion of allocated to pre-purchased allied health sessions. Other services have access to an Allied Health support line. All services can use SRF to access other allied health providers.	Permitted	Permitted Menu includes specific providers.

References and notes

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[2] Australian Early Development Census *National Report 2024*. ISSN 2206-284X (Online). Socioeconomic disadvantage measured by SEIFA quintile.
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[11] Centre for Education Statistics and Evaluation (2020), *Local Schools, Local Decisions Evaluation final report*, NSW Department of Education, cese.nsw.gov.au. The analysis considered a broader reform package (not just needs-based funding), but these lessons apply to needs-based funding and similar views were expressed by other stakeholders consulted for this report.
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[16] See, for example, O'Connell, M., *The Cost of Late Intervention 2024*, The Front Project (2025).
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[22] Commonwealth of Australia, 2026-27 Budget Paper 2, page 112.
[23] In 2026-27, the Inclusion Support Program has $247 million in funding, including a $114 million additional funding top up to meet expected demand. See Department of Education, 2026-27 Budget Fact Sheet: Inclusion Support Program (12 May 2026).
[24] Department of Education, *Schooling Resource Standard* (25 August 2026) (Accessed 30 September 2026). Figures relate to 2026 school year, and only the Commonwealth Government's contribution to school funding. Because the Commonwealth is the majority funder of non-government schools and minority funder of government schools, and government schools attract a higher share of disadvantaged students, these figures likely *underestimate* the overall proportion of all public funding provided for need and cost-based loadings in schools.

[25] ECEC funding relates to all service types, not just long day care. This is an estimate based on recent and 26-27 Budget data, as exact data (e.g. relating only to long day care services) is not available for all funding streams. Schools data from Department of Education, *Schooling Resource Standard* (25 August 2026). ECEC spending includes CCS and ACCS (Child care data tables – June 2026); Worker Retention payment ($3.6bn to extend for 19 months), ISP ($247m per 26-27 Commonwealth Budget) and Community Child Care Fund ($106.9m over 3 years). It does not include parent fees or other governments' funding.

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