

Education Report: Initial advice on the transition to the Unified Funding System

To:	Hon Chris Hipkins, Minister of Education		
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Security Level:	Budget Sensitive	METIS No:	1257299
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Messaging seen by Communications team:	No	Round Robin:	No

Purpose of Report

This report seeks your decision on how you wish to approach the transition to the unified funding system, which may include a funding transition to new funding rates. This transition sits within the broader implementation approach for the unified funding system as a whole.

Summary

This report recommends that you take decisions on transitioning to the new system once modelling work currently underway is completed in the last quarter of 2021. The approach to transition will inform implementation planning and its associated timeframe. If you agree, we will provide you with advice on an approach to transition at the same time as other advice based on modelling in October 2021. This advice will include whether we consider rates to transition between the current and new funding systems will be needed, and if they are, the options for this transition. It will also cover initial advice on the operational approach to transition, including the pace of change.

For most providers the unified funding system (UFS) will involve significant behaviour shifts to meet the aims of the system change. These changes will take time and providers will need support and time to successfully implement them. These shifts include encouraging the growth of work-integrated delivery models and better meeting the needs of learners, their communities and employers.

It will be important to give providers as much certainty as possible about both the changes required and the pace at which changes are needed, as they move into the new funding system. It is likely that Budget 2021 announcements will provide a level of assurance to providers about the future funding available to support the UFS shifts. Implementation of the UFS from 2023 will need to balance expectations of providers as they move toward meeting the aims of the UFS while considering the impact on their financial position, their ability to respond to UFS shifts and the government's overall ability to maintain the network of provision to deliver UFS changes.

Modelling of data collected from the sector by October 2021 will enable us to better understand the distribution of modes of delivery and potential implications of the UFS funding across the system. Drawing on this modelling and on principles we have developed to frame the analysis,

we intend to provide further advice on the funding rate transition and the approach to implementation of the UFS, taking into consideration the policy and operational detail of the UFS components. This would allow us to provide you a whole of system view on the overall transition and implementation of the UFS. We would also advise on the phasing and duration of transitional arrangements which will set the pace of the change. This would include initial advice on the operational details for any transitional arrangements with more detailed advice in early 2022.

This approach would also enable us to provide more comprehensive messaging to the sector in late 2021/early 2022 on how the different UFS components work together and would provide a more complete picture of how their funding would be calculated. As in this approach it will not be possible to indicate transition funding levels to the sector ahead of this time, we suggest that interim key messages be communicated to them on the high level aims for transitions and on when we expect to be able to provide information on a transitions approach. This can provide reassurance that during implementation of UFS and shifting to new funding rates we are seeking to support a smooth and managed transition for providers, giving them time to adjust to the UFS, with the aim of minimising disruption to the network of provision.

Alternatively, if a change was required that was faster than the sector's ability to adapt, this could undermine valuable provision, or lead the sector to superficial/gaming behaviours that attract funding without genuinely delivering on the Reform of Vocational Education (RoVE) aims.

Recommendations

The Ministry of Education and the Tertiary Education Commission recommend that you:

- a. **note** that a transition approach will be needed to support providers as they make the behavioural shifts needed for the unified funding system, and that this may include a funding transition
- b. **note** that any transition arrangements for the unified funding system should seek to move as fast as possible to support the unified funding system roll-out, while taking into account the pace at which the sector can adapt

Proposed approach:

- c. **agree** that we will provide further advice to you, following modelling in the last quarter of 2021, on whether we consider a funding transition will be needed, and if so, on options for this, including the pace of change required for providers to shift into the new system (**recommended**)

Agree / **Disagree**

- d. **agree** that we will communicate to the sector about the high level aims for a transition approach to the unified funding system and when we expect to be able to provide information on transition arrangements (using the key messages in paragraph 27)

Agree / **Disagree**

Alternatively:

- e. **note** that, if you would like to take a faster transition approach, we can provide earlier advice on a funding transition approach which is not based on modelling (**not recommended**)

- f. **agree** that the following principles be used to guide consideration of potential funding transition arrangements:
- a) Enable a smooth transition at a pace that protects the network of provision and does not undermine the stability of provision to learners, employers and industry
 - b) Drive the UFS behavioural shifts while allowing time for providers to make appropriate business model adaptations
 - c) Protect funding for provision of national significance, including the Wānanga
 - d) Are transparent and understandable to the sector
 - e) Avoid overly complex implementation in support of driving UFS goals.
- Agree** **Disagree**
- g. **note** that the Ministry of Education intends to proactively release this education report once final decisions on the unified funding system for vocational education have been taken by Cabinet



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30/04/2021



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19/5/2021



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Background

1. In March you agreed that funding sought through Budget 2021 would ensure the viability of vocational education and training by supporting the sector to shift their behaviours to adapt to the RoVE changes, particularly the implementation of the UFS from 2023 [METIS 1244781 refers].
2. The approved Budget initiative is calculated as a 5% increase to total government funding estimated to be spent on VET in the 2022 calendar year, and a further 8% increase in 2023 [CAB-21-MIN-0116.29; Initiative 13359 refers].
3. Should you decide a funding transition is needed to set rates to transition between the current and new funding systems, rather than a direct shift into final UFS funding rates from 2023, we will advise on an approach for this. This would set the pace of change into the new system.
4. Specifically, advice on funding transition arrangements applies to funding distributed via the funding category and learner component rates. We will provide separate advice on the strategic component and how we consider this could be rolled out. Funding transition advice will not address broader issues, such as fluctuating numbers of international students.

Transition arrangements for funding can support providers to make the UFS behavioural shifts at a manageable pace

5. We have developed principles to guide our analysis of UFS funding transitions. These principles are that any such arrangements:
 - a) Enable a smooth transition at a pace that protects the network of provision and does not undermine the stability of provision to learners, employers and industry
 - b) Drive the UFS behavioural shifts while allowing time for providers to make appropriate business model adaptations
 - c) Protect funding for provision of national significance, including the Wānanga
 - d) Are transparent and understandable to the sector
 - e) Avoid overly complex implementation in support of driving UFS goals.
6. For a successful shift into the UFS, funding, and the expectations of behaviours aligned to this, will need to be paced to match the sectors' ability to adapt, as a whole.
7. Funding needs to stimulate the behavioural changes we want to see the sector make to respond to learner, employer and community needs, as well as supporting the growth of work-integrated learning. While some providers are already demonstrating these behaviours, many others will need to build their capability to do so, and make further investments such as changing how they use their current infrastructure or develop new models.
8. For providers, the shift to the new funding system will be happening alongside a series of other non-UFS factors requiring their response. These include any change from the domestic enrolment peaks this year, as well as whatever transition is agreed for the Targeted Training and Apprenticeship Fund and the Apprenticeship Boost.
9. We also need to consider the pace of funding change. If we required a funding implementation approach that was faster than the sectors' ability to adapt this could undermine valuable provision, and it may also lead the sector to adopt superficial or gaming behaviours that attract funding but do not deliver genuinely on the RoVE goals.

10. On the other hand, if we set an expectation for change that is too slow, we would lose the opportunity to incentivise providers to make changes while their new business models are being designed and embedded.
11. We know from international examples that signalling the appropriate pace in major funding system reforms can help to ensure sector capability and capacity to respond to change, including avoiding significant funding fluctuations for providers and flow on impacts for learners and industry. Tennessee, for example, has undertaken one of the most significant tertiary education funding reforms in recent years, shifting from entirely enrolment-based funding for public colleges to a new formula-based funding model. They put in place a three-year transition period over which time funding to colleges was adjusted in line with previous funding levels. Officials have told us that this transition approach as well as clear communication on the intended end state and journey towards it were critical to successful implementation.
12. The UFS implementation approach we develop will need to consider the other changes being undertaken in the RoVE programme at the same time and consider the timing of their implementation. It will also need to consider and minimise disruption that could be created by “uncoupling” the UFS part from the existing system, particularly for those TEOs that receive funding in foundation and higher education levels, such as Tē Pūkenga. Much of the operational policy and processes in the current system are similar or the same across all levels. Operational changes arising from the UFS could affect operational aspects of the rest of the system that we need to carefully manage.

Modelling data, available in the latter part of this year, can inform a comprehensive funding transitions approach

13. We do not yet have the information needed to advise on the appropriate pace for this shift into the fully funded UFS. In March this year we informed you that the first phase of data modelling will be undertaken by October 2021, after two rounds of data collected from the sector [METIS 1251762]. By March 2022, we will have a full year of data, and be able to confirm with you the final funding rates for the UFS.
14. We are currently collecting data that will allow us to understand the distribution of modes of delivery across the system. This will enable modelling of new rates including how these new rates impact at a regional, sub-sector and provider level. This modelling will cover both the funding category component and the learner success component as final funding amounts for a provider are largely derived from a combination of these two components.
15. This modelling will also support our assessment of whether transitional funding arrangements are needed. This would include identifying major shifts in funding amounts, either positive or negative, for providers and assessing their ability to adapt to these shifts. For example, a small provider receiving a large percentage increase to their funding may not be able to make full use of that increase to further UFS objectives in the first year. It may be better to allow them time for their business model to adapt to new requirements.
16. 9(2)(f)(iv)
[REDACTED]
17. If there are indications that transitional funding arrangements are needed, we will identify and analyse potential options for these, including considering the pace of change, and advise you on these in the latter part of this year.
18. We anticipate that there may be various challenges across the sector associated with moving into the new funding system. Provision of national significance, including that

of the wānanga, may face a particular risk to financial viability without a transitional arrangement for UFS funding to mitigate against funding fluctuations. Potential options for transition for wānanga will depend on decisions made as part of the wider Te Hono work programme.

19. As part of our analysis on funding transition arrangements drawing on the modelling, we will identify potential factors indicating risks to the vocational network of provision to best meet local, regional and national skill needs. These may involve subsectors, parts of subsectors or regions with low volumes of the type of provision we wish to support or for who learner distribution would generate lower levels of funding than currently received.
20. With your agreement, we would include your chosen funding transition approach together with the broad implementation approach for the UFS in a paper seeking Cabinet's approval in the latter part of this year. Following Cabinet's approval, a transition approach would then be communicated to the sector.

While early signalling is possible, the pace of change into the new system is better communicated to the sector later this year, following modelling

21. In UFS engagements to date a commonly raised concern across the sector is that the funding rates are communicated to the sector as early as possible. Providers will want clarity on the baseline funding they can expect to receive in 2023 (subject to amendments based on actual delivery) and how this will be affected by the UFS. The uncertainty about rates may challenge some providers' ability to develop and transition their business models, particularly in regard to new functions which we want to encourage, such as arranging training.
22. It is likely that a successful Budget 2021 bid will provide sufficient assurance to providers about the future funding available to support the UFS shifts. However, it will not be possible to identify providers' funding levels under the UFS until mid-2022. This does not provide much time for providers making business decisions in light of other RoVE changes and risks destabilising some providers.
23. We recommend that you make announcements later this year or early 2022 on a transition approach for the UFS following Cabinet decisions in November this year, and based on the modelling described above. The overall messaging provided to TEOs around the implementation of the UFS will need to provide the direction and shape of the system we are seeking to create, including specific information on how we plan to introduce and implement the UFS and the timeframe for implementation.
24. Some providers may wish to have more certainty than this would provide. You could consider providing earlier certainty by taking a decision shortly on simple funding percentage thresholds below which 2023 funding would not fall. If you wish to do this, we can provide advice on the potential options for this, and we would work to align this communication to the sector with Budget announcements.
25. However, there are several reasons why we do not recommend taking this approach. This advice would not be based on modelling and therefore while we could anticipate some likely impact scenarios, there would be a risk of inaccuracies. Further to this, we have concerns about the ability to convey clear and accurate early messaging to the sector about a transitions approach ahead of having comprehensive information about the shape and structure of the UFS as a whole and broad funding implications of the UFS. Additionally, there is a risk that such an approach could be seen as a signal that there is an intention for future funding cuts.

In the interim, informing the sector about expected timing for rates and overall aims for transitioning can provide some reassurance

26. As it will not be possible to indicate any transitional funding levels to the sector prior to the end of this year or early 2022, we suggest that interim key messages be communicated to them on the high level aims for transition into the UFS, and when we expect to be able to provide information on a transitions approach.
27. This can provide reassurance that during implementation of the UFS and in shifting to new funding rates we are seeking to support a smooth and managed transition for providers. This approach will give them time to adjust to the UFS, with the aim of minimising disruption on the network of provision. In addition to this key message we propose communicating the following points to the sector:
 - a) The UFS project has developed a range of policy proposals and have now entered the detailed design phase of most of these proposals.
 - b) Sector representatives from Tē Pūkenga and its subsidiaries, PTEs, wānanga, transitional ITOs and universities have been involved in this work since the end of 2019 and will all continue to be involved as required.
 - c) It is likely that volume-based funding rates will remain part of the system.
 - d) The UFS project has been working with the sector to collect new data to inform the detailed design work. This collection will also enable us to model and test the setting of funding rates and the distribution of funding between the three proposed components of the UFS. Modelling will take place in late 2021.
 - e) This means that we cannot provide information on UFS funding rates currently. We expect rates to be available in mid-2022.
 - f) We expect to be able to provide additional clarity about an approach for transitioning into the new system later this year or early 2022.
 - g) Officials will continue to provide as much information as possible on the direction and shape of the RoVE programme and the UFS.

Next steps

28. If you agree with our recommended approach, we will provide further advice to you in the latter part of this year on implementing transitions, including whether we consider a transition approach for funding will be needed from 2023.
29. This advice will include initial advice on the operational details for any transitional arrangements, with more detailed advice in early 2022.
30. If you agree, we will communicate with the sector shortly on the high level aims for transitioning to the new system, and when we expect to be able to provide information about an approach for transitions arrangements, using the key messages outlined above.
31. If you opt instead to provide earlier assurance to the sector, we can provide advice shortly on options for simple funding percentage thresholds below which 2023 funding would not fall.