Early Childhood Education Funding Review – Treasury responses to Ministerial Advisory Group questions - Updated

Treasury contacts: Joshua Mackay and Ian Moore

Context:

Treasury officials met with the early childhood education (ECE) funding review Ministerial advisory group (MAG) on Friday 8th August. At this meeting, the MAG requested information on how they should define 'fiscally neutral' within their terms of reference, including:

1. Any relation to demand-driven forecast funding for ECE (i.e. if the review were expecting ECE to be offered to more children, would that need to be met within the existing funding pool).
2. Treatment within vs. across years over the forecast period, and if they had access to the full range of forecast funding.

This is the second version of this note, and has been updated with responses to follow-up questions. A list of those questions and direct answers is included in Annex 1

Treasury's response:

The terms of reference for the ECE funding review state that the review should 'consider options that are at least fiscally neutral for the Crown, that is, within total forecast expenditure in scope.'

Forecast funding for ECE:

Volume-driven funding parameters for ECE are tied to existing policy settings. Therefore, the MAG's consideration of other options that would change policy settings (and potentially influence demand) should not assume that there is any change to current forecast expenditure, and demand changes should be managed within that existing expenditure envelope.

However, given that the Government accepts variation in ECE expenditure in response to demand under current policy settings, Treasury is comfortable with options that focus only on meeting current demand within the existing expenditure envelope **also** being presented.

The appropriate baseline for current forecasts would be the 2025 March Baseline Update, as reflected in the 2025/26 Estimates. We note also that volume changes not driven by policy decisions (e.g. population change) will continue to be captured under existing forecast changes.

Funding across the forecast and across votes:

For expenditure across the forecast period, current expenditure forecasts for ECE are based on expected demand within the five-year forecast period. While all of this expenditure is within scope of the review, moving funding between years risks creating funding cliffs (i.e. by not leaving enough funding in future years to meet forecast demand). Given this, the MAG should consider options that are fiscally neutral within each financial year, rather than seeking to move funding between years within the forecast period.

However, given that Cabinet have included options across different votes (Education, Social Development, and Revenue) within the scope of the review, the MAG could consider options that move funding between areas. This would be constrained by the scope agreed by Cabinet, so funding for Kōhanga Reo and Playcentre (including targeted funding streams) would be out of scope.

We also note that the Ministry of Education in 2024/25 included a provision to manage forecast risks in the Early Learning appropriation. These provisions (if applied in future years) should not be included in the funding available for the review, as they are a non-cash adjustment.

Treasury understands that there is concern that the inability to move funding between years could limit the MAG's ability to cover transitional costs for system changes. While we support flagging this risk in any report made by the MAG, additional funding to cover transitional costs should not be assumed, and would not be fiscally neutral.

Treasury Recommendation:

1. The MAG should consider options that are capture any demand changes within the existing funding envelope, but may also include options which focus only on meeting current demand within current funding.
2. While the MAG can consider funding across the forecast period, options should be fiscally neutral within each financial year.
3. There are no restrictions on considering options that move funding between votes.

Annex 1: Follow-up questions from the original note and specific answers

Key concepts / parameters (forecast demand, allocation over the forecast period)

- We understand Treasury to be saying that any proposals that are likely to increase demand beyond current forecasts would not meet the 'fiscal neutrality' test, unless they can be met within "the existing funding envelope" (i.e. the amount currently allocated over the forecast period). Is this correct?
    - Yes.
- The Treasury note also makes a distinction between policy-driven changes in demand resulting from funding changes vs non-policy / externally driven changes in demand (e.g. population changes). The former would be counted in terms of impact on the bottom line, and the latter not counted. Is this correct?
    - Yes. As under the status quo, volume changes not driven by policy decisions could be captured under existing forecast changes. The 'fiscally-neutral' framing is specifically intended to refer to options for change considered by the ECE funding review, and population changes would be outside of that.
- Should MBU 2025 be used as the forecast that sets the amount allocated over the forecast period? This seems most aligned with the timing of Cabinet decisions on the Terms of Reference. Forecasts are not static, and can vary over OBU, MBU and PRFU. It would be difficult for the review to address the fiscally neutral parameter if the parameter itself is subject to change.
    - Yes, MBU forecasts, as included in the 2025/26 estimates, would be the most reasonable baseline to use for funding here.

Fiscally neutral within each financial year

- The Treasury note indicates that fiscal neutrality applies to each financial year.
- This is quite constraining and leaves no scope for any proposals that might shift costs between financial years (e.g. by grandparenting funding for services that would be losers under a new funding system, the adoption of outcome-based funding approaches, or "invest to save" type proposals).
- Can we also assume that fiscal neutrality in each financial year means that any transitional costs faced in the initial implementation period would be met from additional resourcing via the Budget process?
    - No, new Budget funding would not be considered fiscally neutral. The risks of transition could be flagged in any report made by the MAG, but these should not assume additional resourcing would be provided.

Fiscal neutrality across Votes

- The Treasury note is silent on this. We assume this means that "the funding envelope" includes the amounts specified in appropriations over the forecast period, for Votes MoE, MSD and IRD?
- In terms of providing clarity for the MAG, should they work on the basis that across all three Votes, the full amount of estimated expenditure over the forecast period is available for re-allocation within the overall ECE funding system?
    - Given that Cabinet included multiple funding streams across votes, we are comfortable that the review could re-allocate funding between votes.

However, we would note that funding should be restricted to within the constraints agreed by Cabinet, so funding for Kōhanga Reo and Playcentre would be out of scope (including targeted funding streams), as would the non-cash provision for managing forecast risk included in the Early Learning appropriation for 2024/25.