



Report: Next steps on VET funding from 2026

To:	Hon Penny Simmonds, Minister for Tertiary Education and Skills		
Date:	12 September 2024	Deadline:	20 September 2024
Security Level:	In-Confidence	Priority:	Medium
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Why are we sending this to you?

- You are receiving this report to inform a discussion with education officials next week.

What action do we need, by when?

- Your feedback is sought on the proposed process for finalising funding policy decisions, including the scope of funding policy decisions that would be sought from Cabinet in November 2024, and any other matters you would like advice on in early October following analysis of consultation submissions.
- Please return the signed paper by Friday 20 September 2024.

Key facts, issues and questions

- We seek your agreement to a phased approach to vocational education and training (VET) funding policy decisions, with the November 2024 Cabinet paper seeking agreement to the major system shifts and the detail of funding settings to be agreed by Cabinet in the second quarter of 2025 following further analysis and engagement.
- The November 2024 Cabinet paper is proposed to focus on the overall funding model for VET provision and the scale of the rebalance of funding from work-based learning towards provider-based delivery.
- We will provide you with advice on the substance of these funding decisions in early October after analysis of consultation submissions.

Alignment with Government priorities

- 1 This report aligns with Government priorities by proposing a phased approach to finalising changes to vocational education and training (VET) funding from 2026 to support the success of the entities that will replace Te Pūkenga and Workforce Development Councils (WDCs).

Background

- 2 This is the fifth in a suite of papers to guide the development of your November 2024 report to Cabinet following the current consultation on proposals to disestablish Te Pūkenga and implement a redesigned VET system.
- 3 This paper focuses on potential changes to the VET funding system that would be implemented from the start of 2026. It seeks your agreement to a phased approach to funding changes: initially via your November Cabinet paper; then further engagement on specific settings in early 2025; and final Cabinet decisions in mid-2025.
- 4 This paper outlines the decisions we propose you seek from Cabinet in November but does not seek to engage you on the substance of these decisions – we will provide you with substantive advice on these issues following the conclusion of the VET consultation process.

Confirming funding settings for 2025

- 5 For 2025, Cabinet agreed to disestablish the strategic component of the current funding system and use the funding to increase subsidy rates for provider-based VET by approximately 10 percent, and to fund extramural delivery at those rates. The Budget 2024 cost adjustment of 2.5 percent for all tuition subsidies means the rates will be around 12.5 percent higher in 2025 than in 2024. This is a first step in rebalancing funding across the VET system and will have a positive impact on the viability of some provision.
- 6 Consultation on the proposed variations for 2025 closed on Monday 5 August and you have received separate advice on consultation feedback and the proposed final funding determinations for your approval [METIS 1333713 refers].

Related work

- 7 This paper focuses on the structure of funding settings for VET funding from 2026. It does not cover managing the costs of reforming the VET system or related issues, such as the potential use of reserves and managing transitional costs. This will be part of advice later in the process once the future shape of the system and roles and responsibilities have been determined.
- 8 The paper also does not cover potential funding arrangements for the proposed federation of Institutes of Technology and Polytechnics (ITPs), as that depends on decisions about its nature and structure [METIS 1333758 refers]. This includes any additional funding for the Open Polytechnic to support administrative functions or how funding might be shared where Open Polytechnic programmes are used by member ITPs. Based on recent discussions with you, we understand that your current intention is for the Federation to not be established in a way that requires a dedicated funding stream for how it supports its ITP members.
- 9 It is also important to note that the development of your November Cabinet paper is occurring alongside initial planning for Budget 2025, including advice on managing cost and potential volume funding pressures across the tertiary system in 2026 and beyond [METIS 1335354 refers]. This will include advice on tuition subsidies for degree-level and above delivery,

which is a significant component of funding for many VET providers – particularly many of the ITPs.

ITP financial performance modelling

- 10 This paper has been developed in parallel with the Tertiary Education Commission (TEC), who are working with Te Pūkenga and its appointed specialist advisors on modelling the potential future financial performance of the former ITPs.

- 11 9(2) [REDACTED]
(b) [REDACTED]
(ii) [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

Consultation on potential changes to VET funding for 2026

- 12 The current consultation seeks feedback on high-level changes to VET funding settings from 2026 and commits to further engagement on details before they are finalised.
- 13 The consultation document proposes to use Learner Component funding to further increase subsidy rates for provider-based delivery as part of re-balancing funding to support the success of both provider- and work-based VET.
- 14 Alongside this re-balancing of funding, submissions and feedback are being sought on:
- a. how best to fund standards-setting and related functions; and
 - b. using funding to incentivise ITPs to:
 - engage with industries and other stakeholders to better support regional development and help reduce Jobseeker Support recipient numbers; and
 - bring more of the benefits of international education to regions.

Objectives for the design of the future VET funding system

- 15 Based on decisions earlier this year, we are seeking to confirm your objectives and intended direction of travel for changes to VET funding from 2026. While this remains subject to consideration of consultation feedback, we understand your current intent to seek Cabinet agreement in November to:
- a. further increase subsidy rates for provider-based delivery to what they would have been under the previous SAC system, funded by repurposing Learner Component funding;
 - b. create a dedicated funding stream for standards-settings and related functions by reducing funding rates for work-based learning; and
 - c. establish funding arrangements to incentivise ITPs to: engage with industries to support regional development and help reduce Jobseeker Support numbers, and maximise the benefits of international education for regional New Zealand.
- 16 In relation to the third proposal, the consultation document does not indicate where those funds might come from, but we understand your current intent is that it would be from reprioritisation of current funding for work-based learning. The potential role of a levy in funding standards-settings is discussed further below.

- 17 These will be significant changes to VET funding and require Cabinet agreement, with choices, trade-offs and risks made clear. We anticipate Ministers will have an interest in relation to support for disadvantaged learners, the relationship of funding for ITPs to that for other providers, and implications for work-based learning for key industries.
- 18 Presenting these decisions to Cabinet within the context of a principles-based framework could be a helpful way to communicate your objective of achieving a better balance of funding across the VET system. Recommended elements of the framework include that it be:
- a. Effective: Supports the success of a reformed VET system by:
 - supporting the quality and sustainability of provider-based *and* work-based VET;
 - enabling effective standards-setting that responds to and delivers for industries; and
 - providing regions with access to the VET they need for core industries;
 - b. Efficient: Is easy to understand and minimises administrative and transaction costs for providers, employers, learners and government;
 - c. Transparent: Reflects a relationship with costs of delivery, appropriately balances public and private contributions, and avoids unintended incentives; and
 - d. Equitable: Enables providers to support all learners to succeed, particularly those usually not well-served by the VET system.

Proposed approach to decisions on VET funding for 2026

- 19 We propose that you seek high-level decisions on VET funding settings from Cabinet in November, and seek Cabinet decisions on the details of funding settings in the second quarter of 2025 following further analysis and engagement. We see this approach as having the following advantages:
- a. It would allow the November paper to focus on policy decisions for the overall structure of – and roles and responsibilities within – the VET system and reduce the risk that the specifics of funding policy changes derail these critical broader decisions. You would then have the opportunity to work through these issues with your colleagues separately in the follow-up Cabinet paper.
 - b. It would limit the scope and complexity of policy decisions that you will need to make in early October, noting that many funding issues will not be able to be resolved until after you have made policy decisions on overall system design.
 - c. It would allow for further modelling and targeted engagement on the details of funding policy settings to ensure they will provide the appropriate resources and incentives to support your objectives for the redesigned VET system.
 - d. It would not delay finalisation of funding settings for 2026, which can only be confirmed following consultation on funding mechanisms in mid-2025 (as per statutory requirements).
- 20 Under this approach, it will be important to strike the right balance of providing Cabinet with sufficient clarity on the overall direction of the funding changes needed to support the redesign, without getting into the detail of how funding rates will be structured for 2026.

- 21 You would report back to Cabinet in the second quarter of 2025 with your proposed final structure and core policy parameters for VET funding. These would then be finalised by you following consultation on variations to funding determinations in Quarter 3 of 2025.
- 22 The proposed approach to decisions on the redesign of VET funding is summarised as follows:

<i>Proposed 2024 Cabinet decision(s)</i>	<i>Proposed 2025 actions and decisions</i>
<ul style="list-style-type: none"> • Overall scale of ‘rebalance’ from Learner Component and work-based learning to provider-based delivery • Indicative level of funding for standards setting and related functions and impact on work-based learning funding • Approach to further engagement on proposed funding changes in Q1 of 2025 • Establishment and policy intent of any new funds to support ITPs • Q2 2025 report-back to Cabinet on proposed settings for 2026 	<ul style="list-style-type: none"> • Q1 2025: Further analysis and targeted engagement on proposed 2026 settings • Q2 2025: report to Cabinet on proposed final funding structures for 2026, including changes to appropriations • Q3 2025: statutory consultation on proposed changes to funding determinations • September 2025: finalise funding determinations for 2026

- 23 The following sections step through the main funding areas and the types of decisions we propose for Cabinet in November, and those that would follow in 2025.
- 24 We will provide you with advice on options for the November Cabinet paper in early October following analysis of submissions. This will include broad options for change alongside an indication of the impacts of those options on funding for different categories of providers and learner groups.

Further increasing provider-based subsidy rates

- 25 The current consultation signals using Learner Component funding to further increase provider-based funding rates from 2026. We anticipate significant feedback on this. Earlier this year, we estimated that returning to past subsidy rates would require using around \$38 million (60 percent) of the \$65 million currently designated for the Learner Component [METIS 1320350 and 1328935 refer]. Following Budget 2024 cost adjustments, both of these amounts will now be around 2.5 percent higher.

Decisions for November Cabinet paper

- 26 For the November Cabinet paper, we propose focussing on the overall scale of re-balancing of funding currently for work-based learning to funding for provider-based delivery, including the increase to provider-based funding rates and the amount of Learner Component and/or other funding that would need to be repurposed. Key factors to consider for this are:
- the scale of any further increase will improve the viability of some delivery; but
 - the scale of any decrease in Learner Component funding would be expected to constrain providers’ ability to improve outcomes for under-served learners; and
 - the scale of any funding to be shifted from work-based to provider-based rates is linked to the scale of funding needed for effective standards-setting entities.

Decisions for 2025

- 27 Following the November Cabinet decision, we would provide you with further advice on the structure of the new funding system as well as the specific rates for provider-based delivery. This would include decisions on the structure and groupings of funding rates (alongside decisions on how to structure work-based learning funding rates) and decisions on the design of appropriations.
- 28 You may also wish to consider the option of targetting increases towards some areas more than others. Targeted increases could be informed by further analysis of at-risk provision across the network and may provide an option to support delivery that is important or 'core' to some ITPs and regions, alongside any additional funds for ITPs (discussed below).

Learner Component

- 29 As noted, your intended changes to provider-based funding rates are likely to require reductions to Learner Component funding rates. Repurposing Learner Component funding towards provider-based funding rates represents a net redistribution of funding from work-based delivery towards provider-based delivery (as a significant proportion of Learner Component funding supports work-based delivery). It also involves a redistribution of funding targeted for particular learner groups towards all learner enrolments.
- 30 Approximately 70 percent of the Learner Component is currently allocated to Te Pūkenga, with around two-thirds for enrolments in work-based learning. Low prior achievement enrolments account for around 70 percent of overall Learner Component funding, with a relatively high proportion in work-based learning. Enrolments of disabled learners account for around 20 percent of the funding.
- 31 We have previously advised that further engagement with providers and affected groups would be advisable before finalising Learner Component funding rates [METIS 1331851 refers]. In particular, this reflects strong feedback from Whaikaha that the consultation paper was not sufficiently specific to engage disabled persons' groups on these questions.

Decisions for November Cabinet paper

- 32 We recommend that your November Cabinet paper signal changes to the Learner Component as part of the overall rebalancing of funding from work-based to provider-based delivery, but that it does not set the specific level of reduction to Learner Component funding and the distribution of remaining Learner Component to rates for different learner groups. This would provide you with some flexibility to determine what amount of the funding increase for provider-based rates comes from the Learner Component versus from work-based funding rates.
- 33 Alternatively, you could seek agreement to the amount of Learner Component funding to be used to increase provider-based rates, including the trade-offs and implications of that, and propose further engagement in 2025 on the best use of the remaining funding to support learners.

Decisions for 2025

- 34 Following November Cabinet decisions we would propose to undertake targeted engagement with providers and stakeholder groups on specific changes to the Learner Component for 2026. This could involve developing an approach with a stronger focus on non-financial incentives to drive improvements in achievement for certain groups of learners

by shifting the focus more toward the TEC's Learner Success and broader Investment Plan frameworks.

Funding for arranging and delivering work-based learning

- 35 Designing an appropriate funding approach for work-based learning will need to take account of your and Cabinet's decisions on roles and responsibilities for it and standards-setting, including the respective roles of national bodies (e.g. Industry Skills Boards [ISBs]) and providers (ITPs, Wānanga, and Private Training Establishments [PTEs]). This requires further work and engagement on how funding for work-based learning might interact with other funding for different organisation types.
- 36 In particular, you have indicated that you would like to explore a hybrid of Options A and B for work-based learning, whereby ISBs would arrange training, but providers would be directly funded for delivery. This would be a significant change to the current funding model that we will explore as part of our upcoming advice on a hybrid model [METIS 1335828 refers].

Decisions for November Cabinet paper

- 37 We recommend the November Cabinet paper focuses on any significant changes to the funding model for work-based learning (such as would be required to support a hybrid model) as well as the overall scale of funding to be reprioritised from work-based funding rates to support standards setting and any additional funds for ITPs, with a clear indication of what these funding changes would mean for standards-setting and work-based learning.

Decisions for 2025

- 38 Following Cabinet's decisions, we would propose targeted engagement on the structure of funding rates for work-based learning from 2026. In particular, we recommend further analysis and engagement on the details of any significant change to the funding model (such as for a hybrid model), as well as on whether to return to the past industry training funding model with rates for apprentices and trainees and whether to retain any subject area differentials for work-based learning. These are not explored in the current consultation proposals.

Funding for standards-setting entities

- 39 The consultation document signals both Option A and Option B as having dedicated funding streams for standards-settings. This would be funded by reducing the current funding for work-based learning. However, the two options may have different implications for the funding of standards-setting:
- Option A: ISBs would be responsible for standards-setting *and* arranging work-based learning, so would receive funding for standards-setting *and* arranging training (which could see some cross-subsidising from the latter).
 - Option B: Industry-led bodies would be responsible for standards-setting but *not* arranging work-based learning, so would receive funding only for standards-setting (with funding for arranging work-based learning going to a range of organisations).

Decisions for November Cabinet paper

- 40 We recommend that the November Cabinet paper signals the overall level of funding to be provided for standards-setting, but not the specific methodology for allocating funding to each standards-setter.

- 41 We have previously advised that effective standards-setting entities may require \$30 million to \$50 million per annum [e.g. METIS 1320755 and 1324004 refer]. While further work is needed, we consider the lower end of this range remains relevant for effective (but streamlined) standards-setting entities.
- 42 You have previously indicated a preference for less funding than the above range for these functions. A lower amount may therefore involve a trade-off in the entities' capability to meet the expectations of industries and the needs of providers. These funding constraints are likely to be more critical under any option where the standards-setter will not have the option of cross-subsidising this activity from work-based learning funding.
- 43 We also note that if the New Zealand Qualifications Authority (NZQA) is required to support standards-setting and related quality assurance activities for industries not covered by an ISB or Option B entity, NZQA will need additional funding.

Decisions for 2025

- 44 Following the November Cabinet paper, we would develop a funding methodology for the new standards-setting entities for approval as part of the proposed 2025 Cabinet paper.

Levy Funding for Standards-Setting

- 45 You recently raised with us the possibility of an industry contribution to the cost of standards-setting and related functions in the form of a levy. Current legislation includes provision for a levy to fund WDCs if industry demonstrates its support via a ballot with a high threshold for success.¹
- 46 While the current VET redesign consultation does ask broadly how standards-setting should be funded, it does not raise the prospect of an industry levy. While there is a strong in-principle case for levy funding of standards-setting, the introduction of a new or amended levy-making power would be a significant policy change with high levels of interest from individual employers and some industries. We would therefore recommend consulting explicitly on this change before seeking Cabinet agreement, noting that this would not allow it to be progressed via your upcoming VET redesign bill. Standards-setting levies could instead be progressed following consultation as part of a subsequent phase of legislation, potentially alongside work that MBIE is scoping on levy-funded training.
- 47 If you do want to proceed with introducing levies without further consultation, the risks associated with the approach would be somewhat mitigated by amending the existing levy provisions rather than introducing a new levy power. The simplest way to do so would be to lower the thresholds for a successful industry ballot or removing this requirement and replacing it with a consultation requirement. Further design work would need to be undertaken before any levy could be implemented and any levy is unlikely to be able to be operationalised by the beginning of 2026.
- 48 Introduction of a levy could be an option to either allow industry to support expanded standards-setting functions or could instead reduce the public contribution to the costs of these functions over time. We will provide you with further advice on the option of an amended levy power and the funding implications of levy funding for standards-setting as part of our advice following analysis of submissions.

¹ The levy must receive 60% support in total and 60% support when weighted by size of voting members (employee numbers or production level), and turnout in the levy ballot must be at least 60%. A similar provision existed for levies to fund Industry Training Organisations, but this was never used.

Additional funds to support the regional role of ITPs

- 49 The current consultation is seeking views on funding arrangements to support and incentivise ITPs to engage with industry, support regional development, and bring more of the benefits of international education to regions. While not explicit in the consultation document, funding for these activities would need to come from reducing work-based learning funding as part of the proposed re-balancing of funding for provider-based and work-based VET.
- 50 These funds could support the viability of additional ITPs, depending on their size and purpose. The design of these funds will be a critical issue that we explore in our upcoming advice following analysis of submissions, noting the challenges with developing non-volume linked funding that both avoids administrative burdens and meets accountability expectations for public funds. The scale of reduction of work-based funding rates needed to establish these funds is also likely to be a key consideration for Cabinet.

Decisions for November Cabinet paper

- 51 The November Cabinet paper will need to seek agreement to the scale and core policy parameters of any ITP funds. We will provide you with advice on these matters in early October following consideration of consultation submissions. We will also provide you with advice on any alternative mechanisms to achieve these objectives, such as further targeted increases to provider-based funding rates.

Decisions for 2025

- 52 Following the November Cabinet decisions, further policy work would be required on any ITP funds, including on the methodology by which the funding is distributed, details of accountability arrangements, and operational policy design. Any necessary further Cabinet decisions on these matters could be sought as part of the Q2 2025 Cabinet paper.

Risks

- 53 This paper outlines our proposed approach to considering and progressing further changes to the VET funding system from 2026. You are currently consulting on the proposed direction of change, and need to consider feedback and submissions before locking in any decisions on what to present to Cabinet in November. A perception that decisions have been made before consultation feedback is considered (or that submissions have not been appropriately considered) could lead to reputational and legal risk, including judicial review.
- 54 We have proposed a phased approach to refining and confirming funding settings for 2026. This will allow the November Cabinet paper to focus on the content and decisions needed to progress legislation for the replacement of Te Pūkenga and WDCs.
- 55 As noted elsewhere, there are risks related to limited direct consultation with Māori during the consultation period or decision-making process [METIS 1320447 refers]. While increased funding for provider-based VET will likely be welcomed by Māori providers (e.g. Wānanga), changes to the Learner Component may be seen as disadvantaging Māori learners, particularly if it is viewed as reducing a focus on enabling Māori to succeed in VET.
- 56 Reducing funding for work-based learning may also be seen as problematic from a Tiriti perspective, particularly where iwi-owned companies and the broader Māori economy may be seeking to get more rangatahi into work-based learning. In 2023, 43 percent of Māori learners in VET were in work-based learning (over 25,300 tangata Māori). Work-based learning can provide a learning context for Māori (and Pacific people) that builds on existing

relationships and may be more accessible given the time and cost implications of undertaking provider-based learning.

- 57 We are proposing that core policy settings for VET funding from 2026 be considered by Cabinet in Q2 2025. While this allows refined proposals to be developed, it reduces the time available for the TEC and sector to implement changes to operational settings and IT systems, and to develop indicative funding allocations for providers. Engaging the sector in early 2025 will somewhat mitigate this risk.

Financial Implications

- 58 Changes to the VET funding system will involve a range of financial and fiscal implications, including changes to appropriations within Vote Tertiary Education. Cabinet will need to approve these changes in Q2 2025 or delegate them to you and the Minister of Finance.
- 59 Any Cabinet decisions on funding changes with implications for appropriations will need to occur outside of the Budget moratorium period (typically early- to mid-April until Budget day in mid- to late-May).

Next Steps

- 60 After analysis of submissions and taking into consideration your feedback on this paper, we will provide you with advice on the key funding policy decisions for inclusion in your November Cabinet paper in early October. This will include estimates of the overall shifts in funding and the potential distributional impacts of any options, where possible.
- 61 We will also work with the TEC to ensure the proposed funding shifts are reflected in ITP modelling, where it is possible to do so.

Recommended Actions

The Ministry of Education recommends you:

- a. **Note** that:
- i. consultation feedback needs to be appropriately considered before determining the funding proposals for 2026 that you intend to propose to Cabinet in November 2024; and
 - ii. VET funding settings for 2026 will be finalised in Quarter 3 of 2025 following consultation on variations to funding determinations.
- Noted**
- b. **Agree** to seek Cabinet decisions on changes to policy settings for VET funding from 2026 in two phases:
- i. high-level decisions on objectives and proposed funding shifts in your November 2024 Cabinet paper; and
 - ii. detailed decisions to confirm policy settings for VET funding from 2026 in a Cabinet paper in quarter 2 of 2025.

Agree / Disagree

- c. **Discuss** any feedback you have on the scope of funding changes to be progressed in the November 2024 Cabinet paper and any particular issues or options you would like us to consider in our advice following analysis of submissions.

☒ Agree / ☐ Disagree

Proactive Release:

- d. **Agree** that the Ministry of Education release this paper after Cabinet has taken policy decisions for the disestablishment and replacement of Te Pūkenga, as part of the communications strategy for the announcement of those decisions, with any information needing to be withheld done so in line with the provisions of the Official Information Act 1982.

☒ Agree / ☐ Disagree



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Hon Penny Simmonds
Minister for Tertiary Education and Skills

12/09/2024

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