

Report: Initial 2026 VET funding decisions

To:	Hon Penny Simmonds, Minister for Tertiary Education and Skills		
Date:	14 October 2024	Deadline:	17 October 2024
Security Level:	In-Confidence	Priority:	High
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Why are we sending this to you?

- You are receiving this to support a discussion about changes to vocational education and training (VET) funding, as part of your broader VET system redesign.

What action do we need, by when?

- We would like to discuss the contents of this report with you at our meeting on Thursday 17 October.

Key facts, issues and questions

- For your December 2024 Cabinet paper you will need to indicate main changes that you would like to make to the VET funding system, including the fiscally neutral rebalancing of funding between different elements.
- This report provides indicative options for the rebalancing of funding, advice on reducing the Learner Component and key considerations for the design of any new funds for ITPs.
- After we have discussed this report with you, we will provide you with a more detailed analysis of your preferred approach to inform final decisions for the Cabinet paper.

Alignment with Government priorities

1. This report supports the redesign of the vocational education and training (VET) system, which is one of your 2024 priorities for the Tertiary Education and Skills portfolio.

Background

The path to rebalance funding for vocational education and training

2. As part of your redesign of the vocational education and training (VET) system, you have indicated that you would like to change the basis on which Level 3-7 non-degree funding would be allocated. This affects both provider-based and work-based learning. Some providers also receive other funding (e.g. degree-level delivery, equity or research funding) which will not be affected by these shifts.
3. You have agreed to seek high-level decisions on the rebalancing of funding and objectives for the VET funding system in your upcoming Cabinet paper, alongside system design and legislation drafting decisions [METIS 1333759 refers]. More detailed decisions on funding, including rates, will be sought in 2025.
4. The consultation document included some key proposals for funding changes for 2026. Feedback on these proposals is covered in detail in the summary of submissions report [METIS 1336872 refers], but we have noted themes of feedback where they are relevant to the contents of this report.

This report is intended to support an initial discussion, with more detailed analysis and modelling to follow

5. This report provides material to support a discussion with you on:
 - a. the high-level distribution of funding across the VET system from 2026, including the future direction for the Learner Component; and
 - b. the merits and design of any new funds to support the activities and/or viability of institutes of technology and polytechnics (ITPs).
6. After we have discussed this material with you, we will explore the options that you indicate in more detail. We will then provide you with a further report for your final decisions as the basis of your December Cabinet paper.
7. You are also receiving reports about the design of the ITP network, standards-setting, and the work-based learning system [METIS 1336882 and METIS 1336883 refer]. Your decisions in these areas may influence the relevance of material included here. Subsequent advice will consider your decisions across the VET system design and how they interact to inform your final policy decisions.
8. We note that you have also received advice about the viability of ITPs. That advice is based on assumptions which may need to be adjusted based on your decisions about the balance and organisation of funding. We will work with the TEC to update this modelling as the design of the system progresses. At the same time, the advice you have received to date can inform your decisions about priorities for the funding system.

Objectives for funding changes

9. We would like to confirm our understanding of your objectives for changes to the VET funding system, noting that we have separately sought confirmation of your overall policy objectives for the redesign of the VET system [METIS 1336873 refers]. Based on your previous feedback and decisions to date, we understand your funding objectives to be:
 - a. supporting the quality and financial sustainability of provider-based and work-based VET;
 - b. ensuring the VET system delivers on regional priorities and responds to the needs of employers and industry;
 - c. enabling providers to support all learners to succeed; and
 - d. minimising the complexity of the funding system, including administrative and transaction costs.
10. Please indicate whether these reflect your objectives for the funding system changes or whether you have alternative objectives that you are seeking to progress.

Rebalancing the distribution of funding

The current system state

11. Prior to the introduction of the Unified Funding System (UFS) in 2023, work-based industry training and provider-based VET were funded through separate mechanisms, with work-based learning funded at comparatively low rates. The introduction of the UFS brought significant changes, including:
 - a. bringing industry training and provider-based VET together under one funding system with rates that include the mode of delivery;
 - b. separating funding into the Delivery Component (for core teaching and learning), Learner Component (to support learners and improve outcomes, particularly for underserved learner groups), and Strategic Component (to support the system to respond to regional and national skill priorities as well as programme development and maintenance);
 - c. increasing funding rates for work-based learning (at the expense of rates for provider-based learning) to support a more pedagogically intensive approach to this delivery and to incentivise more delivery in this mode; and
 - d. introducing an extramural delivery mode with a lower funding rate.
12. You have begun to unwind some of these changes for 2025, including lifting the extramural rate to match other provider-based delivery and an initial increase in provider-based delivery rates funded by the disestablishment of the Strategic Component. Decisions next need to be made about how changes from 2026 can support your redesign of the VET system.

Feedback from consultation

13. Feedback on the proposed funding changes for 2026 was mixed. More submitters supported the proposed changes than did not support them, but by a narrow margin. There was support for increasing funding to providers, and for ITPs being better equipped to

support regional needs. The most common feedback was that there is a need for more funding for VET overall.

14. We heard some concern about work-based learning funding being reduced, even among submitters who otherwise supported the proposals. Industry submissions in particular said that more work-based learning was needed and a reduction in funding would potentially run counter to this. One common theme was that standards-setting benefits the whole VET system and should not be funded only by reprioritisation from work-based learning funding.

Decisions for the next stage

15. The key decision that you will need to seek Cabinet agreement to in December is the extent that funding will be rebalanced between elements of the new VET system (both existing and new). This rebalancing is required to be fiscally neutral.
16. This paper focusses on the overall scale and direction of funding changes we understand you may wish to consider. Some funding system elements are dependent on your decisions in other areas. In particular, high-level funding considerations for the Hybrid model are outlined in the accompanying paper on standards-setting and work-based learning [METIS 1336883 refers].
17. Annexed to this report is a table identifying the key system functions that will require funding (**Annex 1**). The table provides three indicative options for each part of the funding system and seeks your direction on which is the closest to your preferred system settings. You are also free to indicate alternative options that you would like us to provide advice on. The intention of this table is to facilitate a discussion with you about how much funding you will need to move to different elements to achieve your objectives, while ensuring that the package of changes remains fiscally neutral (i.e. that the combined fiscal impact of your preferred options is close to zero).
18. Once we have discussed your preferred system settings we will prepare more detailed advice on a final package of changes for your consideration. This will include outlining impacts on individual providers and more detailed analysis to ensure that the package will be fiscally neutral for 2025. This advice could include more than one package for you to choose between if you are interested in exploring the impact of different funding choices in more detail.
19. We have made some assumptions in developing these indicative impacts, including that 'fiscally neutral' shifts should have the ability to fund the same amount of volume for both provider-based and work-based learning in 2026, based on current forecasts, as is currently funded under existing baselines. In practice the exact cost of a decision will vary if enrolment volumes are different to what is forecast.¹
20. The table only focuses on the total amounts of funding to be allocated to different system elements, rather than the structure of funding rates and criteria. You have expressed an interest in targeted funding increases for priority provision, and may wish to signal this intent to your colleagues in the December Cabinet paper. However, specific rates or targeting will not need to be confirmed until the 2025 Cabinet paper.

¹ At this stage we are using an indicative baseline of around \$910 million for VET funding in 2026, taking into account revised expectations for learner volume. We expect to have updated EFTS volumes forecasts in mid-October, after which we will be able to update you on forecasting and its impacts for 2026.

Redesign of the Learner Component

21. The Learner Component of the UFS was designed to encourage shifts across the VET system to meaningfully respond to the needs of learners. It replaced equity funding for VET delivery and is allocated using specific priority learner groups as a proxy for overall learner need, but with a focus on building better capability to support all learners (not just those in the identified learner groups). Having funding targeted towards supporting learners to succeed and achieve qualifications signals that this is a priority and part of the role of tertiary education organisations (TEOs).
22. You have indicated your intention to fund increased provider-based funding rates by reducing the Learner Component. This could involve changes to the basis on which the funding is allocated. However, the split of Learner Component funding between eligible learner groups would be confirmed in 2025 following further analysis and sector engagement.
23. You have agreed that the December Cabinet paper will focus on the overall pool of funding allocated for the Learner Component. The following discussion is intended to inform this decision by providing more context on how the Learner Component is allocated across the VET system, the impacts of proposed changes for TEOs, and how this funding component interacts with the recent Cabinet circular on needs-based service provision.

Feedback from consultation

24. While not all submissions commented on the Learner Component, most which did comment on equity issues did not support the proposed funding changes and saw the Learner Component as an important mechanism to drive improved outcomes for learners traditionally underserved by the VET system. Some submitters who did support the overall direction of funding changes voiced concerns about the impacts of this change for learner equity.
25. Many submitters raised support for priority learners as a good use for non-volume-based funding. Some expressed concern that TEOs would reallocate funds away from initiatives targeting priority learners in response to reduced learner-based funding. A few said that priority learners and equity did not seem to be centred in the consultation proposals.

Rationale for the Learner Component

26. Support for learners who have been underserved by the education system or need more help to succeed in VET was lacking under the pre-UFS system. This was particularly true in work-based learning, as the Industry Training Fund did not include any weighting for equity or funding earmarked for learner needs. Equity funding for provider-based learning under the Student Achievement Component (SAC) mechanism was based on Māori and Pacific learner enrolments only at Level 5 and above,² and was a very small proportion of overall funding (only 0.5% of total SAC funding in 2019).
27. The UFS committed more funding for a Learner Component (approximately seven percent of total VET funding), and introduced a new category for learners with low prior

² A small amount (\$29.41 per EFTS in 2022) was also allocated for supporting learners with disabilities, but this was based on total enrolments rather than the number of disabled learners, largely because disabled learners were not reliably identified in enrolment data.

achievement. The 2024 rates for the Learner Component and approximate allocations are shown below.

Table 1: Learner Component distribution across learner categories

Targeted learners	2024 learner component rates	Approximate total allocation	Percentage of Learner Component	Volume of learners (2022)	
Māori and/or Pacific learners at L1-2 (work-based) and 3-6 (all)	\$148.00 per EFTS	\$6.23 million	8%	39,240 EFTS	
				62% provider	38% work-based
Māori and/or Pacific learners at L7 (non-degree)	\$355.00 per EFTS	\$0.18 million	Less than 1%	473 EFTS	
				100% provider-based	
Learners with low prior achievement	\$1295.00 per EFTS	\$57.64 million	70%	41,492 EFTS	
				45% provider	55% work-based
Disabled learners	\$1295.00 per EFTS	\$18.06 million	22%	13,000 EFTS	
				54% provider	46% work-based

28. As Table 1 shows, Learner Component funding is allocated based on the volume of VET enrolments a TEO has which fall into specific learner groups. These groups are used as a proxy for the general support needs of learners at that TEO, because they have historically been underserved by the system and they can be identified in learner data.³ The largest portion of the Learner Component is based on low prior achievement criteria, which research indicates is strongly correlated with learning support needs – particularly for young learners.⁴
29. We consider that there is value in linking a portion of funding to enrolments of otherwise underserved learners, rather than providing funding undifferentiated by learner cohort. Learner-based funding recognises that TEOs who enrol more learners from underserved learner groups are likely to incur higher costs in supporting them, and it better incentivises TEOs to invest in meeting those learners' needs. Building TEO capability to support high-needs learners is also expected to have positive benefits for all learners, not just those identified as priority groups.
30. However, in an environment where fiscal neutrality is necessary the benefits of the Learner Component must be traded off against the use of funding to support your other priorities.

Impacts of a reducing the Learner Component

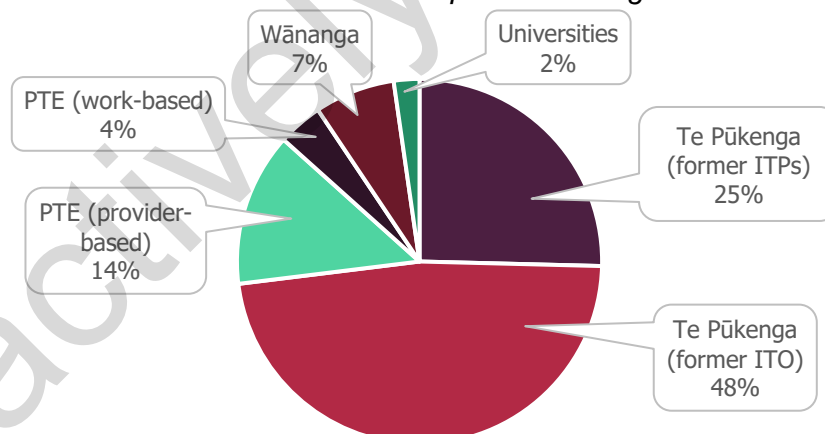
31. There are three key impacts from an overall reduction of the Learner Component:

³ While previous research has identified other factors that correlate with less success in education, such as involvement with police or mental health services, many of these would not be known to TEOs.

⁴ There is less correlation for older learners, for whom schooling or other prior education is less recent and thus less of a predictor of current ability.

- a. **Redistribution from work-based to provider-based learning:** over half of Learner Component funding is currently allocated to work-based training providers (see Figure 1 below). Shifting funding from the Learner Component to bolster provider-based delivery rates will result in a further reduction in the funding allocated to work-based learning, on top of any reduction to work-based funding rates.⁵
- b. **Redistribution from TEOs with more underserved learners:** with more funding allocated on the basis of EFTS volume rather than particular learner factors, there may be a redistribution away from those TEOs in the system who enrol high volumes of underserved learners (although they may also benefit from any resulting increase in provider-based funding). This may also reduce incentives on TEOs to seek to attract enrolments from these learner groups. About 73% of Learner Component funding is currently allocated within Te Pūkenga (see Figure 1), although smaller organisations may experience a larger proportionate impact from changes to their funding.
- c. **TEOs potentially changing the level of support they provide for underserved learners:** TEOs are expected to support priority learners as part of their general operations, not just based on Learner Component funding. However, TEOs may see funding allocated through a different mechanism as being for 'core delivery costs' and allocate less to learner support initiatives as a result. If this eventuates it could affect completion rates over time. The learner success expectations set by the TEC can mitigate this, but we would still expect this change to have an impact on TEO decision-making. This is a particular risk for organisations that did not have strong learner support systems before the introduction of the UFS.⁶

Figure 1: Current distribution of Learner Component funding



32. Because approximately 92 percent of Learner Component funding is allocated based on the low prior attainment and disabled learner criteria, any significant reduction in the total amount of Learner Component funding will require reductions in funding rates for one or both of these groups. These funding rates were the focus of increased learner-based

⁵ If you proceed with the Hybrid model for work-based learning and standard-setting, there will be a future decision about whether learner-based funding is attached to funding for ISBs or providers.

⁶ Te Pūkenga has overall been slow to implement changes in work-based learning since the introduction of the Learner Component, but some PTEs have developed learner-centric models for their work-based learning programmes. Future arrangements will depend partly on your decisions for work-based learning.

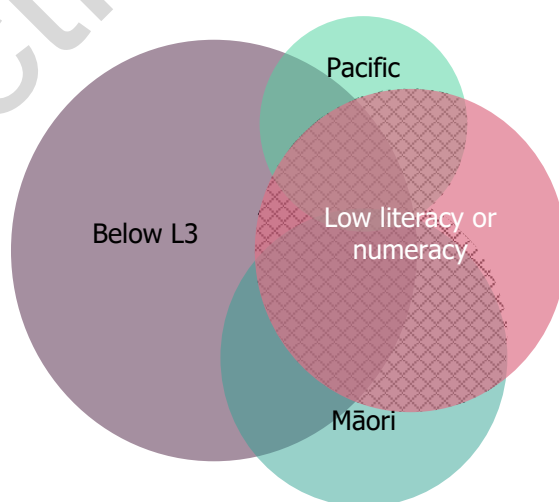
funding in the UFS because they represent factors identified as among the most significant indicators of need.⁷

33. You will have options to mitigate some of these impacts when making decisions about the rates and criteria for 2026, which will shape how the amount you allocate for the Learner Component is distributed across the VET system. You may also wish to consider how you convey your expectations for how providers support learner success and disabled learners, and how Learner Component funding interacts with those expectations.

Needs-based service provision

34. A recent Cabinet circular [CO (24) 5 refers] states that when targeting public services, “all variables should be considered before ethnic identity is automatically used to determine need.” In light of this circular you have the option of reviewing Māori and Pacific learner enrolments as a basis for Learner Component funding (approx. \$6 million total Learner Component funding). While you may wish to signal direction on this in the December Cabinet paper, final decisions would not need to be taken until the 2025 VET funding Cabinet paper.
35. Our view is that the Learner Component policy as it currently exists is not inconsistent with the circular. While the specified learner groups are used for calculating TEOs’ funding allocations, the funding mechanism is clear that TEOs should “identify the unique needs of all their learners ... make decisions about how to support them, and fund accordingly,” rather than use this funding only for the benefit of specific learner groups.
36. There are evidence-based policy reasons to use these learner groups as part of our proxy for overall learner needs. The specified learner groups correlate with needs which are more difficult to identify and target. At the time of the design of the UFS, research showed that around 80 percent of young people aged 18 to 25 who were identified to have low literacy and numeracy were also Māori and/or Pacific and/or had low prior educational attainment.

Figure 2: Overlap between young people aged 18 to 25 years with low literacy or numeracy and other target population groups (2014 population)



⁷ This was informed by data at the time the UFS was designed, and by earlier research (Earle (2018) *Factors associated with achievement in tertiary education up to age 20*, available in full and in summary on [Education Counts](#)).

37. The design of the Learner Component was informed by data that indicated the VET system did not serve Māori learners as well as other learners. Māori learners had lower rates of participation in apprenticeships compared to other industry training, slightly lower completion rates across VET, and were less likely to be in employment four years after completion.⁸ Where available, data for Pacific learners was similar.
38. The Government also has obligations under Te Tiriti o Waitangi | the Treaty of Waitangi to ensure that Māori people have equal access to educational opportunities and benefits. If the VET system is not producing equitable outcomes for Māori, funding is one lever available to support the system to move toward equitable outcomes. We are providing you with further advice on Tiriti considerations for the overall VET redesign, which will include funding implications.

Dedicated or incentive funds for ITPs

39. The consultation document sought feedback on establishing funding for ITPs to support specific purposes or roles they play in the VET system. Potential objectives for these raised in previous discussions and/or in the consultation document include:
- a. incentivising ITPs to engage with industry;
 - b. incentivising ITPs to engage with the development and workforce needs of their regions (including to help achieve the Government's target to reduce the number of young people not in employment, education or training (NEETs));
 - c. incentivising ITPs to attract more international student enrolments to regions;
 - d. 'base grant' funding to support the viability of ITPs; and/or
 - e. funding to support specific at-risk ITPs or ITP campuses.
40. To support your decisions about how funding is used for these objectives, we provide advice on the design and use of dedicated funding for ITPs below. At this stage the only decisions required are whether funding is set aside from the rest of the system for this purpose, and how much.

Feedback from consultation

41. We received a range of feedback on these proposals, with many submitters agreeing that it was important that ITPs be well-connected with industry and their region but some disagreeing that additional funding for these roles was appropriate. A few said that these behaviours should be part of the core business of ITPs, while others thought that other players in the system (e.g. employers, industries, regional development organisations) should contribute funding for what they wanted to see from education and training. Views were particularly divided on whether attracting international students to the regions was valuable or a distraction from a focus on New Zealanders.
42. Suggestions for other areas of focus included support for priority learners and for smaller, more remote ITPs that face challenges in providing for their regions. A few submitters, particularly from industry, said that ITPs were not the only TEOs contributing to these

⁸ Participation data in 2021 showed that 14% of Māori in VET were in apprenticeships compared to 23% of Europeans; 43% of Māori in VET enrolled at Level 4 and 16% at Levels 5-7, compared to 48% and 20% of European learners in VET respectively.

goals and all providers should have access to any additional funding. Many submitters also suggested allocating funding based on performance criteria.

Designing ITP funds

43. In addition to the trade-off involved in reallocating funding from other purposes (which we aim to explore with you in the discussion of **Annex 1**), we would like to discuss your objectives for these funds, whether these are best supported by ITP funds and, if so, the implications for the design of those funds. We will then come back to you with more developed options to meet your objectives in this area.
44. We have presumed that these funds would be allocated based on something other than enrolment volumes, unlike Delivery Component funding (although they could still be linked to the overall size of each ITP). While the funding system could alternatively set higher funding rates for ITPs this would raise concerns about competitive neutrality in the sector, particularly for Private Training Establishments (PTEs).
45. We have also presumed that any new fund is intended to be an enduring feature of the funding system, rather than a transitional measure for the ITP system. Many of the considerations outlined below would also apply to time-limited transitional support, but our assessment of options may be different in that case.

Non-volume-based funds can usefully support some sorts of objectives...

46. Non-volume-based funds are used in the funding system to provide incentives or supports that are different to those provided by volume-based funding. Table 2 outlines some of the purposes for which this style of funding mechanism has been employed in the past.

Table 2: Non-volume-based funding in the New Zealand tertiary education system

Purpose	Example
Incentivising providers to develop new programmes or supporting innovation	Programme Development and Maintenance Fund (2023-2024) Entrepreneurial Universities Fund (2017-2023) Te Tahua o Te Reo Kairangi (2023-present)
Supporting otherwise unviable provision that is regionally or nationally important	Strategic Component of the UFS (2023-2024) PTE Transitions Fund (2023-2024)
Supporting delivery models and provider roles that have costs not adequately recognised in the funding system	TEO Component Fund (2006-2008) Wānanga medium-term funds (2022-present) Section 556 grants to the New Zealand School of Dance and Te Kura Toi Whakaari o Aotearoa: New Zealand Drama School (2005-present)
Incentivising providers to focus on an outcome that is not strongly correlated with enrolment volumes	Performance-Based Research Fund (2003-present) Wānanga Research Capability Fund (2008-2022)
Supporting a specific function	Centres of Research Excellence (2001-present) National Centre of Tertiary Teaching Excellence (2004-present)

47. More generally, non-volume based funds insulate specific funding from the fluctuations of learner volumes, improving provider resilience to enrolment shifts (but, in the process, dampening their incentives to respond to changing learner demand). The TEO Component, and to a lesser extent the Strategic Component of the UFS, were examples of funds that sought to shift the overall balance of funding away from a 'one size fits all' approach on the basis of enrolment volumes.

...but tend to present difficult design and implementation challenges

48. Non-volume based funds tend to be more difficult to design and implement than volume-based funds, because they can require a more complex method of allocation and they lack the inbuilt incentives and accountabilities associated with funding providers for the enrolments that they attract. Whether distributed based on an application process or divided according to criteria, there is often more demand for funding than there is funding available.
49. Such funds can raise challenging questions about the basis on which funding should be allocated and how providers should be held accountable for the use of the funds, with trade-offs relating to simplicity, predictability, transparency and accountability. The smaller the total funding available to a provider through these mechanisms, the more strongly any associated administrative or compliance costs will be felt in comparison.

Whether ITP funds will be helpful will depend on what you want them to achieve...

50. As noted above, non-volume based funds are most likely to be appropriate where the objectives you are looking to pursue cannot be effectively met by the volume-based funding system. This is most obviously the case when funding an activity that is not strongly linked to enrolment volumes (e.g. research), but it can also be appropriate where the volume-based funding system does not recognise specific costs or priorities.

Recognising the broader public benefit provided by ITPs

51. Funds could seek to recognise the role that ITPs play in supporting regional, economic and social development. This funding would recognise the expectation that ITPs (as public institutions) maintain a sufficient breadth of provision, and that this is likely to involve retaining some provision that is of regional importance even when it is loss-making. This sort of fund could lend itself to a less complex design, as it would be primarily recognising a role that ITPs already play rather than trying to incentivise a behaviour shift. However, there would still be difficult questions about the basis of allocation and how to strike a balance between minimising compliance costs and demonstrating clear accountability for public funds.
52. An ITP fund of this sort could be criticised for giving public institutions an advantage over their private competitors. To mitigate this risk of perceived unfairness, any ITP-specific fund should be related to the unique role of ITPs in the VET system. The closest parallel in the current funding system would be the wānanga medium-term funds, which aim to recognise the distinctive role and delivery model of wānanga.

Incentivising particular behaviours from ITPs

53. The ability of an ITP fund to effectively incentivise particular behaviours or behavioural shifts from ITPs will depend significantly on its scale, how it is allocated, and its

accountability mechanisms. Methods which are likely to be most effective in incentivising ITPs to significantly alter their behaviour include allocation of funds:

- a. through a contestable process (but this creates significant compliance costs and reducing providers' certainty about future funding);
 - b. using a formula that measures, or uses a proxy for, the desired activity (which tends to be difficult to design and can lend itself to gaming, where the incentive is to meet the measure not the intent); or
 - c. by enabling the TEC to use some level of discretion in developing a methodology for calculating how much funding to allocate to each provider, based on the TEC's assessment of the provider's investment plan or against agreed criteria.
54. Alternatively the TEC could simply incorporate your expectations for ITPs into the broader investment plan process, but this would provide weaker incentives if it does not directly influence funding allocations. Performance measures and milestone payments can also support accountability for funding after the fact.

Supporting at-risk subject areas

55. If your objectives centre more on supporting delivery of particular subject areas that might otherwise be unviable, we would recommend considering targeted funding rate increases rather than new non-volume-based funds. Funding rate increases in areas identified as at-risk by the Specialist Advisors (e.g. food and fibre provision) would support the viability of this provision for ITPs, while also creating a better incentive for other providers (especially PTEs) to pick up this provision if an ITP withdraws from that part of the market.
56. Targeted funding rate increases are less likely to be effective where provision is only at risk in some regions, or where the at-risk provision is in a small but important niche that does not have its own funding rate and relies on extensive cross-subsidisation. Alternative mechanisms could be considered (such as enabling the TEC to directly procure this provision), but are likely to be complex and would require significant further development.
57. While you may wish to signal your intention to target fund rate increases for priority areas in your upcoming Cabinet paper, you will not need to make specific decisions about rates or targeting until early 2025. It may also be useful to signal your intentions to the specialist advisors earlier to support their understanding of the viability of provision going forward.

Supporting specific at-risk providers

58. While ITP funds could be targeted to support particular at-risk providers, campuses or areas of provision, this is likely to be perceived as a 'bail-out' and could introduce moral hazard risks by reducing ITPs' accountability for their own financial performance. To manage these risks you may want to consider tying the use of these funds to other intervention powers. There may also be tensions between supporting an under-performing ITP and broader policy settings, for example a competitive model that allows ITPs to offer out-of-region provision.
59. Any allocation of funds to a particular provider or providers determined by Ministers (rather than the TEC) would need to come in the form of a grant under Section 556 of the

Education and Training Act 2020, which requires you to establish that it is in the national interest.⁹

...and should in turn inform the design of any new funds

60. While the detailed design of any ITP funds would not need to be finalised until the 2025 VET funding Cabinet paper, the December 2024 Cabinet paper will need to outline both the purpose(s) of any funds and how you expect they would work at a high level.
61. **Annex 2** outlines these key design decisions and some general information on benefits and drawbacks. We would like to discuss these matters with you, seek your indicative decisions and identify any areas where you would like further advice or analysis.

Next Steps

62. We would like to discuss the contents of this report and the tables of decisions in Annexes 1 and 2 as part of our meeting with you on Thursday 17 October.
63. After that discussion we will work to identify the impacts of your indicative decisions in more detail, and provide further advice for your final decisions to inform the upcoming Cabinet paper on the design of the VET system.

Recommended Actions

The Ministry of Education recommends you:

- a. **agree** that the objectives for VET funding changes are:
- i. supporting the quality and financial sustainability of provider-based and work-based VET;
 - ii. ensuring the VET system delivers on regional priorities and responds to the needs of employers and industry;
 - iii. enabling providers to support all learners to succeed; and
 - iv. minimising the complexity of the funding system, including administrative and transaction costs.

☒ Agree ☐ Disagree

OR

- b. **indicate** alternative objectives for VET funding

☐ Agree / ☐ Disagree

- c. **discuss** the contents of this report with officials, in particular:

- i. your indicative decisions on the distribution of funding across elements of the future VET system (**Annex 1**)
- ii. your indicative decisions on the design of any ITP fund(s) to be introduced as part of the future VET system (**Annex 2**)

☒ Agree ☐ Disagree

⁹ Legislation prevents your design of a funding mechanism for the TEC from requiring funding to be allocated to a specified organisation or specified organisations.

- d. **note** that officials will subsequently provide more detailed analysis of the impact of your indicative decisions as well as of any further options you would like to consider.

Noted

Proactive Release:

- e. **agree** that the Ministry of Education release this paper after Cabinet has taken further policy decisions on VET funding in Q1 2025, with any information needing to be withheld done so in line with the provisions of the Official Information Act 1982.

Agree / Disagree



James Campbell
Senior Policy Manager
Tertiary Education and Evidence
14/10/2024

Hon Penny Simmonds
Minister for Tertiary Education and Skills

14/10/24

Annex 1: Overall funding shifts

Funding component	Key considerations	Indicative options	Rationale	Approx. fiscal impact	Approx. sector impact (not factoring any targeting)	Indicative preference
Provider-based funding rates <i>(scale of increase)</i> Starting point: ~\$550 million	<ul style="list-style-type: none"> Increased funding for provider-based delivery will benefit both public and private providers. While it will improve the viability of provision, courses, programmes and providers with low enrolment levels will still face significant viability challenges. You may wish to target funding rate increases towards at risk areas and/or priority subjects. You do not need to confirm the details of any targeting in the December Cabinet paper but may wish to signal your approach. The scale of any increase as well as the nature of any targeting will also impact the modelling of ITP viability. 	A. A small increase , equivalent to a further 4 percent above 2025 levels (in addition to any cost adjustment through Budget 2025)	<ul style="list-style-type: none"> You want to improve the viability of provider-based delivery, but do not want to make significant reductions to Learner Component and/or trade this off against WBL funding rates, ITP funds and standard setting 	-\$22 million	+\$10.8m for ITPs +\$6.5m for PTEs +\$3.8m for Wānanga +\$0.9m for universities	
		B. Returning average funding rates back to the cost-adjusted equivalent of pre-UFS level – about an 8 percent increase above 2025 levels	<ul style="list-style-type: none"> You want to prioritise getting provider-based rates back to the equivalent of pre-UFS levels (although potentially targeted differently) and are comfortable with significantly reducing a combination of learner component and WBL funding 	-\$44 million	+\$21.6m for ITPs +\$13m for PTEs +\$7.6m for Wānanga +\$1.8m for universities	
		C. A larger increase to provider-based rates above pre-UFS levels, equivalent to 12 percent above 2025 levels	<ul style="list-style-type: none"> You want to significantly improve the viability of provider-based delivery and are willing to prioritise this over other funding. You may wish to consider this option as an alternative to dedicated ITP funds 	-\$66 million	+\$32.4m for ITPs +\$19.5m for PTEs +\$11.4m for Wānanga +\$2.7m for universities	
Learner Component <i>(scale of decrease)</i> Starting point: ~\$70 million	<ul style="list-style-type: none"> Reductions would contribute to a shift of funding away from work-based delivery, and proportionately away from those providers who enrol more underserved learners. Reductions are likely to impact on the amount of resource providers dedicate to supporting underserved learners, although you have noted that your expectations of TEOs to provide for learners would remain the same. TEO compliance costs could reduce with less funding to track and report on and fewer milestones. Whaikaha and disability advocates have raised concerns about funding for disabled learners being reduced. There is potential for challenge on Treaty of Waitangi grounds if cuts to funding for Māori learners are perceived as failing to ensure Māori access to education. 	A. A small decrease to learner component, in the order of 20%	<ul style="list-style-type: none"> You want to make some savings from the Learner Component, but want to minimise the extent of rate decreases. 	+\$14 million	- \$6.0m from Te Pūkenga's work-based divisions - \$3.5m from ITPs - \$2.5m from PTEs - \$1.7m from Wānanga - \$0.4m from universities	
		B. A moderate decrease to Learner Component, in the order of 40%	<ul style="list-style-type: none"> You want to make significant savings from the Learner Component but leave flexibility to retain significantly higher rates for disabled and/or low prior achievement learners, compared to equity funding. 	+\$28 million	- \$12.0m from Te Pūkenga's work-based divisions - \$7.0m from ITPs - \$5.0m from PTEs - \$3.4m from Wānanga - \$0.8m from universities	
		C. A significant decrease to Learner Component, in the order of 60%	<ul style="list-style-type: none"> You want to fully fund a return to SAC-equivalent provider-based rates from Learner Component and are comfortable with significant reductions in all Learner Component funding rates. Learner Component would still be a larger proportion of VET funding than Equity funding is for higher education. 	+\$42 million	- \$18.1 from Te Pūkenga's work-based divisions - \$10.5 from ITPs - \$7.6 from PTEs - \$5.0 from Wānanga - \$1.3 from universities	

Funding component	Key considerations	Indicative options	Rationale	Approx. fiscal impact	Approx. sector impact (not factoring any targeting)	Indicative preference
Work-based learning (WBL) <i>(scale of decrease)</i> Starting point: ~\$290 million	<ul style="list-style-type: none"> Under current policy settings, Te Pūkenga is currently forecasting a WBL \$72 million surplus for its WBL divisions for 2024. While this indicates scope for rebalancing of funding, it also reflects the fact that Te Pūkenga has not made the desired improvements to delivery and student support, which were expected to add costs. If delivery rates fall too low, providers could be disincentivised from work-based training. Industry submissions have indicated that they value work-based learning and some industries rely on it heavily. Appropriate funding levels will depend on the final policy design of the WBL system. In particular, if you would like to adopt a hybrid model, then this funding will need to be sufficient to fund both WBL delivery and ISB coordination/pastoral care activity. As an example, Modern Apprenticeship Coordinators (2001-2014) received a per-learner subsidy rate that (at the time the scheme ended) was ~60% of the per-STM rate. 	A. A small decrease to WBL rates, in the order of 10%	<ul style="list-style-type: none"> You want sufficient savings from WBL rates to fund a low-cost standards-setting function, but want to retain rates that are significantly above pre-UFS levels, potentially with differential funding by subject area. More scope to separately fund WBL delivery and WBL coordination/pastoral care under the proposed hybrid model at this leave. 	+29.0 million	Based on current funding model and provision structure: - \$24.2m from Te Pūkenga's work-based divisions - \$4.8m from PTEs Funding impacts for the Hybrid model may differ significantly due to system structure changes. We will provide you with advice on this as part of the next VET funding paper.	
		B. A moderate decrease to WBL rates in the order of 20%	<ul style="list-style-type: none"> You want to make additional savings from WBL rates to either fund modest ITP funds or contribute to the cost of provider-based rate increases, while retaining WBL rates at above pre-UFS levels. Depending on the design of any hybrid model, it may be challenging to fund both WBL delivery and coordination/pastoral care. 	+58.0 million	Based on current funding model and provision structure: - \$48.4m from Te Pūkenga's work-based divisions - \$9.6m from PTEs	
		C. Significantly reducing WBL rates to the cost-adjusted equivalent of pre-UFS levels , a reduction of approximately 25%	<ul style="list-style-type: none"> You want to make significant savings from WBL rates and would like to revert to pre-UFS funding levels, including likely differentiating funding for apprenticeships and trainees. You are unlikely to be able to afford higher funding for some WBL subject areas and it may be difficult to adequately fund both WBL delivery and coordination/pastoral care at this level. 	+72.5 million	Based on current funding model and provision structure: - \$60.5m from Te Pūkenga's work-based divisions - \$12.0m from PTEs	
Standards setting <i>(amount of funding)</i> (currently \$65 million per annum until end of 2024/25 financial year)	<ul style="list-style-type: none"> WDCs are currently funded at \$65 million per annum, with a formula determining funding levels to each WDC. You have previously indicated that ISBs should receive around \$30 million per annum in Crown funding and have decided that you would like to provide for the option of industry levies to supplement this funding where supported by industry. Appropriate funding levels will depend on the functions you want ISBs to perform, the number of ISBs established and any sectors shifted to NZQA responsibility. An increased number and diversity of providers may increase the amount of quality assurance work required of standard-setting organisations. 	A. Funding standards-setting at a significantly lower level compared to the current model, at around \$30 million per annum	<ul style="list-style-type: none"> You want to significantly reduce Crown funding for standards-setting from its current levels, with industry having the option to seek a levy that would supplement this funding. Without levy funding (or other alternative funding), standard-setters would need to significantly scale back core functions, meaning that standards are reviewed less often and existing products are prioritised over developing new ones for industry. 	-\$30 million	<ul style="list-style-type: none"> No direct financial impact, but would impact on capacity of standards-setters to develop and review standards, impacting relevance. Any fees charged by ISBs for their services (if permitted) would need to be paid by the sector. 	
		B. Funding standards-setting at around \$40 million per annum	<ul style="list-style-type: none"> You want to maintain a higher level of standards setting capacity than existed prior to current system but are comfortable with a reduction in core capacity. This is likely to mean standards are reviewed less often and existing products are prioritised over developing new ones for industry. 	-\$40 million	<ul style="list-style-type: none"> As above, although any impact would be lower. 	

Funding component	Key considerations	Indicative options	Rationale	Approx. fiscal impact	Approx. sector impact (not factoring any targeting)	Indicative preference
	<ul style="list-style-type: none"> You have indicated that industry levies could supplement this funding in the future. Under a hybrid WBL model ISBs would also receive both some funding for coordination and pastoral care. 	C. Funding standards-setting based on the current model, reduced to remove current WDC spending on skills leadership and improved operational efficiencies, at around \$50 million per annum	<ul style="list-style-type: none"> You want to maintain a standards-setting system with a similar level of capability to what exists at present, although with less focus on skills leadership. May still have an impact on core standards-setting functions. 	-\$50 million	<ul style="list-style-type: none"> As above, although any impact would be lower. 	
ITP fund(s) <i>(basis and level of funding)</i>	<ul style="list-style-type: none"> Key design considerations are outlined earlier in this paper and in Annex 2. The size of the fund should reflect the purposes that it is looking to achieve, the types of accountability mechanisms that it will have, and the trade-offs against other funding uses. 	A. No dedicated fund for ITPs	<ul style="list-style-type: none"> You want to maintain the competitive neutrality of the funding system and want to prioritise provider-based funding rate increases (or other funding uses) 	Nil	Nil	
		B. A modest fund for ITPs of around \$20m per annum, focused on recognising and supporting the broader regional economic role of ITPs.	<ul style="list-style-type: none"> You want to support the viability of ITPs, noting that the amount of funding will not be sufficient to offset the significant deficits being incurred by many ITPs. 	-\$20 million	Will depend on the allocation methodology (see Annex 2)	
		C. A significant fund (or multiple funds) of around \$40m to support and recognise the regional importance of ITPs, incentivise behaviour changes and potentially provide additional support for at-risk ITPs.	<ul style="list-style-type: none"> You want to support the viability of ITPs, reducing the scale of cost reduction required and viability risks to some ITPs. You may want to incentivise a different set of behaviours than volume-based funding. 	-\$40 million	Will depend on the allocation methodology (see Annex 2)	

Annex 2: Key design decisions for ITP fund(s)

Design decision	Options	Likely to be appropriate if:	Benefits	Drawbacks	Indicative decision
Number of funds	Multiple funds	You are looking to achieve multiple purposes that require different allocation methods or accountability arrangements	<ul style="list-style-type: none"> Allows for different funds with clearly specified purposes and different design choices 	<ul style="list-style-type: none"> Increase in administrative and compliance costs (for providers and TEC) Add complexity to the system Limited funding available for each fund 	
	Single fund	You want to focus on one or more objectives that can be supported by a single set of allocation and accountability arrangements	<ul style="list-style-type: none"> Minimises additional administrative cost and complexity Allows more flexibility for funding to support different purposes at different ITPs 	<ul style="list-style-type: none"> May be more challenging to support a range of different purposes 	
Allocation methodology	Equal funding per ITP	You want to support functions performed by all ITPs You are concerned about the viability of small ITPs	<ul style="list-style-type: none"> Low complexity Provides proportionately more support to smaller, potentially less viable ITPs 	<ul style="list-style-type: none"> Difficult to justify providing more resources per learner at smaller ITPs Unlikely to be a significant incentive for larger ITPs 	
	Funding scaled based on ITP size	You want to recognise per-EFTS costs associated with ITP provision	<ul style="list-style-type: none"> Relatively low complexity Funding would not necessarily need to be based solely on current EFTS 	<ul style="list-style-type: none"> Limited benefits compared to increased funding rates if solely based on enrolments Limited support for small ITPs with viability challenges 	
	Funding allocated based on a different formula (e.g. a proxy for internationalisation or industry engagement)	You want to incentivise a particular activity that is readily measured	<ul style="list-style-type: none"> May better incentivise desired outcomes Some measures will have low compliance and administration costs 	<ul style="list-style-type: none"> Appropriate measures that are not easily gamed may be difficult to develop Compliance costs can be high for some measures 	
	TEC determines allocation via investment plan process	You want flexibility for funding to be allocated to providers whose investment plans best support specified purposes	<ul style="list-style-type: none"> Integrates allocation into the existing investment plan process Strengthens the incentives on providers to focus on developing compelling investment plans 	<ul style="list-style-type: none"> Less transparent allocation methodology as it involves TEC discretion Uncertainty for providers 	
	Contestable funding	You want to support those ITPs who can make the strongest case that they will meet the objectives	<ul style="list-style-type: none"> Strongly incentivises providers Transparent and defensible process for public funds 	<ul style="list-style-type: none"> Compliance costs can be high Uncertainty for providers 	
	Funding allocated to specific at-risk providers (by the TEC based on criteria, or via a Ministerial grant)	You want to maintain provision in particular regions that might not otherwise be viable	<ul style="list-style-type: none"> Allows for funding to be targeted A grant provides the most ministerial control over funding allocation 	<ul style="list-style-type: none"> Moral hazard risks associated with supporting failing ITPs Grants are only permitted when in the national interest Use of grants could be seen as a politicising of funding decisions 	
Accountability arrangements	Reporting via Annual Report and future investment plans	Providers are intended to have significant flexibility, or the allocation methodology already provides strong accountability	<ul style="list-style-type: none"> Simple and low cost Highly flexible for providers 	<ul style="list-style-type: none"> Limited ex-post accountability for the use of funds 	
	Milestone payments	Funds are intended to be tied to a particular activity and could be released on achieving milestones	<ul style="list-style-type: none"> Incentivises providers to ensure that planned milestones are achieved 	<ul style="list-style-type: none"> Some uncertainty for providers 	
	Performance component	You want to send a strong performance signal to providers	<ul style="list-style-type: none"> Funding is closely tied to desired outcomes 	<ul style="list-style-type: none"> Performance measures can be gamed or can involve significant TEC discretion Compliance costs can be high 	