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M E M O R A N D U M

TO: Ontario Coalition for Better Child Care
Code Blue for Child Care

DATE: January 2, 2008 Matter No: 07-12

RE: Child Care Moratorium

Introduction and Summary

The following opinion was prepared for the Ontario Coalition for Better Child Care (OCBCC), and Code Blue for Child Care, and considers questions arising from a plan by private investors to acquire and consolidate the ownership of a large number of licensed child care centres in Ontario. In particular, we consider whether it is practical and lawful to establish a moratorium to prevent this acquisition plan from proceeding.

Over the past few months, daycare operators across Ontario have received letters sent on behalf of a "large financial/child care group" expressing interest in buying their child care businesses. Little is known about the investors behind these offers, but they appear to be closely linked to a multinational child care conglomerate. The potential impacts of these acquisition plans, and the pace at which they appear to be moving forward, have prompted calls for a moratorium to prevent such a scheme from proceeding.

The following opinion assesses the government's authority to declare and implement a moratorium on the acquisition and consolidation of existing child care centres. In this regard, it is our opinion that:

(i) Plans to consolidate ownership of existing child care centres raise serious questions about the compatibility of such a commercial scheme with the requirements of the *Day Nurseries Act* and the present direction of Ontario child care policy. These concerns provide ample policy support for declaring a moratorium that can readily be founded in the requirements of the Act as well as in the policy commitments of this government.

(ii) Under the *Day Nurseries Act*, the provincial cabinet has clear authority to promulgate a regulation that would restrict the acquisition and consolidation of child care licenses. Imposing such a moratorium would

enable the government to determine future policy direction with regard to the ownership of child care centres.

(iii) Such a short term moratorium could be crafted to prevent the conglomeration of existing child care centres without otherwise interfering with the issuance of new, or the renewal of existing child care centre licenses.

In a separate legal opinion, we considered the potential consequences of allowing significant foreign investment in the child care sector in light of Canada's international trade obligations. The essential conclusions of that assessment were as follows:

(i) Provincial governments currently have the authority to restrict or otherwise regulate foreign investment in the child care sector, including by way of imposing a moratorium on the issuance of child care licenses to certain private investors, without running afoul of international trade rules.

(ii) If, however, governments fail to use their authority to prevent significant foreign investment in the child care sector, they will invite the application of trade rules that limit their future policy and program options.

(iii) The unilateral right NAFTA accords foreign investors to claim damages where provincial initiatives impinge on their investments is of particular concern, because if substantial foreign investment is allowed in the sector, these litigation rights would present a significant impediment to present plans to establish a full day program for those attending junior and senior kindergarten.

Without the intervention of a provincial moratorium, it is possible that an international child care conglomerate will soon establish a dominant presence in Ontario's child care sector. Such a development would not only transform the character of child care services in Ontario, but threaten the policy and program flexibility this government needs to proceed with plans for expanding early learning and child care programs for Ontario children.

Given the likely consequences of such an international commercial scheme, it would be prudent for the government to exercise the clear mandate afforded by the *Day Nurseries Act* to declare a moratorium to prevent such an acquisition plan from proceeding. This would allow it to determine the future direction of Ontario child care policy, free from the undue influence of an international child care conglomerate.

The Facts

In recent months, daycare operators across Ontario have received letters[1] asking if they would be interested in selling their centres. The approach comes from Adroit Investments, a U.S. mergers and acquisitions firm, and states that it is being made on behalf of "a large financial/child care group purchasing child care centres across Ontario." Leslie Wulf, the US-based manager of the company who signed the letters, has referred media questions to an executive with a company named "123 Busy Beavers Learning Centres Inc." ("Busy Beavers"). That Canadian firm is a partner of 123 Global, an Australian firm that describes itself as the "growth engine" for an international child care conglomerate, ABC Learning Centres,[2] which is now one of the largest child care corporations in the U.S., the U.K., and Australia.[3]

While little has been made public about its plans, acquisition efforts by Adroit Investments and its corporate client or clients appear to be moving quickly. Over the past four months, 123 Busy Beavers, which is based in Oakville, has also registered in Alberta and B.C. Letters similar to those sent to Ontario child care operators have been sent to companies in both these western provinces.

While the relationships among Adroit Investments, 123 Busy Beavers and ABC Learning are murky, it is worth noting that the quality of the child care services provided by ABC Learning in Australia has come under scrutiny and criticism. An investigation carried out by the Australia Institute in 2006 raised serious concerns about the impact of company cost-cutting practices on the quality of care provided at some of its facilities, and called for further investigation and a tightening of regulatory controls.[4] Others have pointed to the company's problematic role in lobbying against regulatory reforms needed to improve the quality of care.[5]

Ontario's child care sector is currently dominated by non-profit child care centres, but a significant number of for-profit child care businesses operate in the province, and these operators are the target of the present acquisition campaign.

Apparent plans by this conglomerate to expand into Canada have caused concerns to be raised on a number of fronts. Research has shown that large corporations tend to focus on shareholder returns at the expense of quality of service.[6] There is also objection to the use of publicly-

[1] That letter reads, in part: "We represent a large financial/child care group purchasing child care centres across Ontario. Are you ready to see what your business is worth in today's market? The process is simple and all information is confidential ... If the centre meets our criteria we will make you an offer."
[2] Robert Cribb, Dale Brazao: 'Big-box' daycare coming to Canada: Industry worried as Aussie 'Fast Eddy' looking to expand his $2.2 billion empire, Toronto Star October 20, 2007.
[3] Idem.
[4] Idem.
[5] Brennan, D. (2007). The ABC of child care politics. Vol. 42, Winter, pp 212-217. *Australian Journal of Social Issues*.
[6] Cleveland, Gordon et al., "An Economic Perspective on the Current and Future Role of Nonprofit Provision of Early Learning and Child Care Services in Canada: Final Project Report" (March 1, 2007).

funded child care subsidies to fuel private profits rather than improve the quality of, or access to, child care.

As we have canvassed in a separate legal opinion, once foreign investment in the child care sector is permitted, the rights of such investors become vested under the North American Free Trade Agreement (NAFTA), and these include the right make damage claims where government measures impinge on those investments. Such investor rights have been asserted, or identified as formidable impediments to the expansion of public services, notably automobile insurance and health care. [7]

Foreign investment in the social service sector also engages trade agreement obligations that constrain public policy and legislative options going forward. For example, the presence of a foreign owned child care conglomerate would present a significant impediment to Ontario's plan to implement full-day learning for 4 and 5 year-olds. This is because investors have the right under NAFTA to claim damages where government measures diminish profits, as is likely to occur if publicly funded services displace private care for 4 and 5 year olds.

Finally, there is concern about the influence that a global child care conglomerate would exert on the development of child care policy and law in Ontario and nationally, particularly if the company's acquisition plans move ahead in other provinces. As noted, large child care corporations have and can be expected to use their influence and resources to discourage social policy reforms that are regarded as incompatible with corporate interests. In fact, ABC Learning Centres in Australia went so far as to lobby against improvements to maternity leave benefits.[8]

The Regulation of Child Care in Ontario

The regulation of child care services is Ontario is primarily governed by the provisions of the *Day Nurseries Act*, key provisions of which are summarized here and reproduced as Appendix "A" to this opinion.

Under section 11 of the Act, no person is permitted to establish, operate or maintain a day nursery or a private-home child care agency without obtaining a licence issued by a Director. There are two types of licensed[9] child care services that are permitted: day nurseries (commonly

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[7] See for example Jon Johnson; *How Will International Trade Agreements Affect Canadian Health Care*? Commission on the Future of Health Care in Canada, Sept. 2002; and David Schneiderman, *Investment Rules and the New Constitutionalism*, Law and Social Inquiry, Journal of the American Bar Foundation, Volume 25, Number 3, Summer 2000, pp. 757-787.

[8] Brennan, D. (2007). The ABC of child care politics. Vol. 42, Winter, pp 212-217. *Australian Journal of Social Issues*.

[9] Unregulated private home child care is also allowed in Ontario for individual caregivers who look after five or fewer unrelated children under the age of 10. The Ministry does not regulate these family child care homes and the caregiver does not have to meet provincial health, safety and caregiver training standards, nor be monitored by an agency.

referred to as child care centres) and private-home child care agencies. Child care centres may include nursery schools, full day care, extended day care, and before and after school programs.

Those who manage and control child care centres and agencies are defined as "operators" under the Act. An operator may be an individual, a corporation (non-profit or for-profit), municipality, community college, church, Band or Councils of a Band. Section 11(3) explicitly prohibits the issuance of a licence to a partnership or association of persons.

Operators have responsibility for the operation and management of each day nursery or private-home child care agency, including the program, financial and personnel administration of the program. Operators of licensed day nurseries and private-home child care agencies must comply at all times with the requirements of the Act and its regulations - principally Regulation 262. A licence issued under the Act is not transferable, and under Regulation 262, may not be issued for more than a one year period.

A Limited Moratorium on Issuing or Renewing Licences to Operate Child Care Centres Would be Effective and Lawful

A spokesperson for Ontario's Ministry of Children and Youth Services is quoted as saying that the Minister is "not in favour of commercialized, big box child care," [10] and we gather that this view is consistent with those expressed by officials in the Premier's office as well. However, we understand that Ontario officials have also raised questions about the effectiveness, lawfulness and justification of a moratorium on child care centre acquisitions. We address these concerns next.

As described below, a moratorium imposing limited constraints on the issuance or renewal of child care centre licenses in order to prevent the consolidation of existing child care centres by a large conglomerate would be practical, effective and lawful.

Would a Moratorium Be Practical?

For reasons that follow, a short term moratorium on the renewal of existing child care licenses for the purposes discussed here would, in our view, be both effective and practical. This is true even where the acquisition of an existing child care company takes places by way of a share transfer and does not immediately trigger the need to submit an application for a new child care license. However, it would be helpful in this regard for the government to declare its intention to establish such a moratorium as soon as possible.

[10] Cribb, *supra* note 2.

Because of the lack of transparency surrounding present acquisition plans, it not known whether the purchase of Ontario child care centres will take place by way of a share or asset transfer. The former is only possible where the operator is a corporation, and would involve the transfer of the shares from the company being acquired to the conglomerate. An asset transfer would work for acquisitions from all operators whether incorporated or not, and would typically involve the transfer of real estate, leases, contracts, good will and other assets of the child care business.

For practical reasons asset transfer transactions are more likely, although share purchase agreements may be favoured to preserve existing funding entitlements. In the case of an asset transfer, the licence to operate a child care centre is not transferable, so Adroit's client would have to apply for a new license under section 11 of the Act before the acquisition would have effect.

If, on the other hand, an acquisition takes place by share transaction, no new licence application may be required. However, under s. 11(7) of the Act, where a licensee is a corporation, it must notify a Director in writing within fifteen days of any change in the officers or directors of the corporation. Moreover, s.12(2)(e) stipulates that a change in the officers or directors of the applicant may afford grounds for refusing a licence when renewal of the license is sought, and this must occur before the license expires on or before the one year anniversary of its issue.

In these circumstances, it would be imprudent for anyone acquiring shares in a company operating a child care centre to not first ensure that a renewal of corporation's licence will be granted. In any event, existing licence holders would be apprised of a moratorium that would limit the sale of their centre to a large conglomerate, and as noted, the Minister should announce the Government's intentions as soon as she can.

Would a Moratorium be Lawful?

We also understand that questions have been raised about the lawfulness of the moratorium that has been proposed. Reference is made to an alleged legal challenge to a moratorium by Quebec on the issuance of new child care permits to for-profit operators. However, we can find no record in the reported case law of such a challenge. More importantly, the Quebec moratorium in question, which is analogous in some respects to the one being proposed, remained in place for the full five year period for which it was established.[11] While a legal challenge to Quebec's moratorium might have been mounted, if this was the case it apparently was unsuccessful.

[11] The first moratorium established by Quebec on new permits for child care services was established for a year from April 1995. In May, 1996, the government announced that for-profit centres would no longer receive funding in Quebec. This restriction was later modified somewhat when the new family policy was introduced in 1997.

At that time Bill 145 [1997 Chapter 58] *An Act Respecting The Ministere De La Famille et de L'enfance and Amending the Act Respecting Child Care*, established a five year moratorium on the issuance new child care licenses to for-profits operators. That moratorium endured for the full five year period which ran from June 11 1997, to June 12 2002.

As well, our review of the case law indicates that public officials have authority to implement a moratorium, even without a regulation explicitly authorizing such a constraint, so long as the decision to do so is not abusive or irrational.[12] Nevertheless, while the case law supports the imposition of a moratorium as an administrative measure, the more prudent course in our view would be to proceed by way of regulation.

In fact, the Ontario government has established moratoria on several occasions - examples include:

- in 1987, under the *Pension Benefits Act, 1987*, a moratorium was placed on surplus withdrawals from ongoing pension plans;[13]
- in May 2000, a moratorium was imposed on the sale of all coal-fired electricity plants in the province, pending a review of options for environmental protection (the moratorium was lifted October 24, 2001);
- in 2001, a moratorium was put in place on hunting wolves in and around Algonquin Park;
- in 2003, a moratorium was established to prohibit certain school closures;
- in 2003, under the *Ontario Water Resources Act,* a one-year moratorium was declared on the issuance of new water-taking permits or permits that would authorize an increase in the amount of water that would be taken for uses that remove water from watersheds.[14] The moratorium applied only to certain areas of the Province and to certain industries; and
- in June, 2000 Ontario imposed a three-year "pause" on the expansion of new charity casinos, new commercial casinos and slot facilities at racetracks. In 2003, the Ontario Government announced a 12-month extension of its moratorium on introducing gaming to new host communities.[15]

The respective authority of the Cabinet and the Minister to make regulations is set out under s. 18 of the Act. Cabinet's authority to do so is broadly framed, and in our view, clearly engenders

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In that same year the Quebec Assembly passed Bill 11 [1997 Chapter 16] *An Act to Amend the Act Respecting Child Day Care and other Legislative Provisions.* Under the Act, public funding to for-profit operators was significantly restricted.

[12] *1018025 Alberta Ltd. v. Canada (Minister of Health),*(2004), 21 Admin. L.R. (4th) 163.

[13] (R.R.O. 1980, Reg. 746, s. 21(2), as am. by O. Reg. 31/87), which was extended to plans on wind-up in 1988 (O. Reg. 708/87, s. 7a (added by O. Reg. 100/88)).

[14] "The Taking and Use of Water" Ontario Regulation 434/03 was filed and came into effect immediately.

[15] Requirements For Establishing A Casino Or Charity Casino, O. Reg. 347/00, *Ontario Lottery and Gaming Corporation Act*, 1999, S.O. 1999, c. 12, Sch. L

the power to implement a moratorium on renewing or issuing child care licenses where the effect of issuing such licenses would be to authorize a large chain of child care facilities.

In addition to the general authority accorded by s. 18. (1) to make regulations "governing the management, operation and use of day nurseries", authority is also provided to make regulations

> *(h) governing the issuance, renewal and expiration of licences and the fees payable by an applicant for a licence or renewal thereof;*
>
> *(s) prescribing additional powers and duties of a Director;*
>
> *(u) for the purposes of this Act and the regulations, defining "services" and "facilities" and prescribing classes of services and facilities;*
>
> *(w) exempting designated approved corporations, day nurseries, municipalities, delivery agents, bands, or private-home day care agencies from specified provisions of this Act or the regulations for such period or periods of time as the regulations prescribe; . . .*

Accordingly, in our view there is both legal authority and past practice to support and sustain government action to foreclose efforts to acquire and consolidate a large number of Ontario child care centres.

Is There a Sound Policy Justification for a Moratorium?

There are several grounds upon which a time-limited moratorium to prevent the wholesale acquisition and consolidation of existing child care centres can be justified. At first instance such action is warranted simply to provide an opportunity to consider important questions about such an unprecedented development in a key area of social service delivery. For example: is a large scale consolidation of child care centres compatible with current policy direction for child care?

In addition to this broad policy concern, there are a number of specific questions that would need to be answered to know whether present acquisition plans are consistent with the purposes and requirements of the *Day Nurseries Act*. It is important to note that the Act speaks to issues of corporate organization and governance, and specifically indicates that issues of competence and past conduct may warrant refusing a licence to operate a child care centre.[16]

There is the question of whether the Ministry's current regulations and administrative procedures are sufficient to regulate the establishment a large child care conglomerate – in our view, they are not. Existing Ministry licensing practices impose only very limited information and disclosure requirements on applicants for new licences or licence renewals. These would not elicit information that we believe is key, if the Director is to make informed judgment about

[16] S. 12 of the Act.

a plan by an international conglomerate to establish a dominant position in the Ontario child care sector. Moreover, much of this information relates directly to the statutory standards of the Act and would require answers to the following questions:

- Does the conglomerate plan to establish a franchise system or will centres be owned and operated by one corporation?
- Does the conglomerate plan to provide services to all Ontario communities, or will its operations be limited to certain urban centres?
- Does the conglomerate plan to apply for registration on a Canadian or foreign stock exchange or will it be privately owned?
- Is the conglomerate a subsidiary of an international or foreign corporation, and if so where and by whom will decisions about management and administration be made?
- To what degree will Canadian operations be insulated from solvency or other financial problems that may affect a parent or related corporation based outside the country?
- To what extent will the conglomerate be owned by foreign investors, either individual or corporate, and would any or all of these investors be resident in the United States, Mexico, or in any of the other countries with which Canada has negotiated an investment treaty?
- What is the nationality and residence of the members of the Board and senior management?

In addition to these questions, there are also issues relating to the capital structure of the corporation which may affect the affordability of child care services or the disposition of public subsidies provided to centres acquired by a conglomerate. Critical in this regard are the costs of acquisition and the ongoing demands of the capital and debt structure of the child care conglomerate. If these are unsound, the chain may fail. If investor demands for a return on capital or the debt burden of the conglomerate are too high, significant pressure to raise fees and/or cut costs may undermine access and/or quality of care. One can also imagine the pressure for increased public subsidies that would follow a sharp increase in child care fees for a large number of parents across the province. Moreover, in this circumstance, subsidies would be diverted to finance the cost of the conglomerate's shopping spree rather than improve quality of and access to child care.

The need to answer these questions and to thoroughly assess the implications of this corporate acquisition campaign provides more than ample justification for imposing a moratorium on the consolidation of child care licenses and belies any suggestion that in doing so, the government is behaving in a manner that is abusive or irrational. A moratorium would also provide the

Ministry with an opportunity to review its current policy on the expansion of for-profit child care services, particularly in light of the potential consequences brought to light by present plans to acquire and consolidate ownership of existing for-profit operators.

It would be important for the Minister set out the rationale for a moratorium in a policy statement, which she is authorized to proclaim under s.18(2)(c) of the Act.

One final point on the policy context for a moratorium, and this arises from an understanding of Ministry concerns regarding the interest that child care centre operators may have in selling their businesses. To begin with, a moratorium need not constrain the right of existing operators to sell their businesses, so long as the sale is not part of a large acquisition scheme. In this regard, the moratorium would simply preserve the status quo.

We also believe that it is alien to the purposes of the *Day Nurseries Act* to regard child care licenses as commodities, and it would be improper for concern about the resale value of child care centres to influence policy decisions made under the Act. In fact, by limiting the term of child care licenses to one year, by prohibiting their transfer, and by requiring prompt notification of ownership changes - the Act expresses a clear intent that licenses not be considered a tradable asset to be bought and sold in the marketplace.

A Moratorium on the Conglomeration of Child Care Centres in Ontario

The intent of the moratorium proposed would be to prevent the acquisition and consolidation of existing child care centres under the management and control of a large conglomerate. To do so, a regulation should be promulgated by Cabinet pursuant to the authority it has been accorded under s. 18 of the Act. Such a regulation should:

- impose a strict limit on the aggregation of child care licenses;
- prohibit the establishment of such a conglomerate by other means, such as by way of new applications or a combination of renewals and new applications, or by greatly increasing the number of children attending a particular centre;
- impose limits on the increase in the number of children or services that may be provided by an existing operator;
- prevent related companies or individuals from circumventing the intent of the regulation;
- not impede the growth of child care services according to customary norms, and therefore allow for both new applications and renewals of existing licences;
- not apply to non-profit, municipal, Band or Council of a Band child care operators;

- specify the sufficient time for the moratorium to be in place to allow the Ministry to develop and implement a policy concerning the regulation of investor-owned child care centres.

The regulation should also be accompanied by a policy statement that would:

- set out the rationale for the moratorium;
- delineate the issues to be addressed during the moratorium period, and
- describe the processes that it will use to determine future policy.

As noted, given the requirements of the Act and regulations relating to ownership, management and control of child care centres, there are several questions that it would be important for the government to address during the moratorium. These would include:

- Should foreign investment be permitted in the child care sector?
- Should child care franchises be permitted?
- Is there a need to impose limits on the number of child care centres that can be operated by the same or related entities?
- Should publicly traded companies be licensed to provide child care services?
- Are the requirements of the current licensing process adequate to achieve the objectives and purposes of the Act?
- Is there a need for greater transparency concerning the ownership and management of operators?
- Is there a need to strengthen social service safeguards under NAFTA the WTO or the Agreement on Internal Trade?
- Should operators be required to include parents in managerial decisions?
- Should operators of child care centres be limited to public, non-profit and First Nations operators?
- How should the implications of trade agreements be reflected in future policy and legislation?
- Should for-profit child care service providers receive public funding, either directly, or indirectly?

Given the demonstrable failure of current federal child care policies, and the uncertain status of Bill 303, which would assist the establishment of a pan-Canadian and publicly funded child care program, the moratorium would allow the federal government to provide some greater guidance with respect to the future direction of its child care policies and programs.

It is clear that a large scale corporate consolidation of Ontario's child care sector has far reaching implications that may significantly overwhelm provincial policy options, including those needed to implement full-day programs for children in kindergarten. It would be prudent, therefore, for the government to establish a moratorium to provide an opportunity to consider future policy directions for early learning and child care in Ontario before these are, at least in part, foreclosed by the fiat of global markets.

Sincerely,

Steven Shrybman

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