# Children Before Profits:

## Constraining Private Equity Profiteering to Advance Child Care as a Public Good

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# FRONT MATTER


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## ADDITIONAL INFORMATION


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# EXECUTIVE SUMMARY

**Child care is an essential building block of families' financial security, children's education and development, communities' wellbeing, and the country's economic foundations.** Yet, despite its important public benefits, child care is too often perceived and funded as though it were a private luxury—a service that people can choose to pay for if they can afford it, but that is not guaranteed to all as a basic need.

**It is time to reimagine child care in the United States so that it is recognized and supported as a public good.** Under such a vision, the U.S. child care industry and policy system should be designed to prioritize five goals: (1) universal access to care; (2) universally affordable care; (3) thriving caregivers; (4) high-quality care; and (5) diverse choice of providers for families.

**These goals do not preclude individuals or businesses from earning a profit from providing child care.** However, these profits should be understood as a means to an end—that of achieving the vision for the industry—as opposed to a policy priority unto themselves.

**Achieving this vision will require more sustained and robust public funding for the child care industry.** This money is needed to bridge the divide between the true cost of providing child care—which is largely the product of the amount of people needed to staff child care programs so that they are safe and provide ample attention to every child—and families' ability to pay for this care. In 2023, a family would have needed an annual income of at least $165,000 (among the top ten percent of incomes) in order to consider the $11,582 average national price of child care affordable (7 percent of their income) without subsidies (Child Care Aware of America 2023).

**However, the additional public funding needed to achieve the vision for child care will also attract actors, most notably private equity funds, who are more interested in extracting wealth from taxpayer dollars than in building an industry that provides quality services, creates well-paying jobs, and supports the wellbeing of families and communities across the country.**

**Private equity's history and practices in industries supported by public dollars should be a warning for the child care sector.** The well-documented experiences from the other industries that have seen significant private equity investment—such as aging and disability care, hospice care, and physicians' practices—shows that private equity-owned businesses are more likely to push down the quality of the services they provide, the wellbeing of their customers and workers, and the competitive health of local markets (Appelbaum and Batt 2020; Appelbaum, Batt, and Curchin 2023; Ballou 2023; Batt, Appelbaum, and Nguyen 2023; Gupta et al. 2021). This serves as a warning that, if they increase their presence in child care markets, private equity funds and other corporate actors will exploit every opportunity to maximize their profits, even if their own wealth comes at the expense of the other stakehold-

## BOX A: WHAT IS PRIVATE EQUITY?

**Private equity firms—like Kohlberg Kravis Roberts (KKR), Carlyle Group, Blackstone, or Bain Capital—oversee funds that receive money from institutions like pensions funds and from wealthy individuals, and whose purpose is to invest that money in ways that will maximize their returns.** They do this by using debt to acquire companies, restructuring these companies' operations to maximize the profits they generate for their owners (such as by selling off assets, raising prices, or cutting operating expenses), and selling them to the highest bidder within three to five years. This is done with little regard for the long-term health of the companies in their portfolio, let alone these companies' workers, customers, creditors, or suppliers.

**This paper uses private equity as an archetype for profit-maximizing behavior since these investors structurally face more incentives to prioritize short-term profits than any other form of corporate ownership or investment.** This implies that policies and market incentives that have been designed to guard against private equity behavior are more likely to also guard against the worst behavior of other profit-maximizing actors—and thus protect the vision for U.S. child care that centers on children and families.

ers and objectives of the industry. Investor profits taken out of the child care industry before workers are properly paid, before supply catches up to demand, or before care is universally affordable—those profits stand in direct opposition to the needs of U.S. families and communities.

**Paradoxically, the same funding that will attract greater private equity interest in the child care sector is also essential to slowing the collapse of the non-corporate providers in the industry.** Without public support, small- and medium-sized providers will continue to close due to the near-impossibility of earning enough revenue to cover the true cost of care. This will leave corporate providers with an ever growing share of the market, especially in the communities and employer-sponsored parts of the market where revenues are high enough to support profits, even as child care deserts expand in rural and lower income communities. If policymakers delay too long, they may have little choice but to depend on corporate providers to supply care for families, irrespective of whether this is truly in the best interest of families, workers, employers, and communities.

## BOX B: COMMON PRIVATE EQUITY TACTICS

- **Debt and Leveraged Buyouts.** The defining characteristic of private equity is their use of debt to acquire their portfolio companies. The most immediate consequence of private equity's use of debt is that portfolio companies—in this case child care providers—face a new operating expense in the form of loan and interest payments. These payments divert their spending away from other operational expenses, like staffing, and increase portfolio companies' risk of default and bankruptcy.

- **Roll-ups and Mergers.** In the past decade, private equity funds have been acquiring several companies in the same sector, rolling them up into larger companies or chains. These larger companies can then push out their smaller competitors, or create market dynamics that force others to also consolidate to survive.

- **Control Over Management and Operations**. Private equity funds, as the new owners of a company, can install new executives and managers who are ready to reorient the companies' operations to meet the funds' priorities. In many cases, new managers are empowered to do whatever it takes to maximize profits, even at the expense of the long-term health of the company and that of its employees, customers, and suppliers.

- **Property Sale and Leaseback.** Private equity funds can access the value of companies' real estate assets by forcing them to sell their properties and rent them back from their new owners. The portfolio company is now responsible for a new expense, this time paying for something that it used to own outright. This increases pressure on providers to take even more drastic measures to cut costs and raise revenues to make up this shortfall.

- **Vertical Portfolio Integration**. Private equity firms can require their portfolio companies to buy from each other rather than from external competitors. This allows the private equity firm to profit from its portfolio companies' expenses. This creates an anticompetitive dynamic in which independent competitors, suppliers, and customers must now compete with private equity-backed companies that have sources of guaranteed demand or underpriced supply.

- **Secondary Buyouts.** When it comes time for a private equity fund to exit its investment in a company, it can sell it to another private equity fund if they are the highest bidder. Both funds benefit from this transaction, since both are under pressure to either buy or sell assets according to the strict timetable that their investors expect. For the company, this second sale to a private equity fund starts all of these tactics all over again.

**As they develop a new strategy for child care, policymakers and advocates have the opportunity to build protections into the policy and institutional foundations of this industry to prevent profit incentives from overtaking the social priorities for families, communities, employers, and workers.** Such a strategy is particularly important for a sector like child care where many providers are private, for-profit enterprises. These enterprises, large and small, will play a key role in achieving a sector that guarantees universal access and affordability, high-quality care, fair compensation to providers, and diverse care options to families.

## THE RISK OF PRIVATE EQUITY PUTTING PROFITS BEFORE CHILDREN

**Private equity funds are already significant investors in the largest U.S. child care companies, and will likely be even more drawn to this industry if public funding increases.** Of the ten largest child care companies in the U.S., eight are currently owned by private equity investors; meanwhile, the only publicly-listed company, Bright Horizons, was private equity-owned until 2013. These ten companies serve between 10 to 12 percent of children receiving licensed care in the U.S., and the top three companies—KinderCare, Learning Care Group, and Bright Horizons—control an estimated 5 percent of the market. These three companies all directly supply child care through their own chain of programs, or through contracts with employers. Five of the other large companies are franchisors whose programs are classified as independent small businesses despite their financial ties to the larger franchise company.

**A well-funded child care industry will likely display many of the attributes of industries that have in the past attracted private equity investors and other corporate stakeholders.**

- The extreme fragmentation of child care markets creates the same opportunity for private equity investors to profit from roll-ups and other consolidation tactics (see Box B) that they have used elsewhere in the care economy.
- Child care is a service that is in high demand, and even without adequate public funding, certain families and employers are able to pay high profit-generating fees. Therefore, simply capturing this small functional segment of the child care market makes business sense.
- Corporate investors may try to buy up child care providers in anticipation of increased public spending, either from states or the federal government, that would expand the share of families that they could profitably pursue as customers. By expanding their presence in child care markets, corporate providers not only increase their opportunities to receive public funding when it materializes, but they can also argue that they represent the type of provider best suited to meeting the public's child care needs.

**Left unchecked, corporate child care risks threatening all five of the industry's vision goals** (see Table A)**.**

**Underpinning all of these risks is the concern that corporate providers could capture the industry if they are allowed to control a significant share of child care markets.** Once corporate providers become the dominant players in either local or national markets, leaving families and employers with few alternative providers to choose from, then they will have more power to lobby to structure markets around their profit goals as opposed to the priorities of all the other stakeholders who depend on the industry. Private equity will thus join child care advocates in calling for more public funding for the child care sector, as that will grow the market for their portfolio companies. However, when designing guardrails and rules for the child care markets, their interests will likely diverge from those of other stakeholders.

**The private equity policy agenda for child care is likely to focus on:**

- **Maintaining control of profitable markets.** Private equity-backed companies currently make their profits from serving higher-paying families—and especially those who receive child care benefits from their employers. These companies will resist policies that will make their activities in these markets redundant—such as a universal, publicly-funded system that caps family contributions or reduces incentives for employers to offer child care benefits. They will also try to stall the transition towards a more universal system until they can gain enough local market share to argue that they cannot be removed from the sector without causing harm to families.
- **Shaping public funding.** Corporate providers will seek to convince policymakers to distribute child care funding in

| Table A: The Risks to the Child Care Vision Goals from Private Equity in a System Without Guardrails | |
|---|---|
| **Access** | Private equity investments in child care are unlikely to significantly contribute to an expansion in supply. Corporate providers may be rapidly growing, but this is often through roll-ups and other acquisitions which simply converts existing supply into supply under their direct control. |
| | Corporate providers may also redistribute resources towards communities that can pay the full cost of care, offsetting any new centers they create in higher-paying communities and allowing closures to happen elsewhere. |
| | If private equity companies draw staff and other resources away from the providers who serve lower-paying communities, corporate providers may concentrate the net supply of child care in wealthier communities or among employer-sponsored clients. |
| **Affordability** | Corporate providers will raise tuition prices, family co-payment, and fee rates as much as they can in order to maintain their profit margins. This means that they will pass any changes in their operating expenses directly on to families and employers. |
| | If public spending increases to cover providers' operating costs, then corporate providers will lobby to raise this public payment rate as high as they can, deriving their profits from taxpayers. |
| **Provider Wellbeing** | Corporate providers may currently pay marginally higher wages than many smaller programs, but they will resist efforts to raise the minimum wages and benefits for their staff as a condition of receiving public funding. |
| | To cut their operating expenses, they will likely disproportionately rely on part-time staff employed through just-in-time or algorithmic scheduling tactics. |
| **Quality** | Corporate providers will seek to maintain outward signs of quality, especially if they focus on wealthier communities and employers as their clients. However, their emphasis on quantitative metrics of quality and profitability—such as enrollment—may lead them to disregard the important human connections that constitute good caregiving. |
| | Corporate tactics that undermine caregiving job quality will, all else being equal, directly lead to inferior quality care through higher staff turnovers and more tired and stressed caregivers. For children, this churn means constantly being introduced to new caregivers and teachers, never having the chance to form bonds of trust with caregivers, and being forced into an unpredictable environment in which learning is harder. |
| **Provider Diversity** | Corporate growth tactics that depend on acquisitions, roll-ups, or conversions of existing providers into franchisees all contribute to the corporatization and concentration of the child care industry. |
| | Revenues and profits in the industry will increasingly go to (disproportionately white and male) corporate owners and investors instead of from local (racially diverse female) entrepreneurs. |
| | By reducing families' ability to find non-corporate providers, these companies will have more freedom to use uncompetitive tactics to prevent new entrants. |

ways that allow them to use part of this money to maintain profits without having to invest in their operations or service quality. They will want to limit the guardrails placed on this funding, especially those mandating higher operating expenses (e.g. minimum wage requirements), capping their revenues (e.g. tuition caps), or restricting their profits (e.g. caps on dividend payments or stock buybacks). These companies will also lobby for higher public repayment rates, without conditions on how they are to be used, to fund their profits.

- **Keeping industry standards and regulations low.** The child care industry is currently regulated in ways that allow providers to keep their operating costs as low as possible (without endangering children) because providers lack the revenues to pay higher expenses. Private equity-backed companies will want to retain this low regulatory and enforcement environment even after public funding increases so that they can pocket this money without being required to invest in their workers, facilities, or other determiants of care qualtiy.

## A PUBLIC STRATEGY TO PUT CHILDREN BEFORE PROFITS

**It is the responsibility of policymakers to ensure that child care market incentives align with the broader child care vision. To do this, policymakers must build guardrails against profit-maximizing behaviors by large for-profit corporations that seek to exploit public funding at the expense of children, families, and workers, and they must create a system designed to advance the five vision goals.**

**First, regulators must set standard rules of the game.** The minimum standards for industry-wide business behavior must rise so that everyone who wishes to participate in child care markets is required to operate in ways that align with the child care vision. This should include:

- **Raising quality and labor standards,** including health, safety, and educational requirements; minimum wage and benefit requirements; protections of collective bargaining rights, and restrictions on how soon after acquisition a program can be re-sold.
- **Increasing mandatory disclosure requirements as part of the licensing process**. Regulators should collect and publicly disclose information about such metrics as businesses' ultimate owners, investors, debt levels, and relationships to other businesses in the child care or other related industries.
- **Providing technical support and funding to help small providers come into compliance with new operating standards**. This support can come from the Small Business Administration (SBA) and other public entities, or through support to shared-service alliances.
- **Maintaining robust enforcement systems,** including inspection systems and the ability to introduce financial penalties, or to suspend the licensing, of providers who harm children, workers, or the stability of the broader industry,
- **Empowering industry boards**—composed of diverse stakeholders including workers and their representatives, local program owners, and families—to shape the regulatory processes and hold companies and policymakers accountable to the vision for the industry.

**Second, policymakers must develop a funding strategy that ensures funding recipients behave in ways that align with the vision for the industry.** This strategy should be designed to prevent providers from collecting public money while cutting their costs or otherwise behaving in ways that undermine the child care vision priorities. Such a strategy should include:

- **Setting public payment rates high enough to cover the true cost of care.** Private providers are only able to contribute to the vision for child care if they can remain profitable as businesses. Under-funded providers have no choice but to push down their expenses, raise tuition rates, restrict their activities to the wealthiest communities, or sell out to private equity-backed companies.
- **Defining expectations of funding recipients, especially around which services and operational outcomes businesses must provide in return for public funding.** This includes their paying higher wages to their workers, recognizing their employees' collective bargaining rights and committing to union peace, maintaining predictable scheduling, and investing in their facilities and equipment.

- **Prioritizing certain providers by offering higher repayment rates or other forms of support to programs who advance the child care vision.** This includes providers who invest in raising their facilities or quality, who pay their workers higher rates, who are part of co-ops or shared-services alliances, who are worker-owned, or who serve communities facing higher barriers to accessing care.

- **Requiring disclosures from all funding recipients** about their ultimate owners, investors, debt levels, and relationships to other businesses in the child care or other related industries, tuition and co-payment rates, executive compensation rates, and their spending on programming.

- **Restricting or prohibiting antithetical behaviors** such as excessive executive compensation, high debt levels, shareholder dividends, or stock buybacks.

**Third, policymakers must build and protect fair and competitive markets.** Private equity-backed providers must not be able to accumulate excessive market power relative to their smaller non-corporate or non-profit competitors. This means that neither small programs nor families must become dependent on private equity-backed providers for their services or financing. Such measures should include:

- **Providing technical and financial support to small businesses,** ensuring that they can access financing or the benefits of economies of scale without having to sell out to a private equity-backed chain. This can be done through support to shared-services alliances, increased access to public loans and technical assistance, and robust public registries of available providers.

- **Supporting alternative buyers of small businesses,** ensuring that program owners can exit the market without having to sell their businesses to corporate chains. This support can include funding from public pension funds, SBA programs, or Community Development Finance Institutions (CDFIs), as well as public pathways to transition private programs towards worker or nonprofit ownership.

- **Ensuring robust antitrust enforcement of anticompetitive behavior**. This can limit market consolidation and disincentivize practices that make child care markets less fair to non-corporate providers. This must be supported by child care regulators trained and equipped with public information systems who can monitor the health and concentration of local child care markets.

- **Limiting public subsidies of harmful private equity tactics**, most notably by eliminating the tax preferences that incentivize private equity's use of high levels of debt.

**Finally, child care stakeholders must increase corporate accountability by building forms of countervailing power among the stakeholder who share priorities beyond profits.** If properly empowered and mobilized, stakeholders—such as workers, families, non-corporate providers, and long-term investors—can help push back against corporate efforts to put short-term profits over priorities, including child wellbeing and the growth and long-term financial stability of the sector. This requires:

- **Increasing industry transparency**, and thus allowing stakeholders to monitor corporate behavior. This can be done by increasing the disclosure requirements tied to receiving an operating license and public funding; funding and maintaining robust public registries that present key information about available providers; and strengthening whistle-blower protections for both financial and operational misbehavior.

- **Empowering child care workers** by supporting child care worker unions and collective bargaining efforts; including and compensating workers and unions on industry committees that help craft child care regulations; raising standards around workers' wages, benefits, and working conditions; and supporting workers who wish to buy out their employers.

- **Empowering families** by including family advocacy organizations in policy discussions, and compensating families on the industry committees that help craft child care regulation.

- **Empowering non-corporate providers** by including small business advocacy organizations in policy discussions; including diverse program owners on industry committees; and providing financial and technical support to small businesses as competitors to corporate providers.

- **Empowering long-term investors**, such as public pension funds, by providing them financial alternative avenues, such as CDFIs, to invest in child care without having to depend on private equity funds.

**The child care industry is struggling, but a renewed commitment from policymakers and stakeholders from across U.S. society could enable the country to build a child care system that is the envy of the world.** The U.S. has the unique opportunity to get out ahead of the private equity investors who are now entrenched in private child care markets across countries, and to craft a set of market rules and incentives that contribute to, rather than detract from, the vision of child care available to all families as a public good. Achieving this vision will require contributions from all stakeholders, including private providers and investors, and a commitment from all actors to put the wellbeing of children ahead of their individual profits.

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# INTRODUCTION

# INTRODUCTION

**Child care is an essential building block of families' financial security, children's learning and development, communities' wellbeing, and the country's economic foundations**. When families have access to affordable child care, parents are able to work, pursue educational opportunities and otherwise take care of their families. When children are in nurturing settings during the critical years of their development, they gain the tools for long-term success, in and out of school. And when a thriving child care industry supports our economy, employers are more likely to have a stable and reliable workforce that sustains broadly shared economic growth (National Women's Law Center (NWLC) 2021).

**Yet despite its important public benefits, child care is too often perceived and funded as though it were a private luxury—a service that people can choose to pay for if they can afford it, but that is not guaranteed to all as a basic need.** While education for children in grades K-12 is a right, most families are left to figure out how to care for and educate their children during their first five years of life—which are critical for brain development—with few or no public resources.

**Just as the importance of child care to families and employers is often overlooked, so is that of the people who are employed as child care providers and early educators—people who deserve respect and fair compensation for their essential work.** Over a million people in the U.S. work as child care providers, the vast majority of whom are women, and disproportionately women of color and immigrants. This does not count the time and effort that parents, relatives, and community members dedicate for free towards nurturing each new generation.

**The COVID-19 pandemic laid bare the crucial role that child care plays in our economy, as well as the precarity of the existing care patchwork glued together by stressed-out families and under-valued providers.** When parents pulled young children from group settings early in the pandemic, the child care sector began to collapse. By January 2021, the Bureau of Labor Statistics reported that one in six child care jobs had been lost since the start of the pandemic. As a result, frontline workers struggled to find and afford care, exacerbating labor shortages in key professions. Meanwhile, hundreds of thousands of women left the labor force, and families with children of all ages saw the learning loss and socio-emotional fallout of the lack of early care and education options (NWLC 2021). At the same time, many child care programs reopened long before schools did, forcing child care workers to risk their own health, even while earning poverty wages. In short, when the fragile ecosystem of child care went into free fall, the consequences for families and the economy writ large were untenable.

**The intense challenges of the pandemic catalyzed policymakers' understanding of child care as an essential public good requiring public investment, spurring political action.** Lawmakers provided unprecedented stabilization funds and increases in the Child Care and Development Block Grant as part of the 2021 American Rescue Plan (ARP) Act. That relief helped 220,000 child care programs stay open, supporting 10 million children and their families in accessing care. However, plans to enact long-term funding and create a sustainable child care system were left on the cutting room floor during the Build Back Better negotiations,[1] creating two cliffs on the ARP funding in September 2023 and September 2024.

**The end of the pandemic has exacerbated much of the instability that has plagued the sector for years.** Providers have had to reckon with higher operating costs due to the combination of higher prices for items such as food, supplies, and rent, and the need to compete for workers with other low-wage sectors where employers increased salaries in response to worker organizing and a tight labor market (NWLC 2023a). Meanwhile, families in the remote-work-hybrid world use care in more unpredictable ways, threatening providers' revenues. The expiration in the fall of 2023 of the emergency ARPA funding, which sustained providers through the pandemic, has therefore been treated as an existential threat to providers across the industry (Sun 2024). By the start of 2024, 56 percent of surveyed providers reported being under-enrolled, with 89 percent of these providers citing staffing shortages, and 77 percent citing low wages as an explanation. Under these

[1] Funding for priorities from Build Back Better other than child care passed as part of the 2021 Infrastructure Investment and Jobs Act and the 2022 Inflation Reduction Act.

conditions, 55 percent of surveyed providers reported being aware of at least one program closing in their community in the last 6 months (National Association for the Educaton of Young Children (NAEYC) 2024).

**Even though the public consensus is growing around the need to substantively increase public funding in child care, the fight over the form that this funding will take is only just beginning.** The child care sector has the advantage of being able to learn from the fate of other publicly funded sectors—such as aging and disability care, hospice care, and public housing—where well-intentioned policies intended to increase access and affordability to key services ended up creating market incentives that attracted actors to the sector who were more interested in extracting wealth from this funding than in building an industry that provides quality services, creates well-paying jobs, and supports the wellbeing of families and communities. Investor profits that are taken out of the child care industry before workers are properly paid, before supply catches up to demand, and before care is universally affordable for all who need it directly oppose the needs of families and communities across the United States.

**As they develop a new strategy for child care, policymakers and advocates have the opportunity to build protections into the policy and institutional foundations of this industry to prevent profit incentives from overtaking the social priorities of families, communities, employers, and workers.**

## THIS REPORT

**This report draws from the experiences of other industries that receive public funding to predict the ways in which profit-maximizing actors, as epitomized by private equity, might exploit and abuse this support in the child care sector. It then explores possible guardrails to prevent these outcomes and recommends policies to advance the vision of child care as a public good.**

**We chose to use private equity as our archetype for profit-maximizing behavior since these investors, at times referred to as "shareholder capitalism on steroids," structurally face more incentives to prioritize short-term profits than any other form of corporate ownership or investment.** They are also, as Brown et al. (2021) noted, "divining rods of market failure" that are often the quickest to identify and exploit opportunities to extract wealth. We thus are confident that policies and market incentives designed to guard against private equity behavior will also be strong guards against the worst behavior of other profit maximizing actors—and will thus protect the vision for child care that centers on children and families.

**We have grounded our research and analysis in a vision for the U.S. child care system that achieves five goals:** (1) universal access to care, (2) affordable care, (3) high-quality care, (4) thriving caregivers, and (5) diverse provider choice. We do not assume that these five goals are incompatible with child care providers earning profits from providing this service, but we do assume that the child care industry should focus first and foremost on securing these five goals, leaving profits (above and beyond those needed to achieve these outcomes) as incidental positive externalities. Therefore, our aim with this report is to analyze how profit-maximizing behavior interacts with these goals, and to identify which policy and stakeholder responses make it more likely that the industry succeeds in these goals, thus fulfilling its social purpose.

**Section I describes the child care industry setting.** This includes a review of the structure of the industry, and the history that has shaped this sector's policies, workforce, and business models. We next describe the primary objectives of advocate's vision for the child care system, and the ways that current markets are failing to deliver on these goals. We argue that the core problem underlying these failures is the mismatch between the cost of providing child care and families' ability to pay these rates. Although increasing public funding to this sector is necessary for enabling private child care providers to thrive and contribute to the vision, this money will also make this industry more attractive to profit-maximizing investors and companies.

**Section II reviews the business models underpinning the for-profit companies operating in the child care industry.** First, we describe the child care business model, looking at the various expenses that contribute to high child care costs, and the limitations of the three sources of revenue currently at these businesses' disposal. Next, we look at the private equity business model—which we use as an archetype for understanding profit-maximizing business behavior—and the variations that emerge when private equity investments are merged with franchising and growth equity businesses.

**Section III assesses the potential impact of the strategies corporate child care providers could use to maximize their profits in this sector**. Following the stages of the private equity business model—from their acquisition to their sale of a company—we draw on the lessons of other industries that have seen high levels of private equity investments to assess the impacts that their classic tactics could have on child care industry stakeholders. This analysis demonstrates that, left unchecked, private equity investors and other corporate providers are likely to undermine efforts to achieve the child care vision.

**Section IV presents guardrails that can align child care market incentives with the vision for the industry, protecting public funding from corporate capture.** Returning once more to the private equity business model, we discuss the policy and regulatory interventions that can be introduced at each stage of this model to reduce the risks described in Section III.

**Section V reviews the key arguments of the report, and presents the four key policy priorities for guarding the child care industry from corporate profiteering.** These are: (1) industry-wide regulatory standards that raise the bar for how all private providers must behave in child care markets; (2) conditions attached to public funding which define what public entities expect from private providers in exchange for this money; (3) technical and financial support to small businesses and non-profit providers to strengthen market competition against corporate providers; and (4) strategies to build countervailing power among the various stakeholders of the child care industry to increase private providers' accountability to the industrial vision.

### BOX 1: LANGUAGE CHOICE

**This report focuses on the market structures and incentives governing the behavior of private, for-profit child care providers.** This includes the spectrum of enterprises ranging from an individual caregiver licensed to provide child care out of her own home, to multinational chains employing tens of thousands of workers in centers around the world. By definition, all of these enterprises share a common desire to maximize "profits"—the value of what they earn in revenue in excess of what they pay in expenses to provide child care services. Discussions of private not-for-profit providers are outside the scope of this report.

**That said, in this report, we try to distinguish between businesses where "profits" are the primary income of its owner-operator and businesses where "profits" are shared as financial returns to investors.** We will therefore discuss profits-as-income in the context of caregiver "income" and "wellbeing," drawing a parallel between these owners and the staff they work alongside. In this context, making a business "profitable" entails raising revenues enough to cover the cost of care, including guaranteeing a fair income to the staff and business owners. However, when we discuss "profits," we will be exclusively referring to profits-as-financial-returns. We assume that higher investors' profits can be a bonus benefit of child care markets if all other goals are achieved, but should not be a systemic priority.

**Our goal in this report is to discuss business tactics that attempt to prioritize investor-profits ahead of other systemic priorities—businesses that can be described as "profit-maximizing."** We also use this term interchangeably with "corporate." Although we recognize that many small and medium enterprises are also technically registered as corporations, we chose to use this term based on its more vernacular meaning for ease of comprehension. These terms are intended to encompass what other authors have referred to as "investor-backed" or "financialized" business, or those that adhere to "shareholder primacy" in their governance.

**At times, we will differentiate between three different forms of "corporate" business models: private equity ownership, publicly-listed companies, and franchises.** We will discuss private equity and franchise business models in more detail throughout this report. "Publicly-listed" companies refer to those that are listed on the stock exchange and for whom profits flow to investor-shareholders—as opposed to fully "private" companies that are owned by private individuals, families, or investment funds (including private equity). We will discuss the stakeholders who contribute funding to businesses in anticipation of financial returns as "investors," differentiating between private-equity fund investors (limited partners) and publicly-listed company investors (shareholders) when relevant. "Public" providers will solely refer to those that are government owned, funded, and operated.

SECTION 1

# THE CHILD CARE INDUSTRY SETTING

# SECTION I
# THE CHILD CARE INDUSTRY SETTING

## 1. THE STATE OF PLAY IN U.S. CHILD CARE

### AN INDUSTRY OF DIVERSE WOMEN-OWNED BUSINESSES...

**Child care is an industry that is critical to the wellbeing of the U.S. economy and society, and like all sectors, displays its own unique market attributes and challenges.**

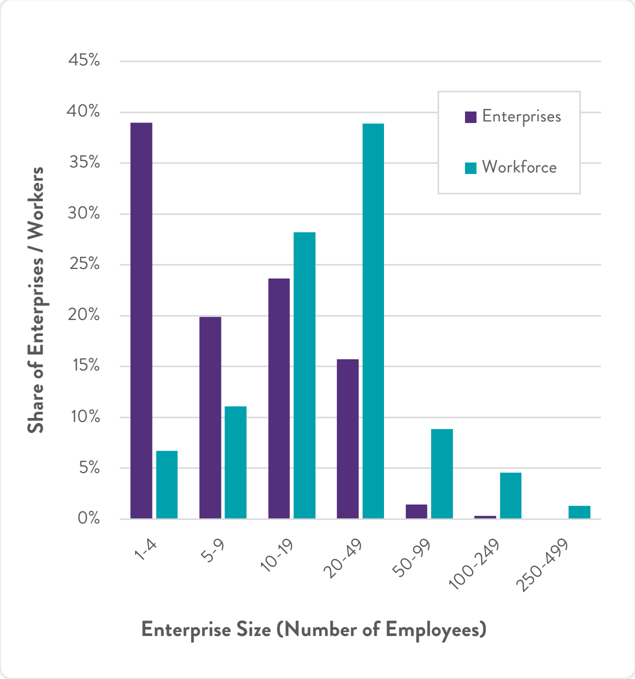
**Although parents provide the bulk of the daily care for the nearly 19 million children in the U.S. under the age of five, most families have set up a patchwork of caregiving arrangements that range from unpaid support from relatives to paid enrollment in a child care program.** Sixty percent of all children under the age of six are regularly cared for by people other than their parents (Treasury 2021).

**The child care industry that has grown to meet this demand generated an estimated $60 billion in revenue in 2019, not counting the value of the care that was provided by unpaid caregivers** (Treasury 2021). In 2019, there were 73,000 private child care enterprises around the country, more than twice the amount in 1990; this growth in the number of enterprises also created an estimated 529,000 new jobs (Herbst 2022). Meanwhile, between 2005 and 2017, the number of available spots from licensed providers grew by 7 percent, from 9.3 million to 10 million (Administration for Children and Families (ACF) 2019).

**Child care is an extremely labor-intensive industry that formally employed over 908,000 workers in 2021, the vast majority of them women, and disproportionately (relative to the rest of the labor force) women of color** (Lepage 2023).[2] Among the more tangible consequences of the longstanding social norms around the gender and racial identity of caregivers is the fact that 94 percent of child care workers are women—of whom 23 percent are Latina, 13 percent are Black, 4 percent Asian, and 24 percent are born outside the U.S. (Lepage 2023).

**Figure 1:** Share of Enterprises and Workers, by Size (2021)

*Source: U.S. Census Bureau*




**The vast majority of private child care providers are small businesses and microenterprises.** In 2021, 82 percent of child care enterprises had fewer than 20 employees, including 39 percent that had fewer than five employees (Figure 1). Larger enterprises nevertheless employ a greater share of the child care workforce, with, 52 percent of child care workers

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[2] The majority of child care workers and businesses are part of the informal economy, and states do not share a uniform set of registry or licensing requirements for these workers or enterprises. This makes it difficult to calculate the true size of the child care labor force. Lepage (2023) draws on the count of people employed in child care businesses as listed in the American Community Survey. The Committee for Economic Development (2019) also included a count of non-employer establishments (counted as creating one job each) to calculate that 1.52 million people are working in child care.

BOX 2: TYPES OF CHILD CARE PROVIDERS

### Center-Based Providers

**Child care centers are typically larger, licensed programs that serve children outside of the home, separating them according to age into different classrooms that provide age-appropriate support for their cognitive development.** They can be for-profit, nonprofit, or entirely public organizations such as public pre-schools, and range from small owner-operated enterprises to franchises in multi-national chains.

**These enterprises are fewer in number than home-based providers, but being larger, they ultimately serve the majority of children that receive care, generating most of the industry's revenue.** Among the children who regularly received care, 62 percent attend a care center, preschool, or pre-K program (Cui and Natzke 2021). In 2019, there were an estimated 121,000 center-based providers serving 9.49 million children aged five and under (Datta, Gebhardt, and Zapata-Gietl 2021). Between 2005 and 2017, 1.3 million new spots were created for children at center-based providers (up 17 percent), compensating for closures of home-based providers and driving a net 7 percent increase in spots across the entire child care industry (ACF 2019).

**These providers can be less flexible in what types of services they can provide to communities.** According to one 2012 study, about a third of child care centers only served children between the ages of three to five, with some of these restricting age requirements even further. Furthermore, 31.3 percent of centers serving children aged three to five in 2019 were open for less than 30 hours a week (Datta, Gebhardt, and Zapata-Gietl 2021).

### Home-Based Providers

**Home-based child care providers, sometimes referred to as "family child care," are typically sole proprietor, owner-operated micro-enterprises.** Among the children who regularly receive care, about 20 percent do so at a private home belonging to someone who was not a relative (Cui and Natzke 2021). About 1.7 percent of home-based providers are licensed, and provide care to an average of eight to nine children at a time (National Survey of Early Care and Education (NSECE) 2021). Other home-based providers are unlisted, like nannies, but are paid to care for an average of four or fewer children (Treasury 2021). Finally, almost 77 percent of home-based providers are both unlisted and unpaid, and include trusted caregivers such relatives or neighbors (NSECE 2021).

employed in enterprises with more than 20 employees, and 5 percent of them in enterprises with over 100 employees. These figures do not capture the prevalence of franchises in the child care industry, as franchisees would likely be listed as small, independent businesses even though they are financially and contractually tied to larger chains. Therefore, a greater share of enterprises and workers are likely tied to larger corporate business entities than these figures suggest.

**These small- and medium-size providers often are members of the same community as the families they serve.** This means that they can provide care according to the cultural, religious, accessibility, linguistic, or even scheduling preferences of families, all of which are crucial considerations for parents with children in their early years.

## ...AT THE INTERSECTION OF NORMS ON GENDER, RACE, AND CLASS

**The history of the child care industry is tied to that of women's expanding participation in the U.S. labor force—and the corresponding efforts to encourage women, and especially white mothers, to stay home.** The first formal child care programs emerged in the mid-1800s to watch the children of poor working women who, in an industrializing economy, were understood as having no choice but to find jobs (Cahan 1989). However, Progressive social reformers at the turn of the century soon encouraged a policy preference for "mother's pensions," direct payments for poor mothers that would allow them to stay out of the workforce (Cahan 1989). Women of color remained largely excluded from these payment programs, and were expected to continue working even though philanthropic support to child care had declined (Kleinberg

2006; Lombardi 2002). Public child care funding emerged during the New Deal and wartime mobilization in the 1940s when encouraging as many women as possible to work was seen as a national priority—but this funding was rapidly wound down when World War II ended and women were pushed back into the home. After women and mothers continued to enter the labor force in the 1960s, without the support of a child care system, Congress passed the 1971 Comprehensive Child Development Act (CCDA). This measure would have provided federal funding on a sliding income scale for high-quality child care programs, available to everyone, administered by the states, but President Nixon (1971) vetoed it due to its "family-weakening implications." No systematic effort to structure the child care industry has been enacted since, despite the reality that two-thirds of families rely on mothers' incomes. Much of today's public child care funding, with its emphasis on supporting child care access for families with low incomes, emerged during the welfare reform efforts of the 1990s, including the 1990 Child Care and Development Block Grant (CCDBG) Act, the 1990 Head Start Expansion and Quality Improvement Act, and 1996 Personal Responsibility and Work Opportunity Act.

**The child care industry, and especially its workforce, has been further shaped by racist norms and policies in the U.S.** Even when child care is socially relegated to the domestic sphere, wealthier women have always been able to delegate this task to domestic workers by employing nursemaids and nannies. In consequence, Black women have long supplied much of the labor of providing child care in the U.S.—first because enslaved Black women were forced to care for the children of their white owners, and after Reconstruction because Black women had access to few jobs outside of domestic work (Vogtman 2017). Furthermore, this concentration of Black women working in private households meant that, during the New Deal, policymakers who wanted to deny Black workers better jobs intentionally excluded domestic workers, including home-based child care providers, from Social Security and laws on minimum wage, overtime pay, collective bargaining and unionization, and other labor standards (Perea 2010).

**Many of the challenges facing today's child care industry stem from this sector's historic place at the intersection of social fights around gender, race, and class.** First, U.S. policymakers have rarely offered more than tepid acknowledgement of the importance of child care for working parents, let alone endorse a guarantee for universal access to care; some continue to operate under the assumption that constricting child care access will encourage women (in heterosexual, two-parent, middle-class families) to stay home, reflecting continued hostility to women's careers. Second, where direct public funding for child care does exist, it is limited to a fraction of families with low-incomes—while wealthier families receive tax incentives to pay for care themselves. This means that today's child care system is almost entirely private in terms of both supply (from private businesses, nonprofits, and individuals) and demand (from parents, families, and employers). Meanwhile, the entire system of private child care has been sustained through blatant disregard for the wellbeing of child care providers. Child care continues to be seen as unskilled "women's work," which should be done, for low wages, out of love of being with children. And many of the women who take these jobs—who continue to disproportionately be women of color and immigrant women—face discrimination and other barriers that prevent them from seeking out better paying alternatives.

**A core requirement of any future child care reform is to avoid perpetuating the inequalities and discriminatory norms born of these historic trends.**

## 2. IMAGINING A BETTER FUTURE

### THE VISION FOR CHILD CARE...

**It is time to reimagine child care in the United States so that it is recognized and supported as a public good, enabling every family to find and afford high-quality care that is supplied by a workforce that is paid fair, living wages.**

**Under such a vision, the U.S. child care industry and policy system should be designed to prioritize five goals.** These goals are highly interdependent, and it is only in working towards all of them simultaneously that families—and the economy overall—will reap the full range of benefits that can stem from child care services. These goals are:

1. **Universal Access to Care**

   **Every child—regardless of race, ethnicity, gender, disability, geography, family structure, immigration status, religion, income, or other differences—has a right to child care that meets their family's needs.** Just like with K-12 public education, eligibility should be universal, and the priority should be to reach and provide resources to children and families who have historically faced the most barriers to accessing care.

2. **Affordable Care**

   **Child care should be affordable to all families.** Ideally, child care should be free, just like K-12 public school. At a minimum, however, policy should ensure that families with low incomes pay nothing, while co-pays are capped for all families at no more than 7 percent of income for all their children—which is what the U.S. Department of Health and Human Services (HHS) considers affordable.

3. **Thriving Caregivers**

   **Child care jobs should be good jobs, and every person employed in this industry—whether in licensed or informal care settings—should be fairly compensated fairly for and supported in the essential work they do.** That means professional caregivers should be able to earn a living income—with access to benefits such as healthcare, paid leave, and retirement benefits—either as the owners or paid employees of child care providing enterprises. Ideally, this income should reach parity with that of people employed in providing kindergarten education given the comparable skills, training, and competency required to provide care and education to young children. Providers should also be able to expect predictable and flexible scheduling practices, a guaranteed right to collective bargaining, and professional support through ongoing training and career ladders.

   **Furthermore, since child care providers largely live in the communities that they serve, child care jobs and businesses should be structured and supported as mechanisms for sustaining community wealth and wellbeing.** All efforts to improve the quality of child care providers must create pathways for the full range of providers to remain included in the industry as it changes.

4. **High-Quality Care**

   **High-quality care accounts for families' and educators' diverse needs and preferences, while ensuring children are able to form a nurturing and stable relationship with their caregivers in safe and healthy settings.** Care quality is notoriously difficult to quantify in any sector, and is particularly challenging in child care given the communications skills of infant and toddler care recipients. Nevertheless, regardless of the setting, quality child care must:

   - **Support deep, trusting, and stable relationships between caregivers and children**; proxy metrics for these relationships are tied to minimizing caregiver turnover and burnout;
   - **Implement best practices for socialization and early learning** whether through a formal curriculum or community of practice;
   - **Guarantee safe and healthy environments**, as reflected in age-appropriate staff-to-child ratios, and facilities in homes, centers, or schools that meet relevant health and safety standards;
   - **Provide access to health screenings, supports and wrap-around services for children and families**.

   **Whether families select care in a center, home, school, or another setting, the quality of care will be directly related to the level of compensation and comprehensive supports for caregivers and educators.**

5. **Diverse Choice of Providers**

   **Every family should be able to find care that meets their needs and preferences.** Families should be able to mix and match different forms of care based on their needs, and should especially be able to find convenient care options that match their work schedules and cultural and linguistic preferences. This could include care provided in a center, a school, a home-based setting, or friend, family and neighbor care. While government entities can provide standardized care through public pre-K, Head Start, or Early Head Start programs, families should also have the choice of turning to local community organizations, faith-based institutions, and businesses, as well as to trusted individuals in their trusted family or community care networks.

**These goals do not preclude individuals or businesses from earning a profit from providing child care, but these profits should be understood as a means to an end—that of achieving the vision for the industry—as opposed a policy priority unto themselves.** Markets and profit incentives can be powerful tools to attract more investment, entrepreneurs, and workers into the child care industry, which could help move the U.S. child care system towards this broader vision. However, since private providers cannot profitably serve the majority of U.S. families without substantive public funding (see Section I.3 and Section II.1), policymakers will have to determine what scale of profits they, and taxpayers, should tolerate in the child care industry, and what outcomes the public should receive from private providers in exchange for this money. Profits should thus be understood as the price that the public pays private providers in exchange for their support of the child care vision—with no private provider entitled to this boon if they undermine or detract for these goals.

## ...THAT EXISTING MARKETS CANNOT DELIVER

**Unfortunately, today's child care markets are not delivering the outcomes that U.S. requires from this industry.**

**Although the supply of licensed child care was growing in the years before the pandemic, this has been insufficient to meet public demand for care.**

**Over half of people in the U.S. live in "child care deserts" where there is either no or insufficient available licensed care—with the problem particularly acute in low-income and rural communities** (Treasury 2021). Nearly 60 percent of Hispanic and Latino families live in child care deserts, as do three of five people living in rural communities (Malik et al. 2018). As a result, care is unequally distributed across communities. Only 50 percent of families with incomes below the federal poverty threshold use nonparental child care services, compared to 62 percent of families whose incomes are at or above the poverty threshold (Tekin 2021).

**A major driver of low supply is the fact that most families cannot afford to pay existing child care prices — let alone prices that would cover providers true operating costs (see Section II.1).**

**In many regions, families spend more on average on child care than they do on any other major expense, including housing or college** (Child Care Aware of America (CCAoA) 2022). Median 2018 child care costs represented between 8 to 19 percent of the median family's income (with the range reflecting the variation in incomes and prices across regions) (Landivar, Graf, and Altamirano Rayo 2023). Furthermore, many families must pay for the care of multiple children, since approximately 30 percent of children aged five and under have a sibling in the same age range (National Academy of Science, Engineering and Medicine (NASEM) 2018).

**Unfortunately, these costs fall on parents at a time in their professional lives when they are least able to pay**. By the time the median family's first child is 16 years old, they will have three times as much wealth as they did when the child was aged five and under (Treasury 2021). Banks, however, do not generally provide loans to young professionals against the promise that, if they are able to remain in the labor force, their future incomes will increase. This inherent "liquidity constraint" is a form of market failure that justifies public support to families who are struggling to pay for care.

**Child care prices are unaffordable even though child care workers' wages and benefits are exceptionally low.**

**Child care workers are paid substantially less than K-3 educators, whose salaries are covered through public investments in schools.** McLean et al. (2021) found that in 2019, the average annual salary of a six year-old's kindergarten teacher ($56,850) placed them in the 61st percentile of incomes, while that of a child care worker ($24,230) placed them in the 2nd percentile. Among workers employed in child care centers, Black women receive the lowest wages since they are the most likely to be working in the lowest-paid roles, caring for infants and toddlers. Meanwhile, the owners-operators of home-based programs often keep their fees down by not paying themselves a fixed salary; instead, their personal income is whatever is left over after all other expenses, including staff salaries, have been paid. A drop in the "profits" or operating margins of these providers therefore directly cuts into these entrepreneurs' pay, and can threaten their ability to pay rent on the homes out of which they run their business.

**These are not living wages.** In all but two states, child care workers earn less than two-thirds the median wage for single adults for all occupations in the state (McLean et al. 2021). For single adults with one child, median child care worker wages do not meet the living wage in any state (McLean et al. 2021)—even though women working in child care are more likely than those employed in other industries to have preschool-aged children of their own (Herbst 2022). As a result, many child care workers cannot afford child care for their own families, and rely disproportionately on public income support programs, such as Medicaid, SNAP, and TANF (CCAoA 2019; McLean et al. 2021).

**Stressed workers and enterprise owners are exiting this industry, eroding the relationships with children and families that constitute the core determinant of care quality.**

**Child care providers risk high turnover rates as workers look for higher paying work elsewhere.** Forty percent of centers in 2019 who did not provide benefits to their workers experienced turnover rates of over 20 percent—whereas only 29 percent of centers who provide benefits experienced the same high turnover rates (Amadon, Lin, and Padilla 2023). In particular, child care providers can find themselves competing with kindergarten and other schools for staff, especially those with training or higher education in early childhood development. Bassok et al. (2013) found that annual turnover rates between 1990 and 2010 were 25 percent—four times higher than in elementary schools. In 2019, only 34 percent of assistant teachers, and 48 percent of lead teachers had been at their program for more than three years (Herbst 2022).

## 3. THE PROBLEM OF PROFITABILITY, PROFITS, AND PROFITEERING

### LARGELY UNPROFITABLE MARKETS...

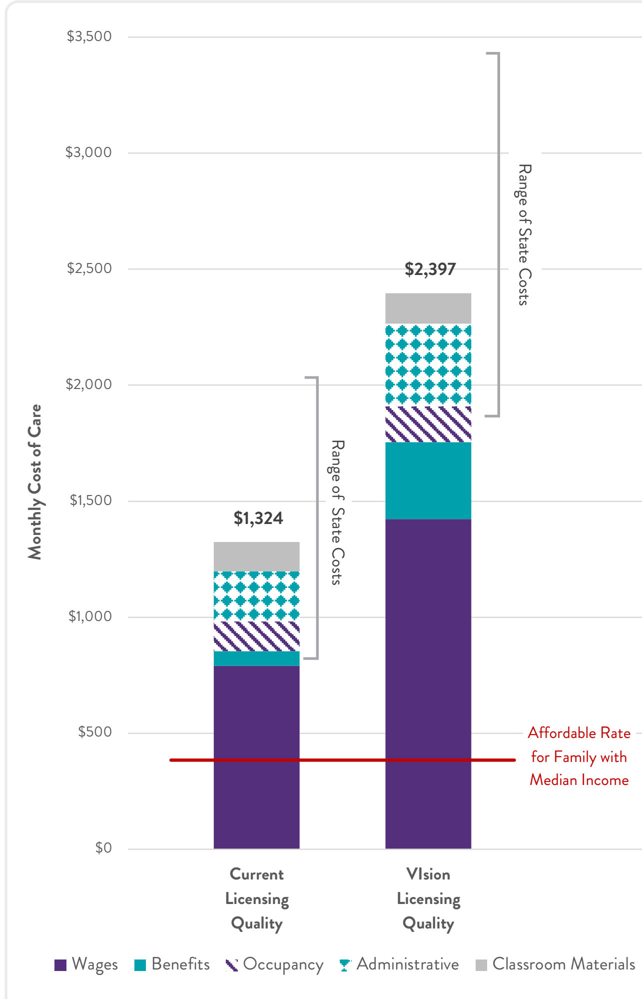
**In setting their prices, providers face a strict lower limit on how much they can charge for care if they are to remain open, and a strict upper limit on how much they can ask families to pay before it becomes so unaffordable that they forsake care entirely** (see Section II.1).

**Child care providers face a number of high, inflexible costs.** In order to create a safe and healthy environment for children, they must retain high staff-to-child ratios that raise their labor costs, invest in their staff to retain caregivers and mitigate burnout, and keep their facilities clean and safe. To meet the needs of their communities' families, they must provide care during the hours that parents are working. Attempting to cut costs in any of these areas risks the quality of the service they provide, and the loss of the workers on which they depend.

**To achieve the vision for the child care system, the cost of providing care must increase.** The most notable change will come from increased labor costs in order to allow for wages and benefits to equalize with those of K-3 educators. Providers would also need to invest in upgrading their facilities, developing a curriculum, and otherwise improving their service quality and business administration.

**Most providers are not receiving enough revenue from tuition to cover their expenses—let alone the additional cost of raising quality, wages, and income.** A family earning the median 2019 annual household income of $65,712 should only have had to pay $4,600 a year on child care if this was to be considered an "affordable" expense. Meanwhile, the average true cost of providing care to an infant in 2019 was closer to $15,900 for centers meeting existing licensing requirements, and would

**Figure 2:** Average National Monthly Cost of Center-Based Infant Care (2019)




*Source: Workman (2021), American Community Survey (ACS) (2019)*

***Note:*** *"Current Licensing Quality" scenarios assume the costs needed for centers to meet existing licensing requirements. "Vision Licensing Quality" scenarios assume fewer children per teacher, bigger classrooms, increased resources for classroom materials, and child care workers who are paid the same as kindergarten teachers, receive retirement benefits and higher contributions to health insurance, and have more time to plan lessons. More details about the methodology behind this data are described by Workman (2020), who referred to these two standards as "base-quality" and "high-quality."*

have reached as high as $28,800 if quality investments and wages had increased in line with the vision for the industry (see Figure 2) (Workman 2021). Public subsidies are limited to only a fraction of low-income families, and are still insufficient to fill this funding gap. In 2019, state subsidy levels covered only 75 percent of the true cost of meeting existing licensing requirements on average, and would only cover an average 42 percent of the costs of raising program quality (Workman 2021).

**The for-profit providers that exist in the child care industry are therefore those who manage to remain within the narrow band between these two limits.** In order to serve the families of their community, providers often set their tuition fees lower than what they need to cover their true operating expenses, and must perpetually keep wages and other expenses as low as possible in order to stay open. Most providers experience profit margins of only 1 percent of every dollar they earn in revenue (Treasury 2021). This places them in an extremely precarious position, since any sudden loss of income—such as a child getting sick for an extended period, or a parent removing their child from care because they themselves lost their job—can push their business into the red.

## ... WITH POCKETS OF HIGH PROFITS...

**Certain companies are nevertheless running profitable businesses in the child care industry, despite these systemic challenges.** These are the providers who serve families who can afford to pay tuition fees that cover the full cost of care, be it on their own or in conjunction with public subsidies or employer benefit programs (Haspel and Russo 2023).

**In particular, the largest companies in the industry have clearly identified ways to thrive in this industry.** Together, the ten largest child care companies served between 10 to 12 percent of the children receiving care in licensed settings, with the top three companies—KinderCare, Learning Care Group, and Bright Horizons—controlling an estimated 5 percent of the market (KinderCare Learning Companies 2021). In 2023 Bright Horizons, the third largest company in this industry, reported over $530 million in profits and 22 percent gross margins (Bright Horizons 2024). These margins indicate that these companies are not only earning enough in revenue to cover their operating expenses, but also enough to provide generous financial returns to their shareholders and investors.

**These ten companies are not a monolith, and use a number of distinct business models—with most of these companies combining diverse practices and revenue streams** (see Table 1)**.** The largest companies, like KinderCare, directly own and operate chains of local programs, mainly providing center-based care. Bright Horizons also operates its own chain, but places a bigger emphasis on contracting with employers than does KinderCare—although both companies operate in both community and company settings. Meanwhile, the companies outside the top three, like Goddard and Primrose, tend to be franchises—meaning that they oversee a network of providers that use their brand and management practices even while technically remaining small, independent businesses (see Section II.2).

**Perhaps the strongest indication of child care's profit potential is the interest this industry has received from private equity investors, who epitomize the type of stakeholders who have singular interest on maximizing profits** (see Section II.2)**.** Of the ten largest child care companies, eight are currently owned by private equity investors—and the only publicly-listed company, Bright Horizons, was private equity-owned until 2013.

**Corporate, and especially private equity, interest in child care is not new.** The top three companies all became dominant players in the child care industry three decades ago through private equity-backed, debt-financed acquisitions and mergers with other providers (See Annex 1). KinderCare has repeatedly received investments from, or been fully owned by, various private equity funds ever since Drexel Burnham Lambert acquired the company in 1987. Learning Care Group was one of several U.S. chains acquired in 2005 by ABC Learning, and was saved from this company's 2008 collapse when private equity investors bought out ABC's U.S. subsidiaries and rolled them up under the Learning Care Group parent company. Finally, Bright Horizons was co-founded in 1987 by a Bain & Company management consultant; Bain has since acted at various times as the company's investor, owner, and shareholder, and continues to be represented on the company's board.

### Table 1: Top-Ten Child Care Providers in the U.S.

| Company | Capacity (2017) | Ownership Type | Business Model | Private Equity Owners | |
|---|---|---|---|---|---|
| | | | | **Investor** | **Dates** |
| **KinderCare Learning Companies** | 200,000 | Private Equity | Direct Provision + Employer Contracts | Drexel Burnham Lambert | 1987-1989 |
| | | | | TCW Special Credits | 1993-1997 |
| | | | | Kohlberg Kravis Roberts | 1997-2005 |
| | | | | Knowledge Universe | 2005-2015 |
| | | | | Partners Group | 2015-present |
| **Learning Care Group**[3] | 129,828 | Private Equity | Direct Provision + Employer Contracts | Morgan Stanley Capital Partners, Barclays Investment Bank, Jacobson Partners, Corporate Partners | 2008-2013 |
| | | | | American Securities | 2013-present |
| **Bright Horizons Family Solutions** | 115,000 | Publicly Listed | Direct Provision + Employer Contracts | Bain Capital | 1986-1997[4]<br>2008-2013 |
| **Goddard Schools** | 65,000 | Private Equity | Franchise | Wind River Holdings | 2002-2022 |
| | | | | Sycamore Partners; Quad Partners | 2022-present |
| **Primrose School Franchising** | 54,240 | Private Equity | Franchise | American Capital; Heartwood Partners | 2006-2008 |
| | | | | Roark Capital | 2008-present |
| **Child Development Schools**[5] | 41,408 | Private Equity | Direct Provision | Glencoe Capital | 2006-present |
| **Kids 'R' Kids Learning Academies** | 35,775 | Private | Franchise | N/A | |
| **Spring Education Group** | 32,000 | Private Equity | Parent company of (29) direct delivery brands (child care + K-12 schools) | Warburg Pincus | 2012-2017 |
| | | | | Primavera Capital | 2017-present |
| **Learning Experience** | 31,020 | Private Equity | Franchise | Ironwood Capital; Norwest Venture Partners; Quad Partners | 2014-2018 |
| | | | | Golden Gate Capital | 2018-present |
| **Cadence Education** | 29,562 | Private Equity | Franchise | Audax Private Equity; Five Points Capital; Roynat | 2007-2016 |
| | | | | Constitution Capital Partners; Morgan Stanley Private Equity | 2016-2020 |
| | | | | Apax Partners; PFR Ventures | 2020-present |
| **Source**: Statista Research Department (2024); Pitchbook | | | | | |

3 LearningCare Group is the parent company of La Petite Academy; Childtime Learning Centers; Tutor Time; The Children's Courtyard; Everbrook Academy; Montessori Unlimited; AppleTree & Gilden Woods; U-GRO; Creative Kids Learning Center; Young School; and Pathways Learning Academy

4 If not the outright owner, Bain Capital was an investor during these years (Lattman 2013).

5 Child Development Schools is the parent company of Childcare Network, Sunrise Preschools, and My Small Wonders. The capacity statistics only reflect that of Childcare Network.

## ... FORESHADOWING RISKS OF PROFITEERING FROM PUBLIC DOLLARS

**In light of the difficulty that most private providers face in profitably operating a child care business, a consensus is growing among policymakers and advocates around the need to increase public funding for this service**. Although long-term federal funding for child care got cut out of the legislation that eventually became the 2021 Infrastructure Investment and Jobs Act and the 2022 Inflation Reduction Act, child care providers received short-term stabilization funding during the pandemic through the 2021 American Rescue Plan Act (Hickey 2022). President Biden also signed a 2023 Executive Order directing HHS to consider strategies for reducing families' child care costs while increasing support to providers.

**Meanwhile, several states have taken the lead in reforming their local child care markets.** The most ambitious of these has been New Mexico, where 70 percent of voters supported a 2022 ballot measure amending the state constitution to extend children's guaranteed right to an education down to children aged five and under, and to create a permanent endowment funding child care using revenues from oil and gas development on public lands (Covert 2022). Meanwhile, Vermont's 2023 Child Care Bill expanded public child care spending while dramatically expanding families' eligibility for subsidies; a similar bill passed the Massachusetts Senate in March 2024 (LeBlanc 2024).

**If enacted, increased public funding could help address the core market failure plaguing the child care industry.** If this funding is high enough, this money could help close the gap between providers' revenues and costs—an outcome that should attract more entrepreneurs, investors, and even creditors into this sector. Furthermore, if public funding is high enough, diverse types of providers would even be able to profit while taking on the higher costs of achieving the sector's vision objectives, thus improving child care job quality (attracting more workers to the sector) and maximizing the benefits to families, communities, and employers elsewhere in the economy.

**However, public funding that increases child care businesses' profitability would do more than make it feasible for the U.S. to achieve the vision for child care—it would also create market conditions that, all else being equal, would attract more private equity funds and other profit-maximizing actors into this industry.** We know this because private equity is already a significant player in the few profitable corners of today's child care markets, indicating that theirs is a business model poised to expand into other communities as market conditions improve. We also know this because private equity is heavily invested across U.S. care industries—such as nursing homes, hospice care, autism services, and hospitals—where public funding through programs like Medicare and Medicaid is the critical determinant of private providers' profitability (Appelbaum and Batt 2020; Ballou 2023; Morgenson and Rosner 2023). In fact, private equity investments in many of these sectors increased dramatically in response to new legislation, like the Affordable Care Act, that increased funding to health care providers (Appelbaum and Batt 2020; Batt, Appelbaum, and Nguyen 2023). There is no reason to suspect that private equity will stay out of child care markets once they have been stabilized with public support. In fact, private equity-backed child care companies exhibit many of the characteristics as their counterparts in other sectors, including their taking out large loans and subsequently acquiring other competitors and suppliers.

**Although increased private equity interest in child care could be seen as a signal that policymakers have solved this industry's profitability problem, this would not guarantee that these actors are making positive contributions to the broader vision for child care.** In fact, the well-documented experiences from the other sectors that have seen significant private equity investment—where private equity-owned businesses have been more likely to push down the quality of the services they provide, the wellbeing of their customers and workers, and the competitive health of local markets—should serve as a warning that private equity funds and other corporate actors will exploit every opportunity to maximize their profits, even if their own wealth comes at the expense of the other stakeholders and objectives of the child care industry.

**Policymakers and other child care industry stakeholders must therefore ensure that policy and market guardrails are in place as more public money enters the child care industry, striking a balance between the need to increase child care businesses' profitability and stabilize child care markets and the need to limiting opportunities for outright profiteering.** This means that policymakers and other stakeholders will have to ensure that the value that private companies take out of this industry in the form of profits does not exceed the value that they create for families, workers, and communities. The long term challenge will be in determining where this threshold between fair profits and profiteering lies.

SECTION 2

# THE FOR-PROFIT PLAYERS

# SECTION II
# THE FOR-PROFIT PLAYERS

## 1. THE CHILD CARE BUSINESS MODEL

### I. OPERATING EXPENSES

#### LABOR

**Labor costs are child care providers' largest expense.** Even through child care wages are extremely low relative to those of comparable industries, they still contribute to 63 percent of the expense of providing infant care, 57 percent of the expense of toddler care, and 52 percent of the cost of preschool care (Workman 2018).

**Providers do not have much flexibility in how many people they hire given that states regulate the maximum permitted child-staff ratio.** These ratios vary according to a child's age, with each member of staff caring for fewer children the younger they are, reflecting younger children's need for more one-on-one attention. As of 2011, a single child care worker was permitted to care for three to six infants, three to 12 toddlers, and seven to 25 preschoolers, with the exact ratios varying by state. By contrast, an elementary school teacher can legally supervise a class of between 10 to 26 children, depending on the state (ACF 2013).

**These staffing requirements are critical to protecting children's safety and fostering nurturing relationships that support their development, but by default, they raise the cost of providing child care, especially to the youngest children.** In 2023, the average annual price of child care for an infant exceeded the cost of in-state university tuition in 39 states and the District of Columbia (CCAoA 2023). Some providers therefore charge a higher fixed cost to care for children of all ages, using the income from older children to supplement the cost of the youngest; others restrict their services to preschoolers only.

**Staffing requirements leave wages as the only major variable that providers can control to keep their labor costs down.** This in turn leads to the systemically low wage and benefit rates across the industry, and the resulting erosion of care quality (see Section I.2).

#### REAL ESTATE

**Child care enterprises must provide care in a safe and healthy environment, but these costs factor into a providers' business model in varying ways.**

**For home-based providers that work out of their own homes, their personal living and business expenses can be intertwined.** This may benefit providers who own their property and have paid off their mortgage, and who therefore do not need to pay additional expenses to run their child care business beyond those needed to maintain appropriate facilities for children and property taxes. However, for many home- and center-based providers, rising rents, mortgage, and housing costs due to post-pandemic interest rate hikes are making it more difficult for them to pay for the space that they need to provide care.

**Facilities also need perpetual maintenance, and providers can struggle to pay the full costs needed to meet minimum quality standards.** A study of facilities in Massachusetts found that it would cost providers an average of $18,000 to make repairs to meet minimum regulatory standards, $90,000 to meet recommended professional standards, and $154,000 to meet best-practice standards (Pardee 2011).

**Some providers avoid real estate costs by contracting with third parties who provide them with these facilities for free.** These arrangements can include local schools, community centers, religious institutions, or charities either contracting with a provider to operate in a given location, or simply donating space to them for free. They also include arrangements with large employers who contract with a provider to offer child care on-site for their employees.

#### OPERATING HOURS

**Child care providers' hours of operation often reflect the needs of working parents, and require these enterprises to stay open longer than most K-12 schools.** Listed home-based providers provide a median of 54 hours a week of care; paid, unlisted home-based providers provide a median of 40 hours a week (NSECE 2016). More community-based providers may also open during non-standard hours, such as during the weekend or in the evening, to serve parents working shifts during these times. These longer hours raise the labor costs of providers who need to hire more staff to operate multiple shifts.

### QUALITY STANDARDS

**Quality standards vary state by state, contributing to the differences in care costs across the country.** Federal child care programs, like Head Start, provide some quality parameters within which states need to operate. The most important quality regulations, such as staff-to-child ratios, create a floor in providers' operating costs.

**Forty-one states and DC have introduced Quality Rating and Improvement Systems (QRIS) to oversee their efforts to regulate child care providers' quality.** These systems define a set of quality benchmarks and goals, and develop a rating system to measure providers' compliance with those standards. The most commonly assessed traits are staff qualifications, curriculum use, and other metrics about staff-child interactions—but not metrics such as staff wages or turnover, even though care workers' wellbeing has a direct correlation to care quality. The ratings are supposed to be shared with parents to allow them to choose higher quality providers, but only 13 states have budgeted for and created a dedicated system for communicating QRIS scores with the public (Herbst 2022). The share of providers participating in QRIS also varies by state, ranging from as low as 2 to 3 percent of providers to 100 percent of them. Herbst (2022) estimates that, nationally, only about a third of center-based providers participate—with participation even lower among home-based providers.

**States vary in the supports and incentives they offer to providers who participate in QRIS, or who achieve higher quality ratings within these systems.** Forty states incorporate at least one financial incentive with QRIS, ranging from start-up grants to financial bonuses tied to their quality score. However, these incentive schemes are only effective if they are large enough to reimburse providers for the costs of meeting higher standards (NASEM 2018). Otherwise, these incentive schemes reward providers that were already more financially secure, without giving adequate support to other providers who need access to money to make necessary improvements. In fact, child care programs that serve higher numbers of Black and Brown children are less likely to be awarded high ratings, which in turn locks them out of many of the benefits that flow to those programs (Bassok, Dee, and Latham 2019).

**Poorly designed QRIS systems can also entrench racial inequity in the child care sector.** QRIS often does not incorporate measures that meet families' diverse needs, including families' cultural and linguistic preferences— which can be particularly important for families of color (Lieberman 2022; Nzewi, Ignatius, and Kruckle 2020). Furthermore, QRIS can disproportionately exclude care provided in home-based settings and during non-traditional hours. This results in family child care providers being less likely than center-based providers to receive public subsidies, in turn limiting access to care for single working mothers of color who disproportionately rely on home-based care.

## II. REVENUE

### SOURCES OF FUNDING

**While children, and by extension their families, are the ultimate "consumers" of child care,  providers can earn revenues from one of three sources: families, the government, or employers.** Many providers earn money from a combination of these sources, but each revenue source presents different opportunities and limitations to providers.

#### FAMILY FUNDING

**In the U.S., the child care system is structured so that families are expected to finance the majority of child care costs** (NASEM 2018). In 2017, 4.9 million households spent $3.6 billion on day care centers, nursery schools and preschools (Palladino and Mabud 2021). These costs have been rising. Between 1995 and 2016, the average out-of-pocket cost for childcare increased by 86 percent (Swenson and Simms 2021). This increase in costs was particularly steep for higher-income families.

**These costs remains unaffordable for most families in the U.S.** In 2023, a family would have needed an annual income of at least $165,000 (among the top ten percent of incomes) in order to consider the $11,582 average national price of child care affordable without subsidies (CCAoA 2023). Child care costs are a particularly serious problem for families with low-incomes, for whom the high cost of care represents a higher share of their income than for wealthier families. Even though 72 percent of families with incomes below the poverty line paid no out-of-pocket costs for child care in 2019, 64 percent of those who did pay for child care were spending more than 10 percent of their income on care. Furthermore, families whose incomes were just above the poverty line were most likely of any income group to pay over 20 percent of their income on child care (E. Hardy and Park 2022).

**The government does provide some support to families to help them cover their child care expenses.** The **Child and Dependent Care Tax Credit (CDCTC)**, for example, allows families to claim a percentage of their care expenses for children under age 13, so long as this care is used to allow parents or guardians to work, look for work, or participate in a qualifying educational program. In 2022, an estimated that $3 billion in tax benefits were claimed under the CDCTC (NWLC 2024). A number of states offer similar tax credits. Meanwhile, people whose employers offer **Dependent Care Assistance Program (DCAP)** benefits can to deduct up to $5,000 a year from their pre-tax gross earnings to pay for child and dependent care expenses. Workers can also reimburse themselves for out-of-pocket expenses throughout the year. These pre-tax funds are deducted directly from a worker's paycheck, reducing their overall taxable income.

**Nevertheless, the primary beneficiaries of these types of programs tend to be wealthier households.** Since the CDCTC is a non-refundable tax credit, it is only available to families who earn enough to incur a tax bill. In 2022, only about 5 percent of all CDCTC benefits went to families with incomes of $30,000 or less (NWLC 2024). The American Rescue Plan Act expanded the CDCTC by making it refundable and thus available to all families—resulting in at least 288,000 more families receiving CDCTC in 2021 compared to 2020 (NWLC 2023b)—but this provision expired at the end of 2021. Meanwhile, employers who participate in DCAP skew toward larger companies with a higher compensated workforce, and provides the greatest dollar benefits to employees in the highest tax brackets. This program also favors people who can afford to deduct funds from their paychecks, and who can risk losing the funds if they do not spend them during the same year.

**If costs rise too high, many families will opt to provide the care themselves, even if it means one parent exiting the labor force to do it.** This outcome becomes especially likely when families calculate that child care costs will eat up a significant share, if not all, of one of the parents' earnings—with women more likely to stop working than men. This is an acute problem for families with multiple children. Non-parental care use drops off substantially for families with more than two children under age five (Latham 2017). This exit from the labor force can significantly decrease their economic security in both the short and long term. Access to affordable care for women with two children can increase their lifetime earnings by about $94,000, their private savings by $20,000, and their Social Security benefits by $10,000 (Hartley et al. 2021).

**The difficulties that families face paying for child care put pressure on providers to keep prices as low as they can, even if they do not cover the full cost of care**. If providers raise prices too high, even if just to cover the real cost of care, they may not only risk harming the families and communities that providers serve—particularly in communities where families have low- and moderate-incomes—but may also cause demand to drop and undermine revenue.

## PUBLIC FUNDING

**The government is a significant funder of the child care industry through the federally-funded Child Care and Development Fund (CCDF) and Head Start programs.** CCDF is the primary source of federal funding for child care, and is funded through the Congressionally appropriated Child Care and Development Block Grants (CCDBG). This money is distributed as block grants to states, who then administer its use to run child care assistance programs. This funding is structured so that eligible[6] families are free to select their preferred care provider, and the state will cover the full or partial cost of their services. Meanwhile, Head Start is a federal public child care and pre-kindergarten program run by the HHS Administration for Children and Families (ACF) that provides grants to public agencies, private providers, and local and tribal governments to operate local programs in home- or center-based settings according to federal Head Start standards. Families that receive care under Head Start pay no fees.

**These subsidies should incentivize providers to serve families with low incomes, who would otherwise find it difficult to pay**

[6] States are responsible for determining CCDF eligibility requirements, but must set these limits so that families are eligible if they earn at or below 85 percent of the state median income

**for care out-of-pocket—except that public payment rates rarely cover the true cost of care.** Workman (2021) estimates that, on average, subsidies cover only 75 percent of the cost of providing care that meets state licensing quality targets for infants, and only 42 percent of what it would actually cost to provide high-quality infant care while paying caregivers a fair wage. This problem is exacerbated by the fact that states often set payment rates for CCDF using market surveys of the average rates that providers are charging; therefore, providers in low-income communities who charge lower fees to keep care affordable for local families will receive less funding from government programs than providers in higher-income neighborhoods where more families can afford to pay higher rates.

**As much as the public sector contributes to child care, the federal government has no commitment to guarantee access to care for all children, or even all of those deemed eligible for support.** Both CCDF and Head Start only serve families with low incomes, and neither program has a large enough budget to fund even the families that are eligible. CCDBG is estimated to have only served served one in seven eligible families in 2018 (A. Hardy 2022). Schmit and Walker (2016) estimate that only 21 percent of Black children, 11 percent of Asian children, 8 percent of Latino children, and 6 percent of Native American children who were eligible for CCDF received subsidized care. Meanwhile, only 31 percent of eligible children aged three to five received care through Head Start in 2016, and only 6 percent of eligible children under age three were served by Early Head Start (Herbst 2022).

**Providers who serve subsidized children must therefore rely on families to cover the remainder of care expenses.** About 76 percent of families receiving CCDF must provide a co-payment for care, with states determining how much they must contribute on a sliding fee basis. These co-payments average 6 percent of families' income, implying that the subsidies have at minimum pushed the cost of care down to affordable levels (Treasury 2021).[7] However, in some states where the public payment rate falls below providers' private tuition fees, families are asked to cover this funding gap in addition to paying their required co-payment.  Families who receive Head Start, however, pay no additional fees, limiting Head Start providers' ability to supplement public funding when it falls short of real costs.

### EMPLOYER FUNDING

**A minority of employers (largely of white-collar professions) fund child care as a form of benefit to their employees.** These benefits can range from offering tuition stipends to families to help pay for the provider of their choice, to partnering with a provider to guarantee pre-paid spots to families, or to contracting with a provider to provide child care on-site for employees. The type of benefit offered may become a function of the size of the employer, with small businesses only able to offer partial cash support for care, and large companies able to absorb the cost of on-site delivery.[8]

**The government has introduced a number of incentives to encourage employers to provide child care benefits to their employees.** The **Employer Provided Child Care Tax Credit** (Section 45F of the tax code) is available to employers who directly provide care, either by providing on-site or near-site care, or by contracting with a local child care facility to reserve spots for their employees. Businesses must spend at least $600,000 to qualify for a credit worth a percentage of their expenditures, up to $150,000. Since the credit is nonrefundable, many non-profits and small businesses do not have a sufficient tax liability to claim the credit. Furthermore, the cost of operating on-site child care far exceeds the value of the credit, making it ineffective at supporting small- and medium-sized businesses who may want to offer this benefit to their staff. Overall, this credit is underutilized (NWLC 2024). Another model for government endorsement of employer-funded care has come from the Department of Commerce, which mandated that any semiconductor manufacturer requesting more than $150 million in funding through the **CHIPS and Science Act** submit plans for providing affordable, accessible, reliable, and high-quality child care for the workers who build and facilitate their plants.

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[7] New CCDF rules limit co-payments to no more than 7 percent of family income, which may push down families' co-payments from their current levels. States are also being encouraged to waive co-payments for families with incomes below 150 percent the federal poverty level (ACF 2024).

[8] Many employers still require that employees who use their facilities pay tuition for this care. Although the employer may subsidize these rates, tuition can remain high.

### BOX 3: THE SYSTEMIC IMPLICATIONS OF EMPLOYER-SPONSORED CHILD CARE

**Employers currently cover a small fraction of child care funding, but corporate interest in these forms of worker benefits are increasing.** On-site or near-site child care at workplaces is only offered by 7 percent of employers, most of them large companies with over 1,000 employees (Matos, Galinsky, and Bond 2017). Even within the companies that provide child care benefits, these services are often restricted to higher-paid, white-collar employees (Haspel 2024a). Nevertheless, especially after the pandemic, child care benefits are seen as an important way for attracting and retaining talent. According to one survey by Care.com (2024), 56 percent of businesses are prioritizing the provision of child care benefits in 2024—a 10 percent increase from the previous year, and a higher percentage than those prioritizing benefits for mental health, paid parental leave, or senior care.

**While employers can benefit themselves and their employees by funding child care, a national child care system that depends on employers to substitute the government as providers of basic public goods—as it does for health insurance—will see similar inequities as those experienced elsewhere in the U.S. welfare system** (Haspel 2024a). Many smaller businesses or nonprofit employers find it difficult to pay for these benefits, making it harder for them to attract workers away from larger and richer organizations. It is primarily available to the fraction of the U.S. workers in full-time jobs, and the cost of paying for child care may deepen the incentive that employers face to hire part-time workers and contractors to avoid paying employee benefits (Even and Macpherson 2015). The workers most likely to receive these benefits are those in higher-wage jobs. However, much of the cost of such benefits are ultimately paid by the employees themselves through lower wages (Gruber 1994; Olson 2002). Furthermore, employers' child care benefits can decrease parents' workforce mobility, increasing their reluctance to switch jobs if doing so will require them to send their child to a different care provider—a process that can be disruptive and upsetting to children.

**Child care providers who partner with employers can benefit from this lucrative, stable source of revenue.** Businesses and other employers do not face the same liquidity trap as parents do, and may be able to pay higher per-child fees to providers (in conjunction with family co-payments) than their employees would have been able to on their own. Employers are also more likely to enter into multi-year contracts with providers, and to pay upfront for the expenses of multiple children, allowing providers greater certainty over their revenues. Furthermore, employers who open on- or near-site programs usually cover the expense of renting and maintaining the facilities, reducing providers' operating expenses.

**Employer-funded care, however, can create its own elements of instability as well.** Providers who serve families who receive tuition stipends may find that their demand suddenly drops during economic downturns if there are mass layoffs from these employers. Employers may also be erratic in which benefits they provide their workforce, and can at any time choose to withdraw their child care benefits or to close their on-site facilities (Haspel 2024a).

### FEE STRUCTURE

**For child care providers, a second critical consideration about their revenue is their fee structure.** Often, fee structure is the function of where a given child's funding comes from, and many providers serve children using a mix of systems. For example, a program can receive a contract from Head Start to run one classroom, while maintaining a second classroom for children whose families make regular tuition payments.

**Under a tuition model, providers get paid according to the amount of care that they provide, as measured in enrollment or attendance rates.** This would include providers that charge families per hour or per day of care. Policies such as the CDCTC, DCAP, and CCDF that allow families to select their preferred provider are more reliant on this fee structure.

**This model provides extreme flexibility to families to split their child care spending across multiple providers, and to vary who they call on to provide care by the day.** This may also be more affordable to families who can more easily make small regular payments to providers as opposed to paying a large sum upfront at the start of a season. It can also allow families to avoid paying for the care that they do not use, such as days when their child is absent.

**However, these perceived benefits for families come at the expense of providers, for whom this fee structure is extremely unpredictable.** Small providers who only serve a handful of children at a time, for example, can struggle to cover their operating costs if even one child is absent for an extended period of time. Similarly, providers' revenues can fall to critical levels during certain seasons, like the summer, or during an economic downturn, when care demand drops across the board. As a result, providers may raise their hourly fees under this model to create a buffer for themselves when their revenues lag.

**Under a contract model, providers are paid a lump sum for making a service available—as measured by the number of seats a program has—regardless of how much of that service is used.** Head Start programs, employer-sponsored care facilities, and many state pre-K systems use this funding model. Contacts can also be expanded to more closely resemble the K-12 funding system, where government pays for the full expense of operating a school, including its affiliated administrative costs.

**The contract funding model is much more stable for providers than tuition funding.** It can also make it easier for providers to hire full-time staff, since they have more certainty about how much care they will need to provide (and how many adults they will need per classroom) over an extended period of time. For this reason, contract funding is the preferred fee structure among child care advocates and providers.

**Contracts also make it easier for the funders—usually the public sector—to set conditions around quality metrics, staff compensation rates, or even opening hours that providers need to meet as part of the contract**.

# 2. PRIVATE EQUITY: ARCHETYPE OF CORPORATE BUSINESS

## I. PRIVATE EQUITY BUSINESS MODEL

**Private equity firms—like Kohlberg Kravis Roberts (KKR), Carlyle Group, Blackstone, or Bain Capital—are companies that manage investment funds**; they oversee funds that receive money from institutions like pensions funds and from wealthy individuals, and their purpose is to invest that money in ways that will maximize its returns. Their funds are distinct from other forms of investment, like venture capital, because they invest in more mature businesses (rather than startups), and take direct control over the management and operations of the companies in their portfolio. Private equity funds thus have more control over their portfolio companies than any of their investment fund cousins, and can more easily restructure these businesses to quickly maximize the wealth that they earn for their owners. The ultimate goal of these funds is to sell their portfolio companies within three to five years at a profit.

**The private equity business model can be summarized as:**

1. **Create a Fund.** The private equity business model begins when a private equity firm, like Blackstone, launches a new fund. A committee of partners and other members of the firm is put in charge of the fund, and they become its general partners (GP), responsible for making all decisions about how to invest and leverage the fund's money. The GP will sponsor the fund with a starting amount of equity capital, which generally represents 1 to 2 percent of the total amount of money the fund will invest. The average fund is designed to exist for a decade, at the end of which it will have to have sold off all its assets so that the invested capital can be returned to the GP and other investors along with all realized gains.

2. **Attract Investors**. The remaining 98 to 99 percent of the money in a private equity fund will come from outside investors, namely institutional investors—like pension funds, insurance companies, university endowments, mutual funds, or sovereign wealth funds—and wealthy individuals. These investors contribute to private equity funds with the expectation that they will deliver outsized returns. These investors become the fund's limited partners (LPs), and they commit to an entirely passive role in the fund's management. LPs cannot take their money out of the fund for the duration of its existence,

and they delegate all decision-making authority over to the GP, to whom they will pay annual fees. Generally, these fees are equal to 2 percent of their investment in the fund—or 20 percent of the value of their investment over the decade span of the fund's life—and are paid to GPs regardless of the financial success of the fund itself (Fleischer 2008).

3. **Leverage Assets to Buy a Portfolio of Companies**. GPs are under pressure to invest the money in the fund in the first three to five years of its life, or else risk having to return the money and the management fees to the LPs. GPs will select companies in which to invest the fund's assets. However, rather than buy companies outright, private equity funds use both their capital and the assets of the company they wish to acquire as collateral to take out loans that will fund the majority of the acquisition. These **leveraged buyouts**, as they are known, allow private equity funds to magnify their capital and acquire a portfolio worth many times more than what both GPs and LPs initially invested. Furthermore, under these deals, the responsibility for paying off the loans falls on the portfolio companies, not the private equity firm or fund.

4. **Take Over Company Management to Increase Value to Investors**. Private equity funds use leveraged buyouts to acquire a majority stake, if not outright ownership, of its portfolio companies. This gives it complete control over company operations. With the exception of private equity firms that specialize in a given industry, GPs generally select these companies for their financial opportunities, not for the role they play in the economy; many funds simultaneously manage firms from multiple unrelated industries. GPs often replace much of the company's management with people whose interests are aligned with those of the fund. Furthermore, during the period while they remain owners of these companies, the private equity fund can charge these companies an assortment of management fees (which go to the GP) or demand dividend payments (which are shared among the GP and LPs).

5. **Company Exit and Fund Closure**. At the end of the fund's lifespan, GPs distribute the investment returns among the LPs. For this to happen, the fund will have to have realized all its investments in companies, either by selling them to other private buyers (including other private equity funds), allowing them to go public through an initial public offering (IPO), or closing companies that have failed. In many funds, if the profits from these investments clear an 8 percent hurdle rate, the GP becomes entitled to 20 percent of these returns—with the LPs receiving the remainder. Since these profits are aggregated from across the fund's portfolio, any losses from the failure of one company in the portfolio can be compensated with the gains elsewhere—especially if the failing company yielded revenue from fees, dividends, or asset sales to the fund.

6. **Repeat**. Private equity firms often raise money for new funds every three to five years, and thus manage multiple funds simultaneously. Any returns that they garner for themselves or for LPs from their funds is money that can subsequently be re-invested in a new fund. Private equity firms therefore effectively hold a portfolio of funds, and net losses from any one fund—which could result in net losses to LPs—can be compensated for the private equity firm (but not for the LPs) with gains in other funds, especially if the losing fund yielded revenue to the GP in the form of fees and capital gains from the LPs and portfolio companies.

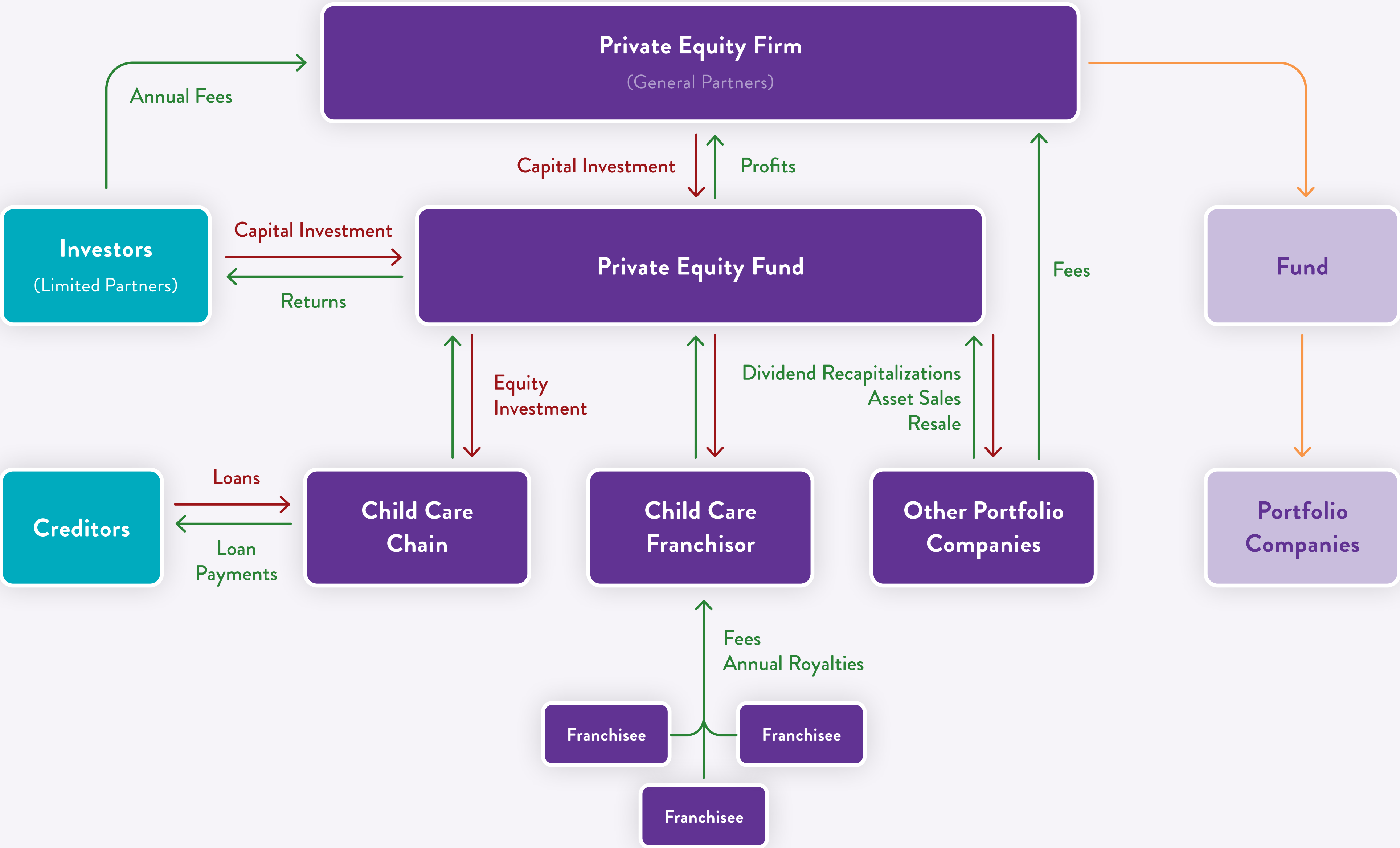
**Private equity firms paint themselves as the investors who buy struggling businesses, shake up their management while providing an influx of capital, and thus set the company on a more successful track.** While this does happen in a minority of cases, this type of distress investing accounts for a small share of private equity buyouts. The key takeaway from looking at the private equity business model is that these funds buy profitable companies with the aim of selling them within a few years at a profit, and they do not face significant structural incentives to consider the long-term health of the companies in their portfolio, let alone these companies' workers, customers, creditors, or suppliers.

**Instead, everything in this business model incentivizes and enables GPs to prioritize maximizing short term profits.**

**First, the GP makes more money the higher the returns from their portfolio**. Although it is common across various types of investment funds to tie asset managers' pay to the returns they achieve, in private equity funds, GP incentives are structurally aligned with no other priority than maximizing profits for the fund.

**Second, the GP faces few financial (or legal) consequences should their tactics fail—incentivizing them to take higher risks.** To start, they face no responsibility for paying back the debt that they load onto companies, even if these companies default—incentivizing them to use high levels of

**Figure 3:** Private Equity Ownership Structure




Adapted from Appelbaum and Batt (2020) we bring together a wide range of sources and empirical evidence to answer these questions. Given the complexity of the sector, we focus on four segments where private equity firms have been particularly active: hospitals, outpatient care (urgent care and ambulatory surgery centers debt, no matter the risk to companies. Similarly, the portfolio companies alone are legally liable for any harm that befalls stakeholders, like customers, from their new managers' business tactics. Private equity funds diversify their risk across numerous portfolio companies and funds, allowing them to profit even if one company or fund fails. Furthermore, private equity funds have so little of their own capital in the fund that they can take enormous risks with LPs' money in pursuit of high returns. Even if their funds were to be unprofitable, GPs earn enough in fees from LPs to recoup much of the value of what they invest themselves.

**Third, private equity invests in their companies for such short timeframes they have every incentive to implement tactics that yield immediate, guaranteed, short-term gains to investors rather than investing in improving the company in ways that will only yield growth in the long term.**

**Finally, GPs do not have to answer to any other stakeholder other than themselves—not even the LPs they are being paid to benefit.** Although LPs, like the shareholders of publicly-listed companies, are primarily interested in maximizing their returns from these investments, shareholders are better able to monitor the management decisions of public company executives than LPs are able to oversee GP behavior. In the interest of protecting investors, public companies are required to publicly disclose large amounts of information about their finances and operations. Neither the private companies in a private equity funds' portfolio nor the private equity funds themselves are required to make similar disclosures to LPs, offering them few opportunities to hold GPs accountable for their investments and management decisions.[9]

**This suggests that any power to rein in the worst of private equity funds' behavior must come from external forces—be it government regulation and enforcement, or countervailing power from other stakeholders such as labor unions.**

## II. PRIVATE EQUITY + FRANCHISING

**Franchise companies make their money by licensing their brand and operating model to local entrepreneurs.** This business model is quite common in sectors like fast food (e.g. McDonalds, Dunkin') where new entrepreneurs may value the brand recognition that can come from running a franchise, as well as the explicit instructions about how to operate their new business. Under this business model, entrepreneurs pay the franchisor company an upfront fee and annual royalty in exchange for being allowed to own and operate an outlet of that franchise brand. Franchisees are technically independent businesses, but they are contractually obliged to operate their business according to the terms of the franchisor—terms that usually detail the types and price of goods and services sold, the decor and facilities that must be used, and the expenses that must be incurred around marketing and other activities. This business model is intended to shift the formal responsibilities of asset ownership and of worker employment (and the regulatory scrutiny this incurs) away from the core company (Callaci 2021).

**This business model is particularly harmful to workers, who are stripped of the benefits that come from employment in a larger company, including promotion opportunities and legal protections** (Weil 2014). Meanwhile, the terms of the franchisor-franchisee contracts often leave the franchisee owners with control over few expenses other than labor, meaning that this is the only area where they can try to push down costs. As has been seen in the fast-food industry, these structures also complicate efforts to organize the workers employed in the same chain, since they are not technically working for the same employer, even though many aspects of their working conditions are set at the franchisor level.

**The relationship between franchisors and their franchisees is, in many ways, analogous to that between a private equity fund and its portfolio companies.** The franchisee/portfolio companies remain independent companies, and thus incur operating expenses, debt commitments, and legal liabilities towards suppliers, customers, and workers. Meanwhile, the franchisors/private equity funds receive regular fees, and

[9] In 2023, the Securities and Exchange Commission (SEC) introduced requirements that private funds—including private equity, venture capital, and hedge funds—provide quarterly disclosures to investors about their fees, expenses, and performance. In June 2024, this rule was struck down by a federal appellate court, arguing that the SEC is empowered to protect everyday retail investors, but not the more sophisticated investors who make up the majority of private fund investors (M. Goldstein 2024).

control the conditions and incentives for franchisee/portfolio company operations. In other words, franchisors and private equity funds benefit whether or not the local enterprise remains profitable and are shielded from many of the legal or financial consequences that may stem from their franchisee/ portfolio company's activities.

**Two significant differences between franchisors and private equity funds are their growth tactics and subsequent control over the value of companies' assets.** Whereas private equity grows through direct acquisition and ownership of its portfolio companies, franchise chains grow from franchisee businesses buying into their brand network. This means that private equity funds can pay themselves dividends from their portfolio companies' revenues, including from selling off assets like real estate, whereas franchisors remain more constrained in their control of franchisee finances according to the terms and fee structures laid out in their contract with franchisees.

**Both private equity and franchisors rely on disaggregated ownership and liability, and private equity ownership of a franchisor simply adds another layer to this structure** (Appelbaum 2017). Franchisees pay fees to the franchisor, who pay fees to the private equity fund; liability is shifted down from the private equity fund to the franchisor and down to the franchisee (see Figure 3). Private equity funds like Roark Capital are very active in franchise-intensive industries (Ash 2021a), both contributing to and benefiting from the profit-maximizing nature of the franchising business model.

## III. PRIVATE EQUITY + GROWTH EQUITY

**One variant of the private equity model are funds who use their money to provide "growth equity" to new businesses rather than acquiring more established companies**. Growth equity funds thus behave more like venture capital funds, working with entrepreneurs to develop or grow new businesses. These funds typically specialize in a given industry, and build on a reputation of operating successful businesses to attract more talented managers to their team. Although many of these funds replace a company's management, some are more open to taking only a minority ownership stake in a business, thus providing financial support to entrepreneurs without supplanting the existing leadership. This offers other stakeholders in a company more opportunities to check the profit motivations of their private equity partners.

**Since growth equity funds are investing in ways that create value for more stakeholders than for themselves, these funds can have a more positive reputation within industries than their buyout counterparts.** This is especially true in industries where small businesses are less likely to be able to access financing from traditional banks (Batt, Appelbaum, and Nguyen 2023). Even though growth equity funds may use similar tactics to other buyout private equity funds—such as rollups or leasebacks—more of the money these tactics create is reinvested in the portfolio companies themselves, as opposed to going directly to the private equity investors.

**Nevertheless, the main goal of growth equity funds remains to acquire a portfolio of companies that they can sell within a given number of years at profit**. These funds are thus grooming companies to be attractive to strategic buyers, who are often larger companies looking to grow by acquiring smaller competitors—a profile that includes companies owned by buyout-focused private equity funds. These types of companies are ideal buyers for growth equity funds, who are interested in selling to the highest possible bidder, since they are often willing to pay a premium on a company that helps them expand into their target markets, even if the cash flow and profit margins of the company do not warrant such a high price. Therefore, the long term impact of growth equity funds often is dependent on which company they end up selling to, and the ways that this contributes to an industry's consolidation into larger chains.

## SECTION 3

# THE PRIVATE EQUITY PLAYBOOK FOR PROFITEERING IN CHILD CARE

# SECTION III
# THE PRIVATE EQUITY PLAYBOOK FOR PROFITEERING IN CHILD CARE

## STEP 1: ACQUISITION

### I. CONSOLIDATION (ROLL-UPS, MERGERS & FRANCHISING)

**Child care is a fragmented industry, which makes it an appealing target for private equity investors who want to create profits through consolidation.** Private equity investors in fragmented markets generate profits by buying up and merging a series of small companies and then selling the consolidated company for more than what they paid to acquire the sum of its parts. This has been one of the features driving private equity acquisitions of health care providers, including local physician practices (Appelbaum and Batt 2020).

**The child care industry is particularly vulnerable to consolidation given the longstanding structural problems facing the industry, which are driving providers to exit.** The economic challenges facing child care providers are not new, but providers were put under even more pressure during the pandemic and, more recently, the expiration of the emergency support that many providers were relying on for their survival. Under these conditions, a growing number of providers risk deciding that they cannot continue to run a child care business. These providers may find private equity investors' offers appealing, either believing that a sale can put their business on more even footing, or looking for the quickest means of exiting the sector altogether.

**Private equity investors can offer two significant benefits to the child care providers who sell them their businesses.**

**The first is the upfront cash payment for the business.** This is particularly valuable for owners who are looking to retire or otherwise exit the child care industry, and whose savings are tied up in their business. Private equity investors will be most interested in higher-quality, licensed providers—especially centers that have multiple locations or classrooms—but for these providers, there may be few, if any, other buyers. In the U.S., they are also likely to be more interested in providers located in wealthier communities where families can independently pay the full cost of care—at least until public funding increases enough to turn less wealthy communities into viable markets for private providers.

**The second promise of private equity is the ability to relieve providers of administrative tasks, and to help them save money through economies of scale.** Corporate chains centralize operations for tasks such as scheduling, accounting, payroll, or insurance, allowing providers to focus on the work of providing care rather than that of running a business. This also has the added benefit of bringing down providers' operating costs. Similarly, corporate providers can buy supplies, from diapers to books, in bulk, thus driving down their cost.

**U.S. child care markets are experiencing three key consolidation tactics.**

**First, small child care providers are being rolled-up into new chains.** This trend is mostly being observed at the local level, where providers are reporting receiving buy-out offers from smaller private equity-backed companies (Haspel 2024a). This tactic can also be a means of converting existing non-profit programs into parts of for-profit chains, as has been observed in other sectors such as home health care (Moss and Valdes Viera 2023).

**Second, large non-franchise providers are expanding through acquisitions of these smaller chains.** This tactic is especially apparent in companies like Learning Care Group, where acquired chains, like AppleTree & Gilden Woods, continue to operate as distinct "brands," even while care offerings and operations are steadily harmonized across the parent company. However, similar acquisitions pepper the history of the non-franchise corporate providers—usually preceded, according to Pitchbook, by the receipt of loans which we can assume are used to finance this growth. These acquisition patterns have also become a core part of the British child care market, which is similarly fragmented and under-funded (Simon et al. 2022).

**A distinct feature of the child care industry when compared with other care sectors is the willingness of these larger companies to acquire single-site providers**; the norm in other sectors is for these larger companies to primarily interest themselves in acquiring providers that have already been rolled up to gain some measure of economies of scale. KinderCare, nevertheless noted in its IPO filing that it actively considers acquisitions of providers with a single site or with multiple sites.

**This interest in small acquisitions is also reflected in the third acquisition tactic of growth through franchising.** The prevalence of franchise companies in child care is another feature that distinguishes this market from those in health care. Franchise growth differs from growth through roll-ups and acquisitions in that the providers that get added to a chain do so at their own expense, and technically remain independent businesses. This shifts the financial risk from growth away from the parent franchisor company onto the local programs who become franchisees. As opposed to receiving a buy-out payment when they are acquired, providers who become franchisees make an upfront payment to the franchisor, followed by regular royalty payments, to gain the benefits of the company's brand name, standardized operating models, and whatever centralized support they offer as a form of economies of scale. Since franchisee owners are also likely to take out loans to pay for these expenses, the growth of franchise chains is debt-financed much like the growth of rolled-up non-franchise chains. Franchisees are also eligible for Small Business Administration (SBA) loans, representing an effective subsidy for franchise chain growth.

**Consolidation presents a number of risks to the systemic goals for the child care industry.**

- **Growth through consolidation allows companies to increase profits without contributing a net increase in the supply of care.** Through roll-ups, acquisitions, and franchising, corporate providers are gaining control over the operations and, more importantly, the revenue flows of existing supply. These companies do open new greenfield providers, but the evidence suggests that most of these companies grow more through consolidation than they do organically. Between 2018 and 2020, for example, KinderCare opened 47 new greenfield centers and acquired 163 pre-existing centers (KinderCare Learning Companies 2021). The picture around franchising is less clear, since there is little data on the percentage of new franchisees that were converted from previously independent businesses, as opposed to being newly created. It is also unclear what share of new versus converted centers are created as part of partnerships with employers, where access to supply would be limited to their employees.
- **Consolidation shifts the flow of revenues and profits away from local (racially diverse female) entrepreneurs and towards (disproportionately white and male) corporate owners and investors.** When a local provider is converted into either part of a larger direct-delivery or franchise chain, they lose control over their financial flows, and profits will flow upwards towards the parent company. This process is the most direct when a provider is acquired outright, but franchisees must also pay a share of their revenue to franchisors, as well as being on the hook for paying fees and other expenses dictated by the franchise company.
- **Provider diversity in communities falls as chains expand**. The more that local providers get converted into parts of larger chains, the less that parents can choose to place their children in non-corporate care settings. This can be a particular problem in communities where several independent providers were rolled-up into a single chain, at once reducing the diversity in provider type and increasing the risk of this new chain unfairly driving out its remaining competition. In the absence of public funding to stabilize child care markets across all communities, this risk of local consolidation into chains is currently most pressing for wealthier communities where child care markets are most "functional," and thus most appealing to corporate providers.

## II. DEBT

**The defining characteristic of private equity is their use of debt to acquire their portfolio companies**. During leveraged buyouts, private equity funds use the money invested in their fund, coupled with the value of the assets of the company they wish to acquire, as collateral for a loan that covers the remaining cost of acquiring that company. The responsibility for paying these loans back falls on the acquired companies, not the private equity fund.

**The most immediate consequence of private equity's use of debt is that portfolio companies face a new operating expense in the form of loan and interest payments**. This implies that, all else being equal, companies must choose to either lower their profits or to divert their spending away from other operational expenses, like staffing, in order to pay back this debt; since the priority of the new private equity owners is to maximize profits, cutting costs elsewhere in the company's operations is often a more likely outcome.

**Private equity investors' habitual use of debt to fund their acquisitions particularly risky in child care given how thin providers' margins are.** Since most child care providers are already struggling to pay their existing operating expenses, new monthly debt payments are an expense that they cannot afford. Franchise chains also face debt risks if franchisee owners take out small business loans in order to pay the upfront cost of joining the franchise.

**Child care is not an industry where debt can easily help struggling providers become more profitable**. Taking on debt can make sense for businesses who can use the one-time cash infusion to make investments in their facilities, or to train their workers, so that they can increase their revenue—thus creating the cash flow that lets them pay back the loan. Most child care providers, however, face a strict upper limit on how much they can receive in revenue based on how much parents are able to pay—an upper limit that does not rise enough to compensate them for any investments they make to improve their operations or service quality. Increased economies of scale may create enough of a financial benefit to acquired programs for them to afford new debt expenses, but this implies that they cannot use this money elsewhere. The child care industry desperately needs an influx of money, but debt financing cannot be a substitute for systemically low revenues.

**In the absence of higher revenues, debt commitments encourage providers to free up money from elsewhere in their business.** Providers may therefore raise their prices or cut their labor expenses—either cutting staff or depending more on lower-paid caregivers (see Section III.4) —to find the money to make their debt payments—undermining care quality, family access, and worker wellbeing.

**Public funding that stabilizes revenues could make debt more sustainable**, **but debt payments would still come at the expense of other investments.** Revenues spent on debt payments cannot go towards raising wages, improving facilities, or otherwise investing in the children in providers' care.

**Debt payments can become an existential risk to providers.** We have seen cases across industries, from retail to nursing homes, where companies and chains saddled with the accumulated debt of their acquisitions go bankrupt from the cost of these debt payments—often after the private equity fund that loaded them with that debt has sold them off and moved on. For example, the world's second largest child care company, ABC Learning, collapsed in 2008 as a result of its debt-financed growth strategy (Sainsbury 2008).

**If entire child care chains—or even just local franchisees—close due to bankruptcy, the families that depend on them for care get left in the lurch, and often struggle to find alternative providers**. To prevent families from losing access to care after ABC Learning's collapse, the Australian government had to step in with a $15 million loan to allow GoodStart, a nonprofit consortium, to take over the management of 570 of ABC's local programs (Hurst 2010).

## STEP 2: POWER WITHOUT ACCOUNTABILITY

### II. DISAGGREGATED OWNERSHIP

**Disaggregated ownership structures shield corporate owners and investors from liability and accountability.** Private equity portfolio companies, like franchisees, are technically independent businesses, and therefore bear sole responsibility for their activities, even though they do not fully control their own managerial decisions. Furthermore, since a large share of revenues automatically flow to private equity funds and franchise owners as fees, the provider companies do not have money on the books that can be taxed, fined, or used to pay back lenders or workers in the event of bankruptcy. This means that while private equity funds and franchise owners incentivize the managers and owners of local providers to cut corners around labor and quality, the funds and franchisors do not bear the risks of being held accountable for this behavior. For example, when Toys 'R' Us went bankrupt in 2017, employees initially received only $2 million of the $80 to $100 million they had been promised (equaling about $60 per person), even though its three private equity owners were estimated to have received $464 million from the company in fees over the 13 years in which they were owners (Ballou 2023). Following a campaign for a better severance package, two of these funds (KKR and Bain) agreed to a $20 million settlement with workers (Vandevelde 2018).

**These structures complicate efforts to regulate or otherwise hold private equity-backed companies accountable for their behavior.** Any regulation or taxation of providers would target either the portfolio company or franchisee, without reaching the managers or finances of the parent investment fund. Families or workers who sue a provider for damages—be it from neglect and harm to a child or labor law violations—cannot target the investor owners, nor access the money they earned from the provider. Especially in franchises, workers will be limited in how much they can unionize across the chain.

### II. MANAGERIAL CONTROL

**Child care enterprises that become part of a larger chain—or that become a franchisee—lose their ability to make most of the decisions about how their centers are run.** The existing owners or leadership team may remain in the center as directors (and, in franchisees, do remain "owner" in name), but they will have little say in the company-wide management that can dictate which operating practices they must adopt, the incentive structures they face, and the expenses and fees that they must spend their revenue on. This means that trained or certified child care professionals no longer make the most important decisions on how care should be provided, and can have especially detrimental consequences for the care of children who require additional services or supports.

**Corporate management will prioritize profits and revenues over care quality.** In particular, the child care program directors in private equity-owned companies report being pressured to prioritize raising enrollment rates above all other considerations, since maximizing the number of children being cared for using existing staff is an important means of maximizing a program's profit margins. Franchisors, meanwhile, will likely encourage franchisees to increase net enrollment irrespective of staffing levels as a means of maximizing the net revenues on which their royalty payments are based. This focus on enrollment is embedded in their personal performance metrics (tied to their bonus), and is more closely scrutinized by their corporate managers than their dedication to improving the care environment for children (Haspel 2024b). This is reflected in companies like KinderCare using enrollment rates as a metric for measuring profitability in their communications with prospective investors (KinderCare 2021).

**Private equity, corporate and franchise chains all exert varying degrees of control over providers' cash flow, diverting money towards investors and shareholders.** Private equity owners and franchisors can both require their portfolio companies/franchisees to pay them regular fees, while corporate managers can be even more direct in controlling the finances of their outlets.

## STEP 3: RAISE REVENUES

### I. RAISING PRICES

**Corporate providers set prices to exceed their operating costs and thus guarantee a given profit margin.** While all businesses strive to make a profit, corporate providers' focus on maintaining this profit margin stands in stark contrast to the many owner-operators of child care programs that must push down their own incomes to ensure that they can remain affordable to the families in their community. The amount that corporate companies are able to charge for these services, and the methods that they will use to raise prices, will depend on who—among parents, employers, and the government—is paying for care, and what limits their ability or willingness to pay.

#### FAMILY FUNDING

**When families pay tuition fees to providers, they are paying to both cover the cost of care and sustain these companies' profits.** Corporate providers who are consistently protecting their profit margins will thus try to raise their fees to match any increase in their operating costs, even if this lowers certain families' access to care. As KinderCare (2021) stated in their IPO filing: "our continued profitability depends on our ability to offset our increased costs, such as labor and related costs, through our families." This implies that if governments enact labor or quality regulations that raise the cost of care, corporate providers will try to ensure that this expense is borne largely, if not entirely, by families rather than companies' shareholders. Similarly, if public payment rates remain below providers' true cost of care (inclusive of the profit margin that corporate providers' demand), families will be responsible for making up the shortfall.

**Corporate willingness to raise prices on families harms the parents who are already paying high fees to access care—undermining efforts to increase accessibility and affordability.** Just because families can pay corporate child care rates does not mean that it is affordable for them to do so—and the evidence suggests that families are often willing to pay more than the recommended 7 percent of their income on child care if that is the only way that they can access this service. Families' extreme need for child care, while in a shortage market, leaves them vulnerable to providers who maximize their prices. Furthermore, as fees rise (in the absence of public funding), a growing number of families may find that they cannot afford care—forcing them to either reduce how many hours they use, or to exit the market entirely. This could be a particular risk in communities where local providers join a corporate chain and replace their affordable spots with less affordable ones.

**Corporate providers have more leverage to raise prices for tuition, co-payments, or fees when families have little choice but to use their services.** This is a particular problem in child care markets given the ongoing shortage in providers, which pushes parents to pay whatever cost is necessary to secure a spot for their child. Increasing supply and maintaining a diversity of provider options are therefore important means of limiting how much corporate providers can charge in excess of their operating expenses.

**Providers who are dependent on family payments for their revenue and profits are also more likely to avoid communities where families cannot pay these costs, contributing to growing inequalities in communities' access to child care.** In the absence of adequate public funding for child care, corporate providers disproportionately serve higher-income communities. One study of the five largest child care providers found that their centers were more likely to be located in census tracts where the median household income was $88,000, compared to the $71,000 median across the states studied (Haspel and Russo 2023). Existing disparities in families' ability to pay may incentivize companies who acquire smaller chains to shut down programs in lower-paying communities in order to divert those programs' capital assets towards expanding services in wealthier areas. This trend was apparent, for example, in the autism services industry, where private equity owners shifted their portfolio companies' resources into states with higher Medicaid reimbursement rates and closed centers in states with lower reimbursement rates (Batt, Appelbaum, and Nguyen 2023).

### EMPLOYER FUNDING

**Employers, like wealthier families, are ideal clients for corporate child care providers, since they can pay the full cost of care, be it independently or by providing adequate financial support to their employees.** We have already seen that employer contracts are the primary focus of companies like Bright Horizons, suggesting that this is a lucrative part of the child care market. Just as corporate providers are more likely to target higher-income families, they are more likely to serve larger, wealthier employers who can pay high fees, as opposed to small- and medium-sized businesses.

**Employer-sponsored contracts with providers are structured in ways that are extremely attractive to private equity.** In particular, employer contracts with providers who manage on- and off-site facilities offer large, flat-fee payments that guarantee regular income that far exceeds the cost of care. These types of contracts are perfect for private equity funds since they allow their portfolio companies to make regular debt payments and to pay regular fees and dividends to their owners and shareholders. In addition, in many arrangements where employers contract with providers like Bright Horizons to run an on-site facility, it is usually the employer, not the provider, who pays for the rent and upkeep of the facility—significantly lowering the providers' cost of care, and allowing them to pocket these savings as profits. In an industry where profit margins average 1 percent, Bright Horizons (2023) reported earning profit margins of between 15 to 25 percent from operating child care programs for employer clients.

**Providers who receive contracts from employers also gain an advantage over other programs by incentivizing families to chose their services over others'.** When employers provide on- or near-site child care programs for their employees but do not help parents cover the cost of other forms of child care, then employees must use the employer-sponsored programs if they wish to receive their child care benefit. Employers also restrict families' choices when they partner with local providers to reserve spots for their employees without allowing this benefit to be applied anywhere else. Similarly, employers can restrict tuition subsidies to approved providers—much as employer-provided health insurance distinguishes between in- and out-of-network health care providers. These types of restrictions make sense for employers since they allow them to get better prices from buying care in bulk and to form reliable partnerships with providers—but they undermine systemic goals for allowing families the freedom to choose their provider.

**Although employer funding is often depicted as an alternative source of financing for the child care industry—an argument that justifies public incentives to employers—this funding model risks favoring corporate child care providers to the detriment of local programs.**

**Employers are more likely to contract with corporate child care providers than with local programs or home-based providers** (Haspel 2024)**.** Corporate providers are particularly appealing to large employers that operate in multiple locations, since these employers can more easily offer standardized benefits to their employees who send their child to a program that belongs to a given chain or franchise. This allows employers to offer child care benefits without having to build relationships with local providers in every community in which they operate—while giving employees some limited choice in being able to select their preferred provider location, even if they are restricted to a single brand.

**In many communities, employer-sponsored programs risk diverting existing resources away from local programs and towards a more exclusive clientele as opposed to contributing to an expansion of supply**. Since the types of employees who receive child care benefits are more likely to be higher-income workers, employer-sponsored programs risk diverting families who could pay a good portion of child care costs away from local providers, thus undermining their revenues . Similarly, given the tight labor child care market, these programs likely are pulling workers from smaller, local programs, depriving them of staff (Haspel 2024a). If corporate providers are more likely to receive employer-sponsored contracts, then they are more likely to benefit from this system even as it weakens their local competitors.

**The strategic entry of corporate child care providers into this employer-sponsored market may therefore represent one of the more significant means by which corporate providers deprive local competitors of funding and skilled workers while profiting from the higher fees that employers are willing to pay.** Families who are employees of the companies that offer sponsored care are the beneficiaries of this system, but the other families in a community who cannot access these employer benefits lose if other local programs find themselves unable to compete.

### PUBLIC FUNDING

**Increased public funding for child care would, by design, allow corporate providers to profitably serve more families and communities.** Depending on how this money is structured, any profits that corporate providers earn will come directly from taxpayers or families (though co-payments and fees). If no limitations are placed on what providers can charge families as co-payments to public funding, then corporate providers would have every incentive to raise these fees without necessarily delivering a comparable increase in service quality or quantity.

**Allowing corporate profiteering from public funding would raise the cost of achieving the vision goals.** This would echo the way that public commitments to providing health insurance through Medicare and Medicaid has left taxpayers on the hook for covering spiraling healthcare costs. Families would no longer see the sticker price for care, reducing public scrutiny over high prices. If corporate providers gain ever increasing market share, as they have in other care industries, they would have more leverage to negotiate higher reimbursement rates from government—without providing a corresponding increase in supply or care quality (Batt, Appelbaum, and Nguyen 2023).

## II. PUBLIC FUNDING STRUCTURES

**Private equity investors are attracted to industries where they can predictably and consistently find high revenues, which are key to the functioning of their business model.** This preference for income predictability is, of course, true of most private investors and entrepreneurs, including small child care providers. Private equity investors, however, look for stable revenues that allow their portfolio companies to make regular debt, rental, dividend, and fee payments—thus allowing the funds to use leveraged buyouts, leasebacks, management fees, and other tactics to maximize their own revenues as owners while increasing their companies' operating expenses (Appelbaum and Batt 2020; Ballou 2023).

**Public programs usually pay flat fees to providers—be it through contracts or tuition payments—which can be exploited if providers get paid regardless of the quality or quantity of services they provide.** In the hospice industry, for example, Medicare pays a flat per-diem fee, even though the amount of care a patient needs from providers will vary day-by-day.[10] Bazell et al. (2019) found that relative to for-profit hospice providers, nonprofit providers offered 10 percent more nursing visits, 25 percent more social worker visits, and twice as many therapy visits. Similarly, both Medicare and Medicaid pay non-negotiable per-diem rates to nursing homes for every day that patients receive care. Gupta et al. (2021) found that after nursing homes were bought by private funds, homes increased their reliance on lower-paid and less-certified staff

[10] Patients generally require more intensive care for the first and last few days that they are in hospice care, but may not even need daily visits in the interim.

(certified nurse assistance and licensed practical nurses) rather than registered nurses.

**As will be discussed more in Section IV, the best guardrails against these types of behavior are funding conditionality and industry-wide quality standards.** One example of these are the new staffing requirements that the Centers for Medicare & Medicaid Services (CMS) introduced for long-term care providers, including nursing homes (CMS 2024). The child care industry is fortunate to already have some protection through its staffing requirements, but corporate providers who benefit from flat-fee revenues may still find other means cutting their operating costs in ways that can undermine care quality or worker wellbeing (see Section III.4). In particular, expanding contract-based funding, which is not tied to enrollment or attendance as in other health care sectors, will require policymakers to define what, in terms of staffing or other facilities, they expect providers to supply in return for this money.

**Public funding (or private insurance) that provides additional fee-for-service payments for programs that supply additional services, such as therapy to children with disabilities, can be vulnerable to different forms of abuse.** In the autism services industry, for example, employees working for private-equity backed providers were more likely to report being pressured to bill for more hours per patient than was medically necessary (Batt, Appelbaum, and Nguyen 2023). The policy challenge here is in expanding children and families' access to critical services while limiting opportunities for the providers of these services to fraudulently claim higher reimbursement rates—and to do so without punishing families for providers' abuse of the system.

## III. ASSET SALES

**Private equity funds can access the value of companies' real estate assets by forcing them to sell their properties, and rent them back from their new owners—a tactic known as a "sale-and-leaseback."** Leasebacks are particularly important in sectors, such as retail or nursing homes, where real estate constitutes a company's primary asset. Not all child care providers own their own facilities, but in an environment of high real estate prices, these businesses may be particularly attractive to corporate investors who otherwise have little interest in the low-margin child care market. Although more research is needed about the use of this tactic in the U.S., leasebacks are already recognized as a core component of the corporate child care business model in the U.K. (Simon et al. 2022).

**When child care providers own the properties in which they operate, this real estate is often their business' most valuable asset—one which can be sold to generate immediate revenue for new corporate owners.** As seen in other sectors where private equity has used this tactic, corporate owners are unlikely to reinvest the value of the property sale back into the business, preferring instead to pocket it as an immediate return on their investment, or using it as a form of collateral to access more debt to make more acquisitions (Ballou 2023).

**Meanwhile, this tactic leaves the local program paying rent to keep using the facilities they once owned—a new regular expense that, like the debt payments and management fees, will require that they spend their income on paying financiers before their own workers, and may ultimately make it impossible for them to stay open in the long term.** For example, Gupta et al. (2021) found that nursing home lease payments on their facilities increase by an average 77 percent after a private equity buyout.

**Real estate sales are an easy way for private equity to extract wealth from an industry that may otherwise seem unprofitable.** This tactic can be fatal to providers who depend on the stability of owning their facilities to manage their expenses, but real estate and other asset sales frequently allow private equity owners to profit even if the local businesses that they acquire go bankrupt. Ultimately, this tactic is most harmful to the workers whose wages may be pushed down to pay new rental expenses, and to the families who depend on the child care providers who may have to close their businesses due to this added expense.

## STEP 4: LOWER EXPENSES

### I. LABOR COSTS

#### WAGES

**Private equity owners across industries actively work to keep wages, benefits, and other labor expenses as low as they can** (Appelbaum and Batt 2014). This behavior would run counter to ongoing efforts to improve child care job quality and to raise providers' incomes above poverty levels, and risks stalling, if not reversing, any progress in this area. A particular concern may be private-equity backed franchises, since these types of employers are notorious for their labor rights violations, including wage theft (Ash 2021b).

**Wages and benefits, of course, will vary based on local minimum wage requirements, but private equity owners can already do a lot of damage to workers by keeping wages at existing levels.** For now, corporate providers appear to be paying comparable, if not slightly higher wages relative to the rest of the industry, especially since they are more likely than other employers to afford to provide benefits such as health care. This is likely due to these providers needing to keep wages high enough to attract workers in a tight labor market where wages, even in sectors such as fast food, have been rising. Corporate providers can keep up with wage inflation without cutting into their bottom line so long as they can pass the costs directly on to their consumers.

#### SCHEDULING

**Beyond directly holding down wages, private equity behavior elsewhere in the care economy reveals other tactics that corporate providers can use to minimize labor costs.**

**First, corporate providers can cut staffing levels down to the bare minimum, even if this requires remaining staff to work longer or more unpredictable hours.** This has been a common tactic observed among private equity-owned nursing home providers, where staffing rates fell by 1.2 percent on average after private equity buyouts, and the remaining nurses were required to work more overtime hours (Gupta et al. 2021). In the child care space, this behavior will be constrained by local child-staff ratio requirements. However, workers have posted on online forums about corporate providers who send staff home at the start of, or even during shifts if low attendance (or early pick-ups) reduce the number of staff legally required to be in the classroom.

**Without changing wages, private equity owners can, as much as state staffing requirements allow, shift towards employing more workers in lower-paid roles, such as assistant teachers (rather than lead teachers) or teachers without advanced credentials.** As seen in the nursing home industry, private equity owners may increase the share of lower-paid workers that they hire, and demand that assistant teachers, for example, take on more of the responsibilities that normally would be delegated to lead teachers (Gupta et al. 2021).

**Alternatively, private equity owners can rely on part-time workers and just-in-time scheduling systems that would help them avoid paying for benefits while pushing down their variable costs.** These tactic may be facilitated by new apps, like Tandem, that facilitate algorithmic scheduling and turn caregiving into a f orm of gig work. This use of algorithmic scheduling apps is being introduced in various health care settings, including nursing homes and hospitals, to hire certified nursing assistants. These apps allow workers to see which shifts local providers need filled, along with the minimum base pay; they then submit a bid to fill a shift, along with an offer for how far above the base pay they wish to be paid. These systems effectively pit workers against each other so that they push their own wages down, while creating opportunities for providers to pay unequal wages for equal work (Wells 2024). In child care, these apps may be designed to help providers find temporary substitute teachers to maintain staff-child ratios—but this implicitly makes it easier for any provider to meet regulatory staffing requirements while increasing their reliance on short-term, low-paid workers who work without predictable schedules.

### II. QUALITY INVESTMENTS

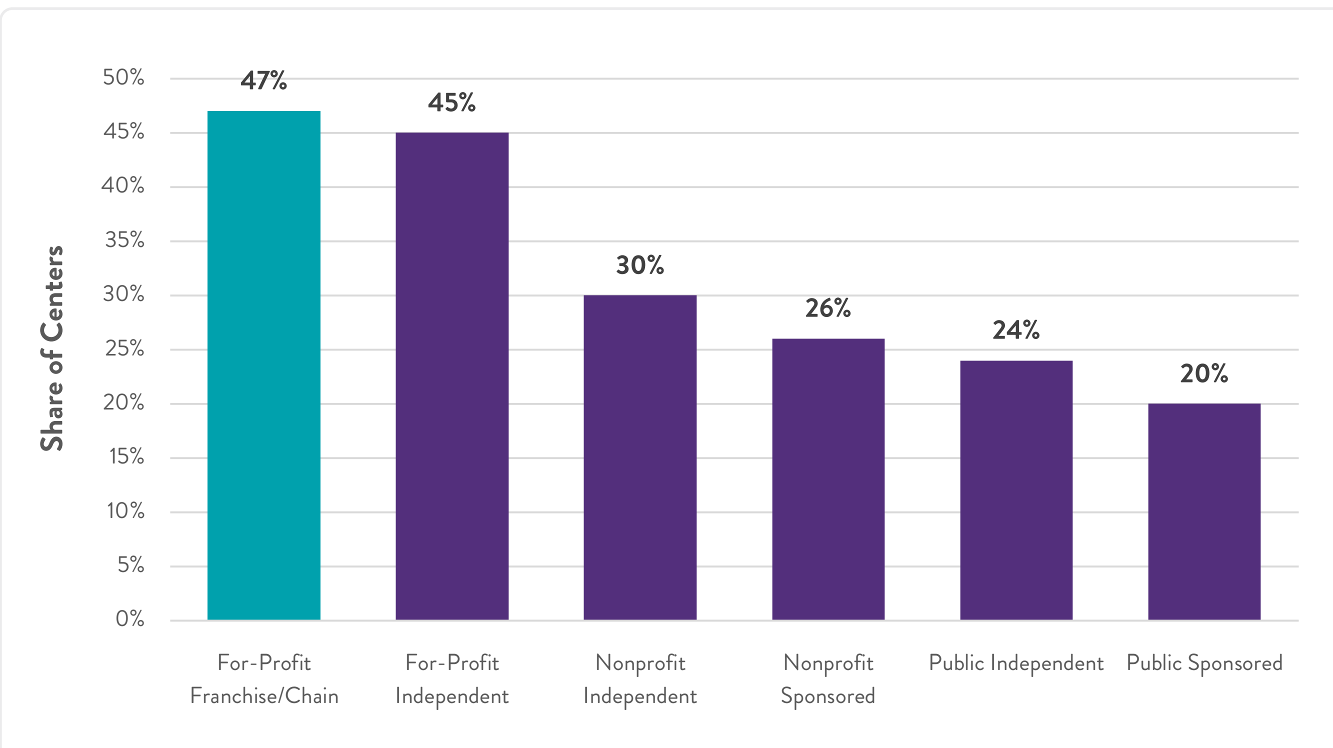
**Corporate providers have an incentive to meet official quality requirements in order to maintain enrollment levels.** Corporate centers are therefore likely to be registered and licensed at the state level, and will pursue voluntary accreditation through organizations such as the National Association for the Education of Young Children (NAEYC) or Cognia.

**However, corporate tactics, especially around labor, undermine quality in ways that are not always reflected in these standards.** The quality of child care is heavily dependent on the strength of the relationships that children build with their caregivers—relationships that deepen with the time that children and caregivers spend together. Children also need stability in their environment if they are to feel safe and comfortable enough to engage with the world with curiosity. By forcing caregivers to work long or irregular hours for low wages, private equity owners risk increasing worker turnover rates, and may even convince some caregivers to exit the industry entirely—two dynamics that have been observed in other care sectors that saw large inflows of private equity investments. In 2019, 47 percent of for-profit centers run through a franchise or chain experienced “high” turnover rates of over 20 percent—a greater share than any other ownership type (Amadon, Lin, and Padilla 2023) (see Figure 4). The higher turnover rates—as well as the part-time and algorithmic scheduling—reported in corporate child care providers should be considered a sign of lower quality, since this churn results in children being constantly being introduced to new caregivers and teachers, never having the chance to form bonds of trust with caregivers, and being forced into an unpredictable environment in which learning is harder.

**Corporate providers can also undermine quality by under-investing in other supplies.** Elsewhere in the care economy, private equity-backed providers have relied on cheaper facilities, cheaper equipment, and even cheaper food options (Appelbaum and Batt 2020). Most child care providers must depend on inexpensive supplies given their tight operating margins. However, this behavior among corporate providers may undermine efforts to advance the vision for child care if it runs counter to public expectations that increased funding will go towards investing in higher quality supplies and facilities—an outcome that is more likely if these expectations are not made explicit in funding legislation or if they are left unenforced.

**Corporate owners can also reduce quality in less quantifiable ways by requiring providers to prioritize activities or outcomes tied to revenue, such as enrollment rates, rather than actual quality.** For example, program directors in private equity-owned companies report being pressured to prioritize raising

**Figure 4:** Share of Centers Classified as High Turnover (2019)




***Source:*** *Amadon, Lin, and Padilla (2023)*

***Note:*** *“Sponsored” non-profit and public programs are those operating with the support of another organization or agency, such as a public school district* enrollment rates above all other considerations, leaving them with little time to oversee the day-to-day management of their centers. Similarly, easily quantifiable requirements—such us that caregivers send parents photographs of their children every hour—can allow providers to give the impression of providing high quality care to parents while reducing from the quality time that care workers spend with their charges (Haspel 2024b).

**Finally, providers can reduce their costs by providing more standardized care to all children to the point that they reduce caregivers' freedom to modulate their activities based on the individual needs of each child.** In the autism services industry, for example, workers at private equity-owned providers were more like to report being pressured to standardize the treatment plans they offered to autistic children (Batt, Appelbaum, and Nguyen 2023). This would be a particular concern for children with disabilities or chronic conditions for whom providers must be willing to provide physical accommodations, engage the child using their assistive technology, or otherwise remain flexible and attentive in supporting the child's unique growth and development.

## III. VERTICAL INTEGRATION

**To decrease spending on supplies, large companies can buy suppliers and absorb them into their operational infrastructure.** In child care, this could include acquisitions of companies that provide curricula or online management portals. For example, in 2020, Bright Horizons acquired Sittercity, an online marketplace that helps families find local and online care providers (Nasdaq 2020). These types of deals can directly reduce providers' expenses since they can access inputs at-cost as opposed to having to fund their suppliers' profit margins.

**Private equity funds can also facilitate integration across their portfolio companies, requiring that the companies buy exclusively from other companies in the portfolio** (Ballou 2023)**.** This allows the private equity firm to profit from its portfolio companies' expenses, and to get around regulatory caps on profits. For example, in the home health care industry, insurance companies offering Medicaid Advantage plans can get around this program's cap on administrative costs and profits (to 15 percent of premiums) if they own both the home health aide (HHA) providers whose services their reimburse and the pharmacy benefit managers (PBMs) who sell the HHAs medicines and other supplies. The HHA company must pay an inflated price for its supplies and counts as spending on patient care according to Medicaid Advantage, even though the PBM and its insurance owner makes a profit from the mark-up (Appelbaum, Batt, and Curchin 2023). Vertical integration also benefits private equity funds because it offers one company a guaranteed source of demand, irrespective of the quality of its products, which can help them gain greater market share. Meanwhile, the purchasing company may benefit if the supplier agrees to favorable deals, but they may also be forced to abandon suppliers that better meet their needs.

**Both forms of vertical integration create an anticompetitive dynamic that harm competing providers and suppliers.** Independent child care providers and child care program suppliers must now compete with private-equity companies that have sources of guaranteed demand, or underpriced supply.

**Vertical integration is difficult to document in child care since there is little transparency about which companies share a common private equity owner, even when they operate in the same or related sectors.** This type of self-dealing has the added advantage for private equity investors of allowing them to profit from both the buyer and seller side of a market transaction.

**One particular concern for the child care industry is the risk of corporate investment in the private companies that state governments contract to oversee their QRIS programs.** Depending on the state, these private contractors can be responsible for identifying the metrics that will be used for QRIS and for inspecting and scoring providers according to these metrics—effectively acting as gatekeepers for whichever benefits providers receive from higher QRIS scores (e.g. higher trust among parents, or even higher reimbursement rates from the state). Private equity funds or other corporate entities do not need to have bought QRIS companies outright for them to be able to build relationships with them or their owners; there is currently little transparency about these contractors that could help identify potential conflicts of interest.

## STEP 5: UN-LEVELING THE PLAYING FIELD

### I. CORNERING THE MARKET

**Corporate providers can drive small providers out of the market to leave families with no choice but to use their services.**

**As seen in other sectors such as physician practices, provider diversity drops when multiple local enterprises either get rolled up or converted into franchisees.** Child care is usually understood as a highly fragmented market that offers families with a diversity of provider options, especially when seen from the national level. However, the health of child care markets are better studied at the local level since families realistically will restrict their search for care to providers near their homes, offices, and communities. Thus, a child care chain that looks relatively small at the national level can still become the dominant provider within a given community and local market, threatening the provider options of local families.

**The growth of chains in local communities can often go undetected in state- or national-level data give how small child care enterprises are.** Normally, federal and state-level antitrust enforcers are empowered to prevent acquisitions that threaten consumer choice and market fairness, including at the local level. However, the value of each child care acquisition in a roll-up is often so small that it does not have to be reported to antitrust authorities, leaving regulators unaware of the extent to which companies control local markets. This has been widely observed in other care sectors, including for local physicians' practices, dental clinics, and even veterinary providers (Chopra 2020).

**Even the providers who do not get bought up can be harmed from the growth of a corporate chain or franchise in their community.**[11] Corporate providers will compete with others in the community for both workers and demand, and then they have the advantage of being able to access financial resources (through debt) to fund marginally higher wages and marketing campaigns. Corporate providers often cycle through their workers more quickly than other providers, but they can undermine the care quality and stability of their local competitors simply by causing then to experience more churn among their staff. Furthermore, in mixed-income communities, corporate providers who target wealthier families or employers can deprive smaller providers of clients able to pay the full cost of care or otherwise subsidize the care of their lower-income neighbors.

**Once corporate chains have become the dominant provider of a community, they can use monopolistic tactics to increase their profits.** As noted throughout Section III, many of the greatest risks from private equity and other corporate providers emerge once families do not have alternative providers that they can turn to. In 2023, the Federal Trade Commission (FTC) filed an antitrust suit against U.S. Anesthesia Partners (USAP)—a portfolio company of the private equity firm Welsh, Carson, Anderson & Stowe—alleging that they had intentionally reduced competition and raised prices in the Texas anesthesiology market by buying up most of large anesthesia practices in the state; they are also alleged to have struck deals with competitors to either drive up prices or else keep them out of the local markets under USAP control.[12]

### II. LOBBYING

**Corporate providers will leverage their financial resources and market power to influence the policymaking process to ensure that child care markets continue to enable their profit-maximizing tactics.** For example, in the real estate industry, corporate landlords, who are often on the boards of the industry's trade associations, worked through these

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[11] This likely includes home-based providers, who otherwise may not be concerned about the roll-ups of local care centers, although more research is needed on the indirect impact of private equity investments on these types of providers. In particular, home-based providers may be harmed by private equity investments in the real estate industry, which has contributed to rising rents.

[12] Originally, this case was also brought against the private equity firm Welsh, Carson, Anderson & Stowe as well as USAP. However, a federal district court granted the private equity firm's motion to dismiss it from the lawsuit, leaving only the case against their portfolio company (Scarcella 2024). This highlights the challenge of holding private equity funds accountable for the tactics their portfolio companies use to provide them with profits.

organizations to lobby against policies such as eviction moratoria, just cause eviction ordinances, and rent regulation during and after the COVID pandemic (Bankson et al. 2024). Corporate child care providers already have a significant lobbying and political presence in Washington through organizations like the Early Care and Education Consortium.

**Corporate providers and other advocates can both agree on the need for robust and sustained public funding for child care and early learning.** The differences will likely emerge in the shape of that funding and the rules that govern it. We can expect corporate child care providers to lobby in three key ways:

- **Protecting profitable markets.** Corporate providers are profiting from serving higher-paying and employer-sponsored families, and they will resist policies that make their activities in these markets redundant—such as those creating a universal, publicly-funded system that caps family contributions and cuts out employer sponsors. They will likely try to stall a transition towards a more universal system until they can gain enough local market share to argue that they cannot be removed from the sector without causing harm to families.
- **Shaping public funding.** Corporate providers will seek to convince policymakers to distribute child care funding in ways that allow them to use part of this money to maintain profits. Given the preference from all stakeholders in this industry for a contract-based payment approach, corporate lobbyists will likely focus on limiting the guardrails placed on this funding, including around proof-of-service-delivery, family co-payment caps, disclosure requirements, or limits on profits. In communities where they have higher market share, corporate providers will also push for higher public payment rates that cover both their operating costs and profit margins (Batt, Appelbaum, and Nguyen 2023).
- **Preventing increased expenses.** Corporate providers will resist efforts to raise wages of early educators through new minimum wage or fair scheduling requirements in the sector or collective bargaining protections.

## STEP 6: SALE & EXIT

**Private equity funds sell their portfolio companies within an average three to five years after first acquiring them, and will look for whatever buyer is willing to pay the highest price for them.** Private equity funds can therefore try to bring a company public through an IPO, can sell them to be merged with a corporate competitor, or can sell them to another private equity fund in a secondary buyout. The small business owners who sell their enterprises to private equity-backed companies may continue to work as caregivers or managers, but they will lose any control over who the next buyer of their business will be (Batt, Appelbaum, and Nguyen 2023).

**Acquisition by a private equity fund thus places providers on a one-way track for long-term corporate control.** From the perspective of private equity funds, the purpose of rolling up small providers is to create an entity that will interest larger buyers—in other words, being the first step in consolidating the industry into larger chains. Even growth equity funds who are more committed to generating value for local communities will be looking to sell to the highest bidder. Strategic buyers who are pursing a growth-through-acquisitions strategy are often willing to pay a premium to buy these smaller chains, since their value comes less from their cash flow and more from the market share they provide.

**The process of being acquired by new corporate owners every few years will weaken providers and undermine the quality of their services.** Six of the top 10 child care providers are on their second set of private equity owners, with Cadence Education notably sold two times since its initial private acquisition in 2007 (see Table 1). Each time that a company is bought out in this way—especially if repeatedly sold to private equity-backed companies—they usually take on new debt and have to undergo management and operational changes, increasing the instability within their programs. This creates more churn within the company, along with increased uncertainty about job stability, that leads to more staff turnover and risks deteriorating the quality of its products. As the company is stripped of more of its assets, and its value falls, it is harder for its owner to find a viable buyer—other than, perhaps, another private equity fund. For an industry where quality is dependent on stability, these repeated changes in ownership should be considered threats to service quality.

## CONCLUSION: PUTTING PROFITS BEFORE CHILDREN

**A well-funded child care industry will likely display many of the attributes of industries that attract private equity investors and other corporate stakeholders.** To start, the extreme fragmentation of child care markets creates the same opportunity for private equity investors to profit from roll-ups and other consolidation tactics that they have used elsewhere in the care economy. Second, child care is a service that is in high demand, and even without adequate public funding,  certain families and employers are able to pay high profit-generating fees—therefore, simply capturing this small functional segment of the child care market makes business sense. Finally, corporate investors may try to buy up child care providers in anticipation of increased public spending, either from states or the federal government, that would expand the share of families that they could profitably pursue as customers. By expanding their presence in child care markets, corporate providers not only increase their opportunities to receive public funding when it materializes, but they can also argue that they represent the type of provider best suited to meeting the public's child care needs.

**Left unchecked, corporate child care risks threatening all five of the industry's vision goals:**

- **Access.** Experience from other industries and countries indicates that private equity investments in child care are unlikely to significantly contribute to an expansion in supply. Corporate providers may be rapidly growing, but this is often through roll-ups and other acquisitions which simply converts existing supply into supply under their direct control. Corporate providers may also redistribute resources towards communities that can pay the full cost of care, offsetting any new centers they create in higher-paying communities with closures elsewhere. To the extent that these companies are also drawing staff and other resources away from the providers who serve lower-paying communities, corporate providers may at once be leading to the consolidation of the child care industry as well as the concentration of it services for wealthier families and employer clients.
- **Affordability**. Absent guardrails on funding, corporate providers will raise prices, co-payment rates, and fees as much as they need to maintain their profit margins, passing any changes in their operating expenses directly on to families and employers. If public spending increases to cover providers' operating costs, then corporate providers will seek to raise this public payment rate as high as they can, deriving their profits from taxpayers**.** These higher prices are unlikely to result in a commensurate increase in quality or supply.
- **Provider Wellbeing.** Corporate providers may provide comparable, if not slightly higher wages than their small, local competitors, but they will actively resist efforts to improve overall job quality for early educators, including through standards on public funding. They are also likely to increase their reliance on part-time staff, or turn to just-in-time scheduling to maintain staff-to-child ratios—even if this reduces job quality.
- **Quality.** Corporate providers will seek to maintain outward signs of quality, especially if they focus on wealthier communities and employers as their clients. However, their emphasis on quantitative metrics of quality and profitability—such as enrollment—may lead them to disregard the important human connections that constitute good caregiving. Most importantly, corporate tactics that undermine caregiving job quality will, all else being equal, directly lead to inferior quality care through higher staff turnovers and more tired and stressed caregivers.
- **Provider Diversity.** Corporate growth tactics that depend on acquisitions, roll-ups, or conversions of existing providers into franchisees all contribute to the corporatization and concentration of the child care industry. If their entry into local communities subsequently deprives smaller providers of skilled caregivers or higher-paying families, they may push smaller providers out of business. And, by reducing families' ability to find non-corporate providers, these companies will have more freedom to use uncompetitive tactics to prevent new entrants.

**Underpinning all of these risks is the concern that corporate providers could capture the industry if they are allowed to control a significant share of child care markets.** Once corporate providers become the dominant players in either local or national markets, leaving families and employers with few alternative providers to choose from, then they will have more power to structure markets around their profit goals as opposed to the priorities of all the other stakeholders who depend on the industry.

**Paradoxically, the same funding that will attract more corporate providers to child care is essential to slow the collapse of non-corporate providers in the industry.**  Without public support, small- and medium-sized providers will continue to close due to the near-impossibility of earning enough revenue to cover the true cost of care. This will leave corporate providers with an ever growing share of the market, especially in the communities and employer-sponsored sectors where revenues are high enough to support profits. If policymakers delay too long, they may have little choice but to depend on corporate providers to supply care for all families, irrespective of whether this is truly in the best interest of families, workers, employers, and communities.

**Once policymakers do decide to increase support to this industry, they must structure this funding in a way that guards against corporate capture and profiteering.**

SECTION 4

# A STRATEGY FOR ALIGNING MARKETS WITH THE CHILD CARE VISION

# SECTION IV
# A STRATEGY FOR ALIGNING MARKETS WITH THE CHILD CARE VISION

**Policymakers and other stakeholders have a responsibility to design a child care system that creates market structures, incentives, and guardrails that align with the vision for child care as a public good.** Such a strategy must include setting expectations about how public funding must be used before it can be diverted towards profits; setting and enforcing quality standards that protect children and workers; protecting competition and provider diversity, including by providing support to non-corporate providers; and building countervailing power among the various stakeholders in this industry who have an interest in holding corporate providers accountable to the child care vision goals and the new rules of this industry.

## STEP 1. PREVENT ACQUISITIONS

**The first step towards limiting the encroachment of corporate child care is to limit the number of existing providers who get acquired through roll-ups or conversions into franchising.** Acquisitions are taking place because small, non-corporate providers are voluntarily selling their businesses to corporate investors. Non-corporate providers may have a number of reasons for selling to a private equity-backed company, and thus, limiting this trend will require providing these providers with alternate means of accessing the resources that corporate owners purport to offer them, such as access to financial capital, economies of scale, name recognition, and/or a means of exiting the industry.

### I. INCREASE ACCESS TO CAPITAL (PUBLIC FUNDING & SMALL BUSINESS LOANS)

**Corporate child care providers have a market advantage given their ability to access large amounts of financial capital, especially by taking on more debt.** However, debt financing remains risky for companies in the child care industry given their low margins and given that one-time debt-funded investments in facilities or staffing often have only a marginal impact on providers' revenues and ability to repay their loans. Although non-corporate providers are more likely to use debt to fund investments that advance the vision goals—such as start-up costs for a new enterprise, or investments in facilities, supplies, or workforce training—they do not have the positive cash flow to be able to pay off this debt, and thus do not qualify for many existing loans. Corporate providers, on the other hand, are more likely to use debt to acquire new companies, and are able access credit on the promise of growth through acquisitions, even though their use of debt threatens the business model of the companies they acquire, and the stability of child care markets as a whole.

**Enterprise owners who sell their businesses to corporate chains may hope that their new parent company will invest more resources towards making the long-term investments in facilities, supplies, and the workforce that they cannot make independently.** This view is misguided since neither the private equity nor franchise business model encourages investments in rolled-up local providers, and most corporate debt goes towards acquisitions rather than long-term investments. Nevertheless, this perception that corporate ownership offers greater financial stability persists.

**Greater public funding for child care is an important first step for reducing small providers' dependence on private equity for access to capital.** To start, this money will help stabilize providers' revenues and allow them to make long-term investments in their own operations. Furthermore, if this funding is large enough to provide providers with a positive cash flow, they will be better able to qualify for loans, including those available through Small Business Administration (SBA) programs.

**In addition to properly paying providers, policymakers can proactively help non-corporate child care providers access loans and other forms of capital.** One model for this is the SBA's recently announced program to provide targeted support to child care providers through its Women's Business Center program (White House 2024). Beyond increasing providers' access to capital, this initiative increases efforts to provide more guidance to child care providers about existing resources that may be available to them. State and local governments may also consider grant and forgivable loan programs for child care providers who use these funds in ways that help their child care industry transition towards a higher-quality future, such as opening new child care enterprises, making investments in upgrading or repairing facilities, funding teacher trainings, or even starting up new child care enterprises. Finally, policymakers and the HHS can consider reform to CCDBG that allows this funding to go towards capital upgrades.

**Small Business Investment Companies (SBICs), who administer SBA loans, could act as an important alternative to private equity as a source of financial capital for small businesses.** Rather than invest in businesses directly, the SBA licenses and contributes funding to private SBICs alongside other private investors; SBICs then invests in small businesses through combinations of debt and equity (Small Business Administration 2024). SBA loans are structured to offer long amortization without balloon payments, allowing small businesses to finance their capital needs over multiple years without facing a deadline by which they have to repay the loan or face a surge in costs. Since SBICs are cash-flow lenders, a business' eligibility[13] for an SBA loan is based on their ability to repay that debt through their regular revenues as opposed to the ownership of assets that they can present as collateral. This will benefit child care providers, many of whom do not have significant capital or real estate assets to use as collateral. Yet the SBA's focus on cash flow underscores the importance of public funding as a prerequisite for supporting child care providers in the long term.

**Community Development Financial Institutions (CDFIs) are another form of alternative financing that child care providers could turn to once they receive more public funding.** CDFIs are private or nonprofit lenders—banks, credit unions, loan funds, and venture capital funds—who provide financing to communities that are under-served by the traditional financial system (Opportunity Finance Network 2024). Many CDFIs target specific industries or regions, but those that are mission driven around supporting a given community, or who focus on providing equity funding to small businesses, could be of interest for child care providers.

**Finally, local policymakers and advocacy organizations should consider investing in public education programs around these alternative financing opportunities.** Organizations that work with child care providers can point them to resources such as those available through Small Business Development Centers and through SCORE, a publicly-funded network of technical advisors prepared to help entrepreneurs and program owners make the necessary changes or follow the correct steps to apply for credit from SBICs and other lenders.

## II. GAIN ECONOMIES OF SCALE (SHARED-SERVICE ALLIANCES)

**Another significant appeal of corporate ownership is that it allows programs to benefit from economies of scale and thus lower their operating expenses.** Programs that are part of the same chain can centralize and outsource business operations such as insurance management, enrollment, accounting, scheduling, marketing, or food delivery. This is particularly appealing in an industry where many business owners are more interested in the work of caregiving than in business management.

**In order to replicate these economies of scale outside of the corporate context, child care providers can join shared-service alliances, including through as co-ops or other nonprofits.** These alliances help their members lower their operating costs by splitting the expense of accessing services and or centralizing administrative roles (Opportunities Exchange 2021). For example, Early Learning Ventures helps its network of child care providers navigate licensing and compliance, as well as offers tools such as online enrollment and attendance tracking. The shared-services route towards scale would likely be slower than the corporate one, but the advantage is that small providers would remain independent, autonomous, and able to exit the partnership. This means that any savings that providers earn from joining the alliance can be used in ways that advance the vision goals as opposed to being diverted to corporate profits.

[13] Providers are no long eligible for SBA loans once they are acquired by a larger chain—however, franchisees remain eligible for this funding since they are technically independent businesses. In assessing franchisee suitability for SBA loans, the loan providers will review these programs' operating agreement with the franchisor, and will look for any signs that this agreement includes any language that is overly restrictive or prevents the franchisee from operating a profitable enterprise. Of course, franchisors are familiar with SBA rules, and draft these contracts in ways that allow their franchisees to remain eligible for this funding. Thus, the SBA effectively subsidizes the franchise business model.

**Shared service co-ops and other alliances are nonetheless difficult to organize in the child care industry since they can require providers to contribute initial funding in order to access the shared services**. This is a challenge given how few providers have discretionary earnings to spare for this type of investment. To increase the feasibility of these organizations, local governments or philanthropists could subsidize a handful of services for alliance members—or could subsidize the service hubs themselves—allowing providers to realize the gains from cooperation, and build trust in the shared entity, without having to risk an initial down payment. These entities would also become a lot more viable if public funding were to increase enough for them to reliably generate the income needed for their owners to join co-ops and alliances without external support.

**One way for policymakers to support child care providers irrespective of the status of public funding would be to provide these services for free or at reduced cost through public technical assistance programs** (see Section IV.4).

## III. ATTRACT CLIENTS (PUBLIC REGISTRIES)

**Another reasons why providers may join corporate chains is in order to benefit from the brand-name recognition of the company or franchise.** Brand-name appeal for child care may be less important than other franchise-intensive industries, like fast food, but providers may still benefit from the perceived uniformity of care and quality of a corporate chain if families come to trust a given brand. Furthermore, being part of a chain can also allow providers to attract employer-sponsored clients whose benefits packages only allow them to buy care from a limited number of "in-network" providers or brands.

**Non-corporate providers may not need to build a brand name outside of a limited community context, but they can benefit from public databases or registries that help local families know about their service offerings, and track information such as ownership, size, and openings.** Beyond funding providers, a critical government responsibility in child care markets is that of providing families with timely information about the availability, pricing, and quality of local providers. Many states have started building such systems through their licensing or QRIS programs—and federal CCDF regulations require state to provide information on child care providers through a "consumer-friendly and easily accessible" website—but these initiatives are usually underfunded and incomplete; only 13 states have budgeted for and created a dedicated system for communicating QRIS scores with the public (Herbst 2022). Finding a child care center through a corporate chain's website is thus often easier than searching through the public database. States and local governments should invest in existing child care registries and referral agencies, and must ensure that the government administrators of these registries know how to make them search engine optimizable.

## IV. FIND ALTERNATIVE BUYERS (WORKER CO-OPS)

**When the owners of child care businesses need to sell—often because their savings, including their retirement, is tied up in the value of their business—workers can be an alternative buyer to private equity.** If this succeeds, then the original owner receives the value of the business in payment, and the workers become the joint owner and operators of the enterprise. This grants them greater control over their working conditions, and allows them to build equity through business ownership—thus keeping the wealth of the enterprise, limited though it may be, in the community. If owners sell to a worker cooperative or an employee stock ownership plan (ESOP), they may also benefit from Section 1042 of the U.S. tax code, which allows them to defer their capital gains tax on the sale, so long as, among other requirements, the proceeds are reinvested in a qualified replacement property (e.g. stocks or bonds in U.S. companies) within a specified period of time.

**The biggest barrier to workers being able to buy out their employer is the challenge of raising the money they need to make this purchase.** Unfortunately, whereas private equity can apply for a loan while using the value of the entity it intends to buy as collateral, workers interested in making the same purchase cannot list the business as an asset in their loan applications. Instead, lenders will usually look at workers' personal income as child care providers to assess their suitability for a loan. Unsurprisingly, child care workers' incomes are so low that they often cannot secure the funding they would need to become joint business owners.

**To support the creation of worker-owned co-ops in the child care industry, policymakers would need to increase the means through which child care workers can access funding.** CDFIs already act as a potential funder for this type of ownership transfer. The SBA could also change its lending conditions to exempt workers trying to create co-ops from requiring a personal income guarantee, much as they do for those creating employee stock ownership plans. Public technical assistance resources, especially those that target child and home care, could also expand their support of cooperative development.

**Finally, if policymakers want to encourage worker buyouts as a private equity alternative, then they should support information and technical assistance schemes to support owners and workers through this process.** In particular, owners need to be aware that these buyouts are an option for them, and to have support in making succession plans well in advance of their planned retirement or sale. The workers should also receive support as they transition into their new ownership responsibilities.

## V. BLOCK EXPANSION (ANTITRUST ENFORCEMENT & LICENSING LIMITS)

**When roll-ups persist and a single company gains disproportionate control over a local market, antitrust enforcers are empowered to block or add conditions to that company's proposed acquisitions.** Enforcers are capacity-constrained and cannot prevent all roll-up acquisitions, but they are empowered to intervene when a chain gets so big that it threatens the competitiveness or structure of local markets. Antitrust enforcement has not yet been mobilized to preemptively counter private equity-backed roll-up trends, but federal regulators are paying more attention to this space as evidence grows about the consequences of roll-ups in other sectors (FTC 2021; Polsinelli 2024). This suggests that this may be a tool that child care advocates can leverage moving forwards. State regulators also have their own state merger laws that grant them the authority to monitor and protect local market diversity.

**The biggest barrier to antitrust enforcement of roll-ups is a lack of information.** Companies must notify regulators of proposed mergers and acquisitions, but only if the value of the transaction (and in limited cases the size of the parties) exceeds a given threshold ($119.5 million as of 2024). As a result, even when a large company is pursuing roll-up tactics, it does not need to disclose each acquisition of an individual local provider. This does not mean that enforcers cannot intervene to preemptively block an undisclosed merger,[14] but they need to be aware of the deal and its potential threats to competition in order to act in the short window of time between when a merger is announced and actualized.[15]

**Regulators may also consider restricting how much of a state or local market a given provider is licensed to serve.** In the case of corporate providers who wish to create new supply in a community where they already operate, regulators would need to balance demands for increased supply and market diversity. That said, a cap on the share of a local market that a given company can serve would at once restrict future acquisitions of existing providers, incentivize entrepreneurs to start new independent enterprises rather becoming franchisees, and restrict employers' ability to only contract corporate providers for their on-site care facilities—thus simultaneously restricting corporate providers three means of dominating markets.

**All of these tactics would require state child care regulators to take greater responsibility for monitoring child care market competition and provider diversity.** State health care regulators commonly monitor company ownership and concentration risks in markets such as the hospital sector, given the potential consequences that unfair market practices or business failures could have on local health outcomes. In light of the systemic importance of child care to local communities, and the inclusion of provider diversity as a vision goal for the sector, states should be similarly concerned with protecting the health of child care markets as they are in other care sectors. State regulators can monitor market diversity through their licensing systems, which should require providers to disclose their owner, ultimate parent entity, and investors in that entity, and should work with state competition policy

[14] Notably, the Department of Justice and Federal Trade Commission's 2023 Merger Guidelines specified that when a merger is part of a series of acquisitions (as in a roll-up), federal regulators are empowered to consider the cumulative impact of the series in determining whether the next acquisition, even if small and unassuming, should be blocked. These guidelines are not binding, but they set the standard for how federal and state regulators interpret evidence of risk or harm.

[15] There is no statute of limitations on merger lawsuits, and regulators can unwind a merger once it has taken place, but they are generally reluctant to pull apart companies out of concern of *possible* harms. That said, regulators may still require chains to divest themselves of some or all of their centers in a given local market if evidence of harm emerges (see Section IV.4) (Kwoka and Valletti 2021).

authorities to more closely monitor communities where one or more corporate providers control a disproportionate share of the market. Given that the current role of state child care regulators is very focused on child health and safety, this would require the hiring and training of a new set of regulators with the skills to monitor the health of child care markets.

## STEP 2. BUILD COUNTERVAILING POWER

**Stakeholders in the child care industry—including workers, families, and non-corporate providers—all depend on building an industry that supports the five vision goals**. If properly empowered and mobilized, these stakeholders can help push back against corporate efforts to put short-term profits over other priorities, including child wellbeing and the growth and long-term financial stability of the sector. This power will be one of the child care industry's greatest protections against the ownership and managerial structures that corporate providers use to shield themselves from liability or oversight.

### I. MAGNIFY STAKEHOLDERS' EXPERTISE (INDUSTRY COMMITTEES & ADVOCACY ORGANIZATIONS)

**The extreme fragmentation of the child care industry translates into fragmentation among the various stakeholders who could play a role in countering corporate investors' influence.** Individual families, workers, or business owners all benefit from being able to join advocacy organizations that can provide them with support and connect them to policymakers and regulators. While workers and educators can join unions (see below), families and small providers can find support through advocacy and grassroots organizations like Community Change, MomsRising, United Parent Leaders Action Network (UPLAN), and The Child Care for Every Family Network; trade organizations such as the National Association for the Education of Young Children (NAEYC) and Child Care Aware of America (CCAoA); cooperatives; family child care associations such as the National Association for Family Child Care, Home Grown, and All Our Kin; or small business associations like Small Business Majority. These organizations can act as intermediaries between policymakers and individual stakeholders, and can take on the work of keeping track of policy debates, inviting policymakers to speak directly with their members, collecting testimonials from their members to inform policy discussions, and equipping their members, through training and leadership development, with the advocacy skills they need to make direct demands on lawmakers. Their work is critical to countering corporate lobbying power and other political influence tactics, and policymakers should proactively ensure that these stakeholders are included in decision-making processes. Meanwhile, organizations should encourage engagement from stakeholders by helping to cover expenses like travel, child care, and stipends for their time and expertise.

**Policymakers should also create industry committees to systematically ensure that stakeholders are actively involved as more than just advisors in the creation of regulations and standards in child care.** State and local governments can, for example, create industry committees that include representatives from government, caregivers and early educators and their representatives, employers, and families. These types of committees are commonly used in other sectors to set standards around wages, benefits, and working conditions. For example, in 2023, Minnesota created a Nursing Home Standards Board empowered to set minimum workplace standards in response to the industry's chronic worker shortage in the state (Madland 2023). In the child care sector, a similar body would be useful to ensure that public payment rates remain in line with the true cost of care, and that quality standards remain effective guards against exploitative tactics.

**These committees should have a mandate to act as more than mere advisory councils**. Instead, these bodies should be empowered to shape regulation and hold providers and other public entities accountable for fulfilling their responsibilities to the child care vision. Furthermore, these committees should be designed to provide adequate compensation to their members so that that individual providers, workers, and family representatives have the resources to engage with and advise these bodies.

### II. WORKER ORGANIZING (UNIONS)

**Child care workers are often the first to see the consequences of corporate providers putting their profits ahead of the vision priorities.** Workers will be among the primary beneficiaries of a child care system that properly funds, valorizes, and supports caregiving labor, and their wellbeing is directly tied to the quality of care children receive, and providers' ability to attract new workers into this sector. However, workers will also be the first to experience the consequences of managers' efforts to cut down on operating expenses, be it through lower wages, more unpredictable scheduling, fewer long-term training opportunities, or increased demands on their attention while they are with children. Child care workers therefore are both motivated and well placed to spot and alert other child care stakeholders, especially regulators, to corporate malpractice.

**Child care workers need the ability to defend their own right to good jobs and fair wages and benefits, which is essential for achieving the child care vision.**

**Unionization and collective bargaining remain important mechanisms for improving working conditions in low-wage sectors like child care.** Union activity in states like Massachusetts and Rhode Island, for example, helped expand home-based providers' rights to benefits such as paid leave (McLean et al. 2021). Unions, along with the industry committees discussed above, are also important for mobilizing workers in policy discussions, ensuring their perspective is included alongside that of corporate lobbyists.

**However, union membership rates remain low among child care workers, and corporate providers have proven hostile to unionization efforts.** For example, in 2024, Guidepost Montessori, a Montessori program chain owned by Higher Ground Education, closed two schools and furloughed 30 members of staff after workers announced their plans to join the International Longshore and Warehouse Union Local 5 (Gruben 2024).[16] Meanwhile, both KinderCare and Bright Horizons cite unions as a risk to their profits in their filings with the Securities and Exchange Commission (SEC) (KinderCare Learning Companies 2021). In 2023, only 5.4 percent of child care workers were union members, and 6.2 percent were covered by a union agreement (Hirsch, Macpherson, and Even 2024).

**Policymakers can protect public investment in crucial services as well as workers' path to a union by requiring that recipients of public funding, if not all licensed providers, recognize their employees' collective bargaining rights and commit to labor peace.** They should further specify that employers who misuse public funds for non-program purposes, such as opposing workers' choice to organize, are ineligible for continue public funding.

**Policymakers should extend collective bargaining rights and workplace protections to all child care workers in recognition of the varied employer-employee relationships in this sector.** In particular, policymakers in states that have not yet done so should recognize home-based caregivers' right to collectively bargain using the state government, which pays them through its funding of child care, as their unifying employer (Collins and Londono Gomez 2023). Policymakers can also protect these workers by passing a Domestic Workers Bill of Rights, repealing the New Deal exemption of domestic workers from labor protections. Finally, policymakers should consider strengthening protections for workers retained through third-party agencies and gig-style apps.

**Workers must also have clear mechanisms for voicing concerns about systems and practices that are harmful to other stakeholders or the vision goals.** Child care workers must be granted whistleblower protections that extend beyond disclosing instances of financial fraud to include providers' violation of workplace or quality standards, or cases of negligence or abuse. Policymakers should also create easy-to-find and accessible portals for workers and other members of the public to report violations or make complaints, and policymakers should set up processes to ensure that these reports are followed up with a timely investigation. Worker participation in industry committees is another important means of ensuring that workers' insight into the systemic challenges facing the industry shapes the ongoing policy effort to achieve the child care vision.

## III. MOBILIZING INVESTORS & ASSET MANAGERS

**Investors, and particularly public pension funds, are major beneficiaries of corporate providers' profit-maximizing tactics, but are also often individuals or institutions who have their own motivations to minimize risk and broader societal harm.** Although discussions are ongoing around the scope of public pension fund managers' fiduciary duties towards workers and retirees, these funds remain legally bound to ensure their pensions remain adequately funded, within the guidelines set out by policymakers, so that they can continue to pay

[16] The National Labor Relations Board review of this case remains open as of the date of this report's publication (National Labor Review Board 2024).

retirees over the long term. Child care stakeholders who want to recruit investors and asset managers as guardrails against harmful profit-maximizing behavior will have to frame their arguments around protecting these investors' financial returns, and stress the headline and financial risk of driving a critical sector like childcare into risk of bankruptcy and disruption.

**One means of limiting corporate child care providers' financial strength would be to dissuade asset managers from investing in corporate child care in the first place.** Although some states have instructed fund managers to divest from companies in the fossil fuel or weapons manufacturing industry (Lichtenstein et al. 2023), this outcome is less likely for child care given that this is an industry that policymakers will want private investors to support using investment tools that align with the child care vision. However, child care advocates may be more successful in convincing pension funds to reduce their investments in private equity more broadly given the growing concerns that private equity funds do not actually deliver the low risks and high returns that they promise to investors (Flood 2020; Phalippou 2020; Sommer 2023; Wiggins 2022).

**Asset managers' ability to withhold money from private equity funds may in fact be their greatest source of leverage over private equity fund managers (the general partners, or GPs).** A core feature of the private equity business model is that investors (the limited partners, or LPs) have little control over how GPs use their money once they have handed it over to them. Since LPs commit to leaving their money with the GPs for the duration of the fund, they are unable to draw out of the investment if they learn that GPs are using tactics in acquiring and managing portfolio companies that risk harming other stakeholders. However, if asset managers—and especially the large public pension funds that constitute a core source of private equity funding—are willing to threaten withholding investments in a private equity firms' future funds in response to the GPs of existing funds misusing their money, these firms would have a strong incentive to more mindful about their broader impact. That said, this would require asset managers to demand greater disclosures about GPs' investment and management tactics, and to monitor funds' activities through the duration of their lives. Asset managers would also have to be clear and transparent to the public about what outcomes in particular they feel would warrant them following through with this boycott threat. In 2023, the SEC introduced requirements that private funds—including private equity, venture capital, and hedge funds—provide quarterly disclosures to investors about their fees, expenses, and performance. In June 2024, this rule was struck down by a federal appellate court (Goldstein 2024). The SEC will likely appeal this decision, but in the interim, the responsibility for demanding these disclosures remains with the investors themselves.

**Meanwhile, investors who are shareholders in publicly-listed companies can, relative to private equity LPs, be more easily mobilized to respond to threats to their long-term returns.** Publicly-listed companies are undeniably structured to prioritize high profits and shareholder returns, but since many shareholders—including pension funds—plan to invest in companies for years at a time, they have strong incentives to push back against managers who cannibalize a company's long-term health in order to boost short-term profits. In the child care industry, shareholders interested in the long-term health of a provider therefore have an incentive to monitor its use of debt, its levels of worker turnover and levels of job satisfaction, and any threats to a company's reputation that might lose them families' trust. Asset managers who invest in multiple companies across an industry also have an incentive to ensure that the companies in their portfolio are not causing wider harm to that sector.

**Shareholders have a number of means of influencing publicly-listed companies' management to keep them aligned with long-term goals.** First, they have the power to vote on companies' board members, and can introduce and vote on proxy resolutions to request or require that management pursue a specific course of action. Large investors naturally have a greater vote share, and thus larger influence over companies, than small ones—although their power will generally be more diluted in public markets relative to private markets, where they are likely one of only a handful of investors in a fund or company. Asset managers are thus free to divest from a company at any time if they disagree with their practices, but the threat of any one investor's departure will be less likely to sway managers in publicly-listed companies than it might a private equity GP.

**Policymakers and regulators can help align investors' incentives with the child care vision goals by strictly enforcing the rules and standards that they set for businesses operating in child care markets** (see Section IV.4)**.** If providers who violate regulatory standards face credible threats of being fined or losing their license, thus disrupting their revenues, then their investors will have an incentive to keep a close eye on these companies' behavior in order to protect their own financial returns.

**Policymakers can also strengthen investors' oversight of**

**corporate providers by increasing transparency in child care markets.** Both private equity LPs and shareholders need to have information about the risks that company managers are taking, or the harms they are causing, if they are to use their limited powers to hold them accountable. Furthermore, child care advocates need information about which investors are tied to which providers so that they can alert investors to harms tied to their support of a company, and pressure these investors to act. Public company shareholders naturally have more information than private equity LPs given these companies' existing public disclosure requirements, but policymakers should first and foremost require—as a condition of receiving public funding and/or an operating license—that all providers disclose their owner, ultimate parent entity, and investors in that entity. Policymakers should also require disclosures about other measures of companies' activities, including their debt ratios, executive and management compensation packages, staff turnover and wage rates, and tuition and fee levels.

## STEP 3. MORE REVENUES, WITH STRINGS ATTACHED

**Funding policy is the primary way that policymakers will be able to shape the incentives, market structure, and outcomes of the child care industry.** To achieve the vision goals, public funding will have to become the primary source of revenue for the majority of child care providers given the discrepancy between providers' necessary expenses and families ability to pay. Through public funding policy, policymakers have the power to determine how much providers earn as income, which providers receive support, and which conditions they must meet to do so. Of course, companies can still operate without receiving public money by relying on families' tuition payments or contracts with employers. Policymakers must therefore be careful to not depend so much on their funding policy to regulate providers' behavior that they leave the corporate providers who opt out of receiving public money to operate in a separate section of the child care market with fewer guardrails, standards, or oversight (see Section IV.4)

### I. SET NEW RULES OF THE GAME (PUBLIC FUNDING CONDITIONALITY)

#### CONDITIONS ON HOW FUNDING IS USED

**Contract-based public funding policies are best suited to giving providers larger and more stable revenues, but must include well-defined expectations about what services and investments are to be provided in exchange for this money.** Corporate providers will try to minimize their operating expenses so that more of this revenue can be diverted to profits. In the child care industry, this risks harming care quality, since quality is largely correlated with providers' operating expenses in labor, supplies, and facilities. Funding policy must therefore set clear minimum standards about which expenses are a necessary cost of doing business in this industry—expenses that are required because reducing them would compromise one or more of the vision goals. Only after paying these expenses should providers be allowed to divert taxpayer money towards other uses, such as debt payments, franchising, royalty or management fees, or investment dividends.

**Policymakers can ensure that funding contracts also increase the income stability of workers by tying funding to staffing requirements associated with the number of seats an enterprise is paid to supply.** For example, to deter the existing practice of cutting staffing levels shift-by-shift based on attendance levels, policymakers could consider requiring providers to maintain staff-to-child ratios corresponding to either the number of children in attendance or the number of seats the provider has been contracted to support—whichever is greater. In cases where fee-for-service funding is provided for specialty services—such as early intervention services or other forms of therapy—providers should be required to disclose the name of the specialist serving each child and the hours that services were delivered, to guard against providers pocketing the extra payments without delivering it in the quantities promised (as has occurred in the hospice and other care sectors) (Appelbaum, Batt and Curchin 2023).

**Public funding should also include conditions on child care workers' wages, benefits, and career advancement opportunities.** Baseline wage requirements are rarely included in existing child care funding policy, but should become the norm in public funding, and require pay parity with K-3 teachers. Staff wages are the primary expense that corporate providers will seek to minimize to keep their operating expenses down, and public funding must prioritize raising job quality in this sector as a means of attracting more workers and enabling an expansion in supply. To this end, policymakers must make sure that funding levels are sufficiently high to support both expanded access *and* higher caregiver incomes.

**Finally, policymakers can set limitations on uses of public funding that do not advance the mission goals**. Most notably, policymakers can set limits on executive compensation, debt ratios, dividend recapitalizations, and for publicly-listed companies, stock buybacks and investor dividends. Policymakers who wish to directly deter franchise companies or private equity-backed companies could also consider ways to limit the franchise or management fees integral to these business models. These types of restrictions are particularly important while the child care industry is in transition—while supply expands and wages and incomes rise— as they ensure that the funding that enters this industry remains at the level of the local provider (as opposed to the parent company or franchisor), where it can be invested towards achieving the mission goals.

### CONDITIONS ON HOW MUCH FAMILIES SHOULD PAY

**Families are vulnerable to providers who pass on the higher cost of care onto them in order to retain their current profit margins—and will become more vulnerable as policymakers mandate higher operational expenses.** In sections of the market where families will contribute tuition co-payments in addition to public subsidies, these families will likely remain more discerning about whether providers' prices remain broadly aligned with those of the rest of the market. However, the child care shortage limits families' ability to properly discipline price-gougers since they cannot easily switch to other providers in response to price hikes.

**Therefore, to protect families from shouldering the cost of fixing child care markets, policymakers should consider capping how much providers can charge families as co-payments to public funding, and restrict how much providers can raise their prices year-on-year.** This would mimic Vermont's funding model, as well as the new CCDF regulations that cap families' co-payment rates to their incomes, ensuring that they do not pay more than 7 percent of their household earnings on child care for all of their children. More broadly, the ideal would be for public funding to make child care free for the majority of families.

### CONDITIONS TO IMPROVE MARKET SYSTEMS

**Policymakers can set preconditions for receiving public funding that require providers to behave in ways that help strengthen child care markets.** To start, policymakers should require providers to recognize workers' collective bargaining rights, which can help improve worker wellbeing and increase accountability in the industry (see Section IV.2). Policymakers should also require funding recipients to disclose any ties to a chain or franchising entity; any investors with a 5 percent or greater ownership stake; both their immediate owner and ultimate parent entity; the percent of their revenues coming from public sources; the percent of their spending that goes towards direct care services; tuition and co-payment levels; debt levels; and worker-executive pay ratios. Given the risks that private equity investment and other forms of corporate ownership pose to the child care vision goals, it is critical for maintaining accountability that regulators and other stakeholders have as much transparency as possible about corporate investment flows in this industry.

## II. RESTRICT MARKET ACCESS (PRIORITIZE FUNDING RECIPIENTS)

**Policymakers should use public funding to advance the child care vision goal of a sector made up of diverse types of providers and business owners.** Given how drastically child care supply needs to increase to meet families' needs, funding policy will help determine which types of enterprises enter this industry and become the foundation of the future child care system.

**Funding should prioritize or even favor providers who meet certain operational criteria.** For example, policymakers can provide additional funding to providers based on their size; their participation in co-ops; their inclusion of parents or workers on boards or in management decision making; the unionization of their workforce; or to nonprofit or community-based ownership. One model for this is the Rural Electrification Administration, a New Deal program that prioritized co-ops and nonprofits in its distribution of low-interest loans to new enterprises expanding access to electric and telephone lines in rural communities; this program succeeded in increasing supply, access, and affordability to this critical infrastructure while ensuring that the financial gains of this industry remained in the hands of local communities and workers (Waters 2020). Policymakers can also provide higher payment rates to providers who enter areas with a severe shortage of licensed child care, or who serve other low-income or marginalized communities, in order to encourage increased supply in these communities.

**Policymakers can structure public funding in ways that encourage providers to make the types of investment that advance the child care vision.** State and local governments that want to encourage providers to make investments that increase their quality, build supply in under-served areas, or otherwise advance the vision goals can set higher payment rates for providers who meet metrics tied to those goals—but they must ensure that these rates are high enough to cover the cost of the investments providers need to make to reach these standards. Many states that have introduced such incentive schemes through their QRIS programs have set payment rates for high-quality providers too low to enable providers to make these investments. This shortcoming has led more governments, with HHS backing, to use cost-of-quality calculations to set their repayment rates, as opposed to using the market rate surveys that disadvantage providers in lower income communities (ACF, n.d.).

**Policymakers can also opt to wield a stick in addition to offering carrots, and directly restrict the funding that goes to corporate providers.** Growing evidence of the systemic harm that the private equity and franchise business models are causing across industries could justify policymakers deciding to limit the share of public funding that providers using these business models are eligible for. For example, the Massachusetts Senate has passed a bill wherein any company directly or indirectly (e.g. franchising) operating more than 10 center-based programs can receive no more than 1 percent of the total funding distributed by the state (Haspel 2024a). This type of policy limits the market share that any one provider can gain, at least through public funding.

### III. STRATEGIC REFORM (EMPLOYER INCENTIVES)

**As policymakers expand public funding to child care providers, they should consider how to reform public incentives around employer-sponsored child care to encourage employers to contribute to the industry vision goals**. For example, incentives should encourage employers to make their child care benefits transferable so that employees can receive financial support while sending their children to the caregiver of their choosing. The goal of these reforms should be to reduce employers' incentive to restrict their employee' child care choices, and to contract primarily with corporate providers. Some families will value the option of bringing their children to on-site care facilities, but policymakers should consider how such providers can be better integrated into the wider child care system and vision, and how employers can support their employees without making them fully dependent on benefit packages to access care.

## STEP 4. REGULATE OPERATIONS

**High standards backed by a well-funded system to enforce adherence to these standards are essential guardrails for industries whose revenues come primarily from public funding.** Although public funding does not currently make up the majority of child care providers' revenues, an influx of public spending in this sector will necessitate greater oversight from child care regulators to protect the system from abuse. Successful regulatory systems set a floor under providers' operations, restricting their ability to cut costs at the expense of other stakeholders or the vision goals. By limiting corporate providers' ability to fall below these standards, more of the profit generated with public investment will be reinvested into the businesses as opposed to going to corporate shareholders. Similarly, standards that ensure that workers receive benefits—such as health care, paid leave, retirement benefits, and investments in their professional development—ensures that taxpayer funding going into child care is used to build and retain a talented workforce that can grow with career ladders, rather than toward private profits.

### I. SET NEW RULES OF THE GAME (QUALITY AND LABOR STANDARDS)

**In addition to the conditions tied to public funding, policymakers must set industry standards that apply to all providers in the child care industry.** Providers should retain flexibility in the type of care that they offer families to protect the diversity of care options, but policymakers must define the minimum quality and workplace outcomes that all providers must be able to achieve to remain in this line of business. Child-to-staff ratios are an example of such a standard, and represent one of the most important protections that the child care industry currently has. Regulations around staffing ratios were notably absent in many of the other care sectors that have been harmed by private equity investments, such as the nursing home industry.[17] Policymakers should consider

[17] In April 2024, the Biden Administration introduced the Nursing Home Minimum Staffing Rule intended to introduce such a guardrail against understaffing for nursing home providers receiving Medicare and Medicaid payments (White House 2024).

what other operating outcomes and expenses—such as safety standards, or the provision of diapers or meals—they consider to be necessities for child care enterprises.

**Given the strong correlation between caregiver wellbeing and care quality, policymakers must introduce labor and workplace standards that prevent corporate providers from extracting profits at workers' expense.** These standards should include requirements ensuring child care workers have a living wage, predictable work schedules and access for full-time hours for those who want them, a right to unionize, and paid sick days and paid family and medical leave. Policymakers could also consider requirements around the number of lead teachers, assistant teachers, or other caregivers that should remain in a classroom or other setting, to prevent corporate providers from shifting towards lower-paid caregivers, as was seen in hospitals and nursing homes for nursing staff.

**Governments must ensure that their standards remain responsive to the changing challenges and needs of providers, workers, and families, and should therefore include diverse stakeholder voices in the creation of these standards.** Industry committees (see Section IV.2) thus represent an important means of ensuring workers, parents, educators, unions and small providers are active participations in the standards-setting process, given that low unionization rates and high fragmentation in this industry can complicate these stakeholders' efforts to have their concerns heard.

## II. REGULATORY COMPLIANCE AND ENFORCEMENT (INCENTIVES, INSPECTIONS & FINANCIAL PENALTIES)

**In order for standards to be effective, providers must have the tools and resources to comply, and governments must have the tools to properly enforce these rules.** Policymakers must thus design and fund systems capable of catching and penalizing licensed providers who fail to abide by these regulations.

**For many smaller providers, consultation, support, and resources are the best remedies to help them come into compliance with regulatory standards and from there, to improve the quality of their programs.** Rather than rely on QRIS, which disadvantages home-based providers and can entrench racial inequities, policymakers can introduce progressive funding formulas that increase providers' revenues enough to reimburse them for the cost of investing in higher quality, thus helping the most disadvantaged providers strengthen their programs.[18]

**Governments will need to expand their inspection capabilities in tandem with any growth in child care supply.** Even if they contract third-party inspectors, governments should commit to directly inspecting a given share of providers in order to verify that contractors' assessments remain aligned with the regulatory goals. Governments should also guarantee whistleblower protections to workers and other stakeholders who alert them to financial or operational abuses, and should commit to quickly following up with these reports.

**To counter the financial incentive that corporate providers have to cut costs, regulators should impose a financial penalty on providers who violate quality regulations.** Providers who create unsafe conditions for children, who violate required workplace standards or workers' legal rights, or who are found to be abusive or negligent in their caregiving should face the credible threat of being fined or having their license to do business suspended or revoked. For example, Massachusetts fined KinderCare $540,000 for wage, sick, and meal time violations (Office of the Massachusetts Attorney General 2023). These punitive systems should operate in tandem with regulatory processes that work with programs to improve their operations, and should focus on enforcing against behaviors that cause the greatest risk to children, early educators, or the broader sector.

[18] State and local governments' quality metrics will vary, but organizations like the National Association for the Education of Young Children (NAEYC) design their quality accreditation systems to capture whether child care providers support: sensitive and responsive relationships between caregivers and children; a curriculum promoting social, emotional, physical, language, and cognitive development; effective teaching approaches; child progress; an emphasis on safety, health and nutrition; staff competencies, preparation, and support; strong and durable relationships with families; connections to community resources and relationship; a safe and healthy physical environment; and strong leadership and management.

## STEP 5. PROTECT COMPETITION

**Policymakers must proactively level the playing field in child care markets to prevent corporate providers from using their relative size and market power to unfairly shape the industry to their advantage.** This will entail enforcing existing antitrust laws against anti-competitive practices while ensuring that non-corporate providers have access to the support and resources that they need to remain active in child care markets and offer families non-corporate care options.

### I. COMPETITION ENFORCEMENT (ANTITRUST)

**It is illegal for companies to use their power in a given market, or to collude with other companies, to reduce competition or otherwise harm stakeholders in that market, and state and federal competition policy and justice authorities are empowered to enforce these laws in child care markets.** As an example of what law enforcement of this behavior could looks like, the FTC has sued a private equity-backed anesthesiology chain in Texas, alleging that they rolled up some local providers and coordinated with others to raise prices, and that they colluded to keep competitors out of the piece of the Texas market under their control (FTC 2023). Companies that are found guilty of this behavior can be forced to pay a fine and/or spin-out or sell-off their subsidiaries in a given market.

**Since provider diversity is one of the five vision goals for the child care industry, and given the risk that corporate concentration poses to this and other vision goals, state and local governments should prioritize protecting diverse ownership and market competition in their child care regulatory system.** State and local regulators should therefore require disclosures as part of their licensing and public funding systems about providers' ownership and ultimate parent entity, relationships with other providers, tuition rates and fee structures, wages and benefit levels, and quality certifications. This information should be included in public information databases, and state child care regulators should work closely with competition policy and attorneys general's offices to monitor and protect child care market competitiveness and owner diversity.

**With or without the assistance of publicly managed databases, child care stakeholders should also monitor this sector with an eye towards alerting competition policy enforcers to any negative impacts that corporate providers may be causing as they expand.** To be the most effective, activists should try to bring regulators as much of the evidence as they will need to make the case against a company's behavior, including details about which company should be the target of an investigation, and specifics about the negative impact they have had on local markets (e.g. higher prices, lower wages). Grassroots organizations and other activists can work with private plaintiffs or nonprofits to bring evidence of harmful behavior to state attorneys general or federal antitrust regulators in the Department of Justice or FTC.

### II. SUPPORT COMPETITORS (SMALL BUSINESS & PUBLIC OPTIONS)

**Small home- and center-based providers will be the largest source of competition to corporate providers, and should receive public support to fulfill this market function and remain an option for families looking for providers.** In tandem with supporting shared-services alliances (see Section IV.1), state and local governments should consider opportunities to supply providers with technical assistance resources for free or at low costs. They can do this by working with the SBA's Small Business Development Centers and Women's Business Centers, or else the Department of Commerce's Minority Business Development Agency. Technical support should also target new entrepreneurs who are looking for guidance on the best practices of running a child care business; rather than turning to franchisors for a ready-made operating model, these entrepreneurs should have access to public and nonprofit resources, such as SCORE, that can provide them with similar levels of support and guidance without compromising their independence.

**Families who depend on private and nonprofit child care providers also benefit from the increased market competition that comes from them having the option to send their child to a public provider** (Sitaraman and Alstott 2019). First, if public providers become a default choice for families—especially in states that do not guarantee public funding to families using private providers—then corporate and other for-profit providers would only be able to attract customers by providing care of equal or higher quality than public providers, and at a reasonable cost to local families. Second, public providers guarantee access to all children, ensuring that families will be able to find care even if they are not accepted in a private facility.[19] Public providers can also increase access for underserved populations, either by serving families in areas with a limited supply of licensed child care or communities where demand is too low to support multiple providers, or by providing additional wrap-around services, such as screening and supports for children with disabilities.

**Of course, public child care options have their own market advantages, and these programs must be designed to avoid undermining the business model of private small businesses**. For example, public pre-K for 4 and some 3 year olds has, in some cases, deprived local private programs of these older children whose tuition they depended on to subsidize the care of younger children. Thus, public pre-K programs inadvertently increased the price of care for infants and toddlers who do not have access to public school (J. Brown 2018). While public options can be an important tool to hold larger providers accountable, given the prevalence of smaller providers in the child care market, it will be important that there is a level playing field that ensures access to resources for small businesses and non-profits, and that ensures public options also cover the infants and toddlers that are most expensive to serve.

## STEP 6. HAVE AN EXIT STRATEGY

**Private equity funds typically own companies for only a few years before they try to have it go public or be sold to the highest bidder**. Buyers tend to be strategic companies in the industries seeking to grow through acquisitions, or else other private equity funds. Few other stakeholders have the financial resources or access to debt to make such an acquisition, and both strategic buyers and private equity firms can be willing to pay a premium to acquire a company that expands their local market power. This implies that once a child care provider has been acquired (or created) by a private equity fund, it is overwhelmingly likely that it will remain on the one-way path of corporate ownership in perpetuity.

**Policymakers should cooperate with other child care stakeholders to experiment with ways to create off-ramps from corporate ownership for private equity-backed providers.** The purpose of these measures would be to allow private equity, growth equity, and other investment funds to inject financial resources and market expertise into the child care industry—either creating new supply or getting struggling enterprises back on their feet—without this jeopardizing the vision goal of maintaining diverse provider-types, and keeping the gains from the child care industry flowing to local communities. All of this, of course, would be conditional on the introduction of the guardrails and additional funding discussed throughout this report that will ensure that corporate providers contribute to the vision throughout their ownership of child care programs.

**The core element of any such off-ramps would require identifying and robustly funding alternative, non-corporate buyers of private equity portfolio companies—mirroring the tactics policymakers might introduce to prevent private equity from buying small providers in the first place** (see Section IV.1). Policymakers could, for example, provide forgivable or low-interest loans to local entrepreneurs, workers interested in forming a worker-owned co-ops, or even local governments, community organizations, or nonprofits who could take over the enterprise. Public pension funds could also be encouraged to provide part of this funding—for example by investing in CDFIs as opposed to private equity funds—as a means of ensuring that their money is being used in ways that directly contributes to the communities of the workers and retirees they serve.

**Policymakers should also consider restricting the frequency in which child care providers can be bought and sold.** For example, California prohibits hospice care providers from changing ownership within the first five years of their being licensed as a business (Appelbaum, Batt, and Curchin 2023). Especially in a sector like child care where policymakers will want to encourage the entry of many new entrepreneurs into the sector, this type of restriction can help sift out the types of entrepreneurs or investors who are not interested in building businesses that could provide quality care in the long term.

[19] This is also important in communities where faith-based providers make up the majority of care options. In these cases, public providers ensure that families who desire a secular care option can find a local slot for their child.

## STEP 7. SUPPORT CONCURRENT CAMPAIGNS

**Efforts to protect the child care industry from corporate capture is one piece of a much larger fight against corporate actors who have shaped the American economy around the concentration of wealth among a few individuals and corporations at the expense of the majority of workers and families**. Child care industry stakeholders must first and foremost focus on campaigns to protect their own sector, but should also draw support from—and provide support to—parallel campaigns taking place across industries and levels of governments to build guardrails against private equity and concentrated corporate power.

### I. WEAKEN PUBLIC SUPPORT FOR CORPORATE TACTICS (TAX REFORM)

**Advocates for tax reform have been working to remove the elements of the U.S. tax code that encourage the private equity business model.**

**Private equity benefits from the tax code primarily in three ways** These tax advantages contribute to the structural incentives that private equity funds have to use high levels of debt, and to prioritize the maximization of company profits and investor returns.

**First, private equity benefits from companies' ability to deduct debt interest payments from their taxes.** This helps reduce the tax liability of the portfolio companies that have been loaded with debt. Any money that companies save in taxes can be passed on to boost the returns of their private equity owners.

**Second, private equity funds' GPs benefit from the carried interest tax loophole.** The share of the fund's return that is paid to the GP is known as "carried interest," and is intended to align the GP's incentives with the other investor's desire for maximized returns. The carried interest tax loophole refers to the fact that income from carried interest is taxed as if it were an investment return rather than a form of income, and thus is taxed at a lower rate than wages (Huang 2023). This reflects how private equity funds are legally viewed as investors in their portfolio companies, not managers—despite the control that they have over company operations. Private equity funds as owners therefore benefit in the tax code more than other forms of ownership. The Biden Administration attempted to remove this loophole through the 2022 Inflation Reduction Act but had to drop these provisions to get it passed (Rappeport and Flitter 2022).

**Third, private equity is exempt from paying the Corporate Alternative Minimum Tax, which was also introduced in the Inflation Reduction Act**. This tax requires companies that earn at least $1 billion in profits to pay a minimum tax rate of 15 percent on these profits. Although the original legislative proposal would have required private equity to pay this minimum tax if their combined profits from across their portfolio companies and funds exceeded $1 billion, private equity firms were ultimately exempt from this tax in the final bill (Stein 2022).

**In 2025, several tax provisions that disproportionately benefit the wealthy will expire, which will open up a broader debate on reforming the tax code.** As part of that package Congress should address these loopholes in the tax base that disproportionately benefit private equity investors. This should include getting rid of the carried interest loophole and private equity's exemption from minimum corporate tax rates, and limiting the degree to which tax deductions for debt subsidize financialization of taxpayer investments in services such as child care. While doing so would not directly mitigate some of the worst excesses of private equity, it would limit the ways that taxpayers subsidize and incentivize predatory financial behavior. Closing tax loopholes and raising taxes on private equity firms would also raise revenue that could be invested back into communities and services like child care.

### II. INCREASE TRANSPARENCY (CORPORATE DISCLOSURE REFORM)

**Child care advocates should support federal efforts to increase transparency in private markets.**

**As private entities, private equity firms, funds, and portfolio companies face far fewer disclosure requirements from the SEC than their publicly-listed counterparts.** Private equity funds do not need to disclose which companies they buy, how much debt they use in these transactions, or how much money they take from companies in the form of fees, dividends, asset sales, or other returns. This complicates regulators efforts to track the systemic risks that private equity funds may be creating by acquiring companies from across industries, or by growing their market share within given industries. Meanwhile, this lack of transparency makes it nearly impossible for stakeholders like workers and families to know enough about companies' ownership structure to hold anyone accountable or financially liable should a company cause them harm through their profit maximizing efforts.

**The Biden Administration has been working to increase transparency around private equity to address some of these concerns**.

**The SEC tried to introduce new rules requiring private funds to issue quarterly reports on fees and performance, as well as perform annual audits** (Mandl and Prentice 2023), but this rule was struck down by a federal appellate court in June 2024 (Goldstein 2024). Even if the SEC succeeds in restoring these rules through the appeals process, these disclosures would have only marginally increased their ability, along with that of third party advocates, to continually monitor the sector. This is because private equity funds would not have to send disclosures directly to the SEC, but rather would only have to make this information available to them on demand.

**Meanwhile, the FTC has proposed reforms to its pre-merger notification requirements, demanding, among other rules, that parties to a merger disclose information about their corporate relationships and financial structures** (FTC 2023). This is notable for making it easier for the FTC to take action against roll-up tactics that are used to create unfair markets. However, small acquisitions continue to be exempt from these disclosure requirements, placing the onus on the FTC, state attorneys general, and local stakeholders to identify harmful acquisitions in highly fragmented industries like child care.

**These types of disclosure provisions are being undermined by big business lobbyists who are arguing that they are overly burdensome to businesses, especially small business owners**. Child care stakeholders, and in particular small business owners should join other advocates campaigning for regulatory reform and legislation, such as the Stop Wall Street Looting Act, that would increase transparency and accountability around private equity. Groups that have campaigned on these issues at the federal level include Americans for Financial Reform, the Private Equity Stakeholder Project, and the Center for Economic and Policy Research; grassroots leaders in this space include United for Respect and Community Change. Additional allies can be found across the industries and stakeholders that have been impacted by private equity including doctors and nurses, long-term and home-care providers, hospital and emergency room staff, fair housing advocates, retail workers, fast food and other franchisee workers, and many others. Private equity firms undoubtedly have deep pockets that they can use to shape U.S. markets and policies to their benefit—but child care stakeholders have power in their numbers, the breadth of their allies, and the broad appeal of the vision that they have for their industry and for what it can contribute to U.S. society.

SECTION 5

# CONCLUSION: PUTTING CHILDREN BEFORE PROFITS

# SECTION V. CONCLUSION
# PUTTING CHILDREN BEFORE PROFITS

**Child care is an essential building block of families' financial security, children's education and development, communities' wellbeing, and the country's economic foundations.** Ideally, the U.S. child care industry and policy system should be designed to achieve (1) universal access to care; (2) universally affordable care; (3) thriving caregivers; (4) high-quality care; and (5) diverse choice of providers for families.

**As more policymakers at both the state and federal level consider increasing public funding to the child care industry to address the market failures that stand in the way of achieving this vision, they must also consider means of protecting this industry from corporate actors who will seek to extract wealth from this funding without contributing to the public's broader goals.**

**The evidence from other industries that have received large amounts of private equity investments suggests that, left unchecked, these types of profit-maximizing actors will threaten the success of the child care industry.** Private equity-backed companies will likely prioritize growth through acquisitions rather than increasing supply, drawing resources from the sector without increasing families' access. These companies will pass on the higher operating cost of achieving the vision to families and taxpayers by raising their tuition and fees. They will cut down on their operating expenses, undermining both worker wellbeing and service quality. And, through their use of consolidation and uncompetitive market practices, they will reduce the diversity of private providers operating across the industry.

**Policymakers and other stakeholders have a responsibility to design a child care system that creates market structures, incentives, and guardrails that align with the vision for child care as a public good.**

**First, regulators must set standard rules of the game.** The minimum standards for industry-wide business behavior must rise so that everyone who wishes to participate in child care markets is required to operate in ways that align with the child care vision. This should include:

- **Raising quality and labor standards,** including health, safety, and educational requirements; minimum wage and benefit requirements; protections of collective bargaining rights, and restrictions on how soon after acquisition a program can be re-sold.
- **Increasing mandatory disclosure requirements as part of the licensing process**. Regulators should collect and publicly disclose information about such metrics as businesses' ultimate owners, investors, debt levels, and relationships to other businesses in the child care or other related industries.
- **Providing technical support and funding to help small providers come into compliance with new operating standards**. This support can come from the SBA and other public entities, or through support to shared-service alliances.
- **Maintaining robust enforcement systems,** including inspection systems and the ability to introduce financial penalties, or to suspend the licensing, of providers who harm children, workers, or the stability of the broader industry,
- **Empowering industry boards**—composed of diverse stakeholders including workers and their representatives, local program owners, and families—to shape the regulatory processes and hold companies and policymakers accountable to the vision for the industry.

**Second, policymakers must develop a funding strategy that ensures funding recipients behave in ways that align with the vision for the industry.** This strategy should be designed to prevent providers from collecting public money while cutting their costs or otherwise behaving in ways that undermine the child care vision priorities. Such a strategy should include:

- **Setting public payment rates high enough to cover the true cost of care.** Private providers are only able to contribute to the vision for child care if they can remain profitable as businesses. Under-funded providers have no choice but to push down their expenses, raise tuition rates, restrict their activities to the wealthiest communities, or sell out to private equity-backed companies.

- **Defining expectations of funding recipients, especially around which services and operational outcomes businesses must provide in return for public funding.** This includes their paying higher wages to their workers, recognizing their employees' collective bargaining rights and committing to union peace, maintaining predictable scheduling, and investing in their facilities and equipment.

- **Prioritizing certain providers by offering higher repayment rates or other forms of support to programs who advance the child care vision.** This includes providers who invest in raising their facilities or quality, who pay their workers higher rates, who are part of co-ops or shared-services alliances, who are worker-owned, or who serve communities facing higher barriers to accessing care.

- **Requiring disclosures from all funding recipients** about their ultimate owners, investors, debt levels, and relationships to other businesses in the child care or other related industries, tuition and co-payment rates, executive compensation rates, and their spending on programming.

- **Restricting or prohibiting antithetical behaviors** such as excessive executive compensation, high debt levels, shareholder dividends, or stock buybacks.

**Third, policymakers must build and protect fair and competitive markets.** Private equity-backed providers must not be able to accumulate excessive market power relative to their smaller non-corporate or non-profit competitors. This means that neither small programs nor families must become dependent on private equity-backed providers for their services or financing. Such measures should include:

- **Providing technical and financial support to small businesses,** ensuring that they can access financing or the benefits of economies of scale without having to sell out to a private equity-backed chain. This can be done through support to shared-services alliances, increased access to public loans and technical assistance, and robust public registries of available providers.

- **Supporting alternative buyers of small businesses,** ensuring that program owners can exit the market without having to sell their businesses to corporate chains. This support can include funding from public pension funds, SBA programs, or CDFIs, as well as public pathways to transition private programs towards worker or nonprofit ownership.

- **Ensuring robust antitrust enforcement of anticompetitive behavior**. This can limit market consolidation and disincentivize practices that make child care markets less fair to non-corporate providers. This must be supported by child care regulators trained and equipped with public information systems who can monitor the health and concentration of local child care markets.

- **Limiting public subsidies of harmful private equity tactics**, most notably by eliminating the tax preferences that incentivize private equity's use of high levels of debt.

**Finally, child care stakeholders must increase corporate accountability by building forms of countervailing power among the stakeholder who share priorities beyond profits.** If properly empowered and mobilized, stakeholders—such as workers, families, non-corporate providers, and long-term investors—can help push back against corporate efforts to put short-term profits over priorities, including child wellbeing and the growth and long-term financial stability of the sector. This requires:

- **Increasing industry transparency**, and thus allowing stakeholders to monitor corporate behavior. This can be done by increasing the disclosure requirements tied to receiving an operating license and public funding; funding and maintaining robust public registries that present key information about available providers; and strengthening whistle-blower protections for both financial and operational misbehavior.

- **Empowering child care workers** by supporting child care worker unions and collective bargaining efforts; including and compensating workers and unions on industry committees that help craft child care regulations; raising standards around workers' wages, benefits, and working conditions; and supporting workers who wish to buy out their employers.

- **Empowering families** by including family advocacy organizations in policy discussions, and compensating families on the industry committees that help craft child care regulation.

- **Empowering non-corporate providers** by including small business advocacy organizations in policy discussions;

including diverse program owners on industry committees; and providing financial and technical assistance to support small businesses as competitors to corporate providers.

- **Empowering long-term investors**, such as public pension funds, by providing them alternative avenues, such as CDFIs, to invest in child care without having to depend on private equity funds.

**The child care industry is struggling, but a renewed commitment from policymakers and stakeholders from across U.S. society could enable the country to build a child care system that is the envy of the world.** The U.S. has the unique opportunity to get out ahead of the private equity investors who are now entrenched in private child care markets across countries, and to craft a set of market rules and incentives that contribute to, rather than detracting from, the vision of child care being available to all families as a public good. Achieving this vision will require contributions from all stakeholders, including private providers and investors, and a commitment from all actors to put the wellbeing of children ahead of their individual profits.

# ANNEX: THE BIG THREE

The child care 'big three'—KinderCare, Learning Care Group, and Bright Horizons—have been tied to private equity funds for decades. Their history is thus also the history of private equity investments in the child care industry. These companies leave behind them a trail of leveraged buyouts, roll-ups, high levels of debt, bankruptcies, financial fraud, vertical integration with suppliers, and other threats ot the stability of child care markets. By following this trail, we can catch a glimpse of the impact that unchecked private equity investments can have on the child care industry, and the threat these kinds of companies can pose to the vision of child care as a public good.

## KINDERCARE LEARNING COMPANIES

KinderCare Learning Companies is the largest child care provider in the U.S. Headquartered in Portland, Oregon, the company manages over 1,490 early childhood education centers for children ranging from 6 weeks to 12 years old. The company has three lines of business: (1) KinderCare Learning Centers (KCLC), which is the largest provider of early childhood education, and contributed 79.2 percent of the company's 2020 revenue; (2) KinderCare Education at Work (KCE), which provides employer-sponsored child care, and generated 17.8 percent of the company's 2020 revenues; and (3) Champion, which provides before- and after-school programs (KinderCare Learning Companies 2021). They have been owned by Partners Group, a Swiss private equity firm, since 2015 (Holman 2015).

Kinder-Care Nursery Schools was founded in 1969 by Perry Mendel, a real estate developer in Montgomery, Alabama, with the aim of generating child care in bulk—a business model designed to replicate the success of fast food franchise chains that *Fortune Magazine* referred to as "Kentucky Fried Kids" (Chicago Tribune 1990). The company went public in 1972, and, expanded rapidly through the 1970s, relying increasingly on growth through acquisitions as the decade wore on.

In the 1980s, under the leadership of the Richard Grassgreen, KinderCare fell into the orbit of Michael Milken, who led the high-yield securities (i.e. "junk bond") division of Drexel Burnham Lambert, an investment bank. Kinder-Care "diversified" its operations and borrowed money (purportedly to build child care centers), and invested it in the preferred stocks and junk bonds sold by Drexel. Thus, KinderCare helped finance Drexel's takeovers of companies across diverse industries, and acquired its own portfolio of companies in industries as varied as life insurance, chemicals production, and shoe retail (Chicago Tribune 1990). Drexel eventually took KinderCare private through a leveraged-buyout in 1987, a year when the company oversaw a portfolio worth $613 million (Gilpin 1996; Chicago Tribune 1990).

This business model fell apart when the junk bond market crashed in 1989, forcing KinderCare to reorganize itself into two companies: KinderCare Learning Centers, re-focused on child care, and Enstar Group, which took over the financial services and retail operations. Despite this restructuring, KinderCare struggled under $400 million in debt, and filed for Chapter 11 bankruptcy in 1992. In the interim, both Mendel and Grassgreen got caught up in the New York prosecution of Milken that found him guilty of securities fraud, and sent him to almost two years in prison. Grassgreen, who testified against Milken, pled guilty to two counts of securities fraud, while Mendel plead guilty to evading taxes on money the pair had personally received in exchange for their agreeing to have KinderCare buy $85 million in junk bonds from Drexel (Los Angeles Times 1991).

KinderCare emerged from Chapter 11 in March 1993, having never ceased its operations. TCW Special Credits, a unit of the Trust Company of the West, gained a majority stake in the company as it returned to private markets, using Oaktree Capital Management to manage these funds. KinderCare expanded its operations to the U.K., and in 1996, Kohlberg Kravis Roberts (KKR) announced that they would acquire the company for $487 million in equity and $130 million in debt (Gilpin 1996); the deal was finalized the following year.

The same year that KinderCare emerged from bankruptcy, Milken was released from prison after serving 22 months of his ten year sentence. In collaboration with his brother, Lowell Milken, and Oracle chief executive Lawrence Ellison, he founded the holding company Knowledge Universe, which began acquiring companies tied to education. In 1996, Knowledge Universe acquired the child care chain Children's Discover Centers (CDC) for $80 million, renaming the company Knowledge Learning. In 2004, KKR announced their sale of KinderCare to Knowledge Learning for $550 million in equity and $490 million in debt (Atlas 2004; CNN Money 2004).

In 2015, Partners Group acquired Knowledge Universe Education (KUE)—consisting of KinderCare, Children's Creative Learning Centers, and Champions—from Knowledge Universe for $1.5 billion (Holman 2015). They soon changed the company's name from KUE to KinderCare Education, reverting to the more familiar brand name (KinderCare Learning Companies 2016). In 2021, amidst the Build Back Better negotiations that included discussions of a substantial increase in public funding for child care, Partners Group tried to bring KinderCare public through an initial public offering (IPO). KinderCare was expected to be valued at $3 billion, helping the company to raise $460 million, while allowing Partners Group to retain 74.4 percent ownership (McCurdy 2022). However, that IPO was postponed within days. A second IPO filing from May 2022 was withdrawn by July 2023.

## LEARNING CARE GROUP

Learning Care Group is the second-largest for-profit child care provider in North America. They operate 11 brands, including La Petite Academy, Childtime Learning Centers, Tutor Time, The Children's Courtyard, Everbrook Academy, Montessori Unlimited, AppleTree & Gilden Woods, U-GRO, Creative Kids Learning Centers, Young School, and Pathways Learning Academy. They have been owned since 2013 by American Securities, an American private equity firm.

The company that would eventually become Learning Care Group was founded in 1967 as Childtime Learning Centers. They were acquired in 1973 by Gerber Products, the child food company, and renamed Gerber Children's Centers. The company quickly expanded across the U.S., and was the first to open a corporate child care center in 1981 at the Hurley Medical Center in Flint, Michigan. Nonetheless, through the 1980s, Gerber focused its attention on child food, and began to sell off operations its unprofitable operations.

In 1990, Gerber sold its child care subsidiary, renamed as Childtime Children's Centers, to KD Acquisition Corporation. KD's strategy at the time was acquiring poorly managed companies and bringing them back to profitability. They focused on growth through the acquisition of employer-sponsored facilities, introduced management incentive programs to increase enrollment and operations efficiency, and launched a marketing campaign to target dual-income families. Childtime recorded $1 million in profits by 1993 (Reference for Business).

The company reincorporated as Childtime Learning Centers in 1995, and went public in 1996. They committed to opening 25 to 30 new facilities a year, targeting communities of home to dual-income households or office buildings. Through a mix of greenfield investments and multiple acquisitions, Childtime grew to operate 270 facilities across 19 states and DC. In 2002, Childtime announced plans to double their size by merging with Tutor Time Learning Centers, a Florida-based franchise company. In 2004, as the two companies merged their operations, they changed their name to Learning Care Group.

In 2006, the world's largest child care company, ABC Learning, became the second-largest child care provider in the U.S. through its acquisition of Learning Care Group and La Petite Academy; Learning Care Group's CEO, Bill Davis, was left to oversee ABC's U.S. operations.

ABC Learning's aggressive debt-financed acquisition tactics led to its collapse during the 2008 financial crisis. To pay off its debts, ABC[20] sold 60 percent of its U.S. child care operations under the Learning Care Group name to Morgan Stanley Capital Partners, Corporate Partners, Jacobson Partners, and Barclays Investment Bank for $420 million. Learning Care Group and La Petite Academy thus survived the crisis as a single merged entity. While it was owned by Morgan Stanley et al., Learning Care Group took on over $300 million in additional debt, before being sold five years later to American Securities for $700 million (Pitchbook). Since then, the company has continued its acquisition-driven expansion across the U.S., buyout out providers like Creative Kids Learning Center, UGro, and AppleTree & Gilden Woods.

[20] ABC Learning, a publicly listed company, continues to represent many of the risks associated with corporate child care provision. In 2008, at the time of its collapse, ABC operated 38 subsidiaries and a quarter of all child care facilities in Australia (Sainsbury 2008). That year, they faced a $1.78 billion dollar loss and were $2.7 billion in debt (Hurst 2010). The company was forced into receivership, and its director, Martin Kemp, stood trial for breaching his duties as director (he was found not guilty); ABC's chief financial officer admitted to concealing more than $46 million from shareholders (he was released on bond) (SBS News 2016).

## BRIGHT HORIZONS FAMILY SOLUTIONS

Bright Horizons Family Solutions is a publicly-listed child care chain that operates over 1,000 care centers in the U.S., Europe, and India. Its primary focus is on managing child care centers through employer-sponsored contracts.

Bright Horizons was founded in 1986 by Linda Mason and her husband Roger Brown, a management consultant at Bain & Company, using funding from Mitt Romney at Bain Capital, Bain & Company's investment firm spin-off. Their goal was to create a child care chain that would primarily serve large companies. The company grew to operate 130 centers by 1997, when it went public.  In 1999, Bright Horizons merged with CorporateFamily Solutions—a company founded in 1987 by Marguerite Sallee, who was similarly interested in expanding employer-sponsored child care—and became the largest child care business in the U.S. (Lattman 2013). The merged company took on the name Bright Horizons Family Solutions.

A decade later, amidst the 2008 financial crisis, Bain Capital took Bright Horizons private through a $1.3 billion leveraged buyout. Bain contributed $590 million to this buyout, and got a $850 million loan from Goldman Sachs Credit Partners (Flaherty 2008). Within five years, Bain's share of the company would be worth $1.4 billion, even as the company continued to be burdened with $922 million in debt, most of it tied to Bain's buyout (Dieterich 2013). Bright Horizons went public once more in 2013, issuing $222.2 million in new shares while allowing Bain to retain 80 percent ownership stake (Dieterich 2013). Bain sold $1.6 billion of its shares in 2014, losing majority control of the company; they sold the last of their holdings in 2018 to an undisclosed buyer (Pitchbook).

Since it went public in 2013, Bright Horizons has continued to grow through the acquisition of such companies as Little Unicorn Day Nurseries, Phoenix Day Nursery, Asquith Nannies, Yellow Dot Nursery, My Family Care, Steve and Kate's Camp, and Only About Children. Bright Horizons has also vertically integrated such businesses as Sittercity, an online marketplace that helps families find care providers, and GP Strategies, a tuition program management company (Pitchbook).

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