Education Report: Final modelling of UFS rates for 2023 and other policy decisions

To:	Hon Chris Hipkins, Minister of Education		
Date:	9 March 2022	**Priority:**	High
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Messaging seen by Communications team:	No	**Round Robin:**	Yes

Purpose of report

This report seeks your agreement to:

- the rates for the unified funding system (UFS) for 2023, ahead of seeking final agreement to the rates from you and the Minister of Finance, and
- a transition approach for private training establishments (PTEs).

We seek your feedback by 14 March so that UFS rates can be announced in mid-April.

Summary

In December 2021, Cabinet agreed to the broad parameters for the design of the new UFS for vocational education and training (VET). This included maintaining funding for provider-based provision at 80-85 percent of current Student Achievement Component (SAC) rates, increasing industry training rates by 40-90 percent and setting funding for learners with low prior achievement and disabled learners between $1,100 and $1,300. Cabinet delegated decisions on setting the final funding rates for 2023 to you and the Minister of Finance [CAB-21-MIN-0525 refers]. You have already made key decisions to support modelling of the final UFS rates and settings for 2023, which (alongside the parameters agreed by Cabinet) form the basis of the proposed rates in this paper.

Our modelling to date has been based on enrolment data available to the end of July 2021 (projected to full year). We now have full-year 2021 data and greater clarity on the total appropriated funding for UFS in 2023. Some volume shifts in the full-year 2021 data means there is a shortfall of approximately $10 million if we apply the most recent version of the indicative rates that you agreed to in February [METIS 1281674 refers] to the new total funding pool for modelling the UFS. The resulting shortfall will need to be made up to ensure that the new rates are fiscally neutral.

We have considered several different approaches to modelling the rates, all of which are very close to neutral in terms of the subsector or provider level impacts when compared to the previous version of the rates you agreed to in February. We have proposed an approach to the final UFS rates for 2023 that is consistent with Cabinet's previous decisions and continues

to drive the right incentives, supporting learners to transition to work-based training and improving success and support for learners. The proposed rates that we seek your agreement to are shown below in Table 1.

Table 1: Proposed delivery component rates for the UFS 2023

	Mode of delivery				
Funding categories	**Provider-based**	**Extra-mural**	**Work-based**	**Pathway to work**	**A&V[1]**
Humanities, Business and Social Service Vocations (F1)	$5,425	$4,750	$5,155	$6,240	$1,500
Trades, creative, IT and health-related vocations (F2)	$8,626	$4,750	$7,075	$8,801	$1,500
Engineering, Health, Science and Primary Industry Vocations (F3)	$9,711	$4,750	$7,726	$9,669	$1,500
Pilot Training and Priority Eng. (F4)	$11,881	$4,750	$9,028	$11,405	$1,500
Specialist Low-volume, high-cost vocations (F5)	$16,275	N/A	N/A	N/A	N/A
Te reo and Tikanga Māori (F6)	$6,589	N/A	N/A	N/A	N/A

To meet the $10 million shortfall, the funding rate for learners with low prior achievement and disabled learners has reduced by $166 (12 percent) from $1,366 to $1,200, which is within the range agreed by Cabinet. The proposed rates also very slightly adjust the subject weighting relativities for three funding categories (F2, F3 and F4) to lower these funding rates by an average of $52 (0.5 percent). Despite these rates decreases, this still results in a significant increase for work-based training and funding to support learners. The strategic component remains at the same amount as previously indicated ($74 million, including $37 million for the Programme Development and Maintenance Fund).

It is important to note that the rates modelling is based on 2021 volumes and does not attempt to predict behavioural shifts and resulting volume changes that could occur from 2023. There are existing processes in place to manage any significant volume changes (including shifts in mode) within the baseline and to mitigate the associated risks.

In December, we indicated that the Tertiary Education Commission (TEC) would further develop an approach to the transition to the UFS for PTEs [METIS 1276773 refers]. This paper also seeks your agreement to a proposed transition approach for PTEs. The proposed approach limits funding reductions to 10 percent for priority and niche provision at PTEs with significant funding reductions in 2023 and 2024. There will also be 50 percent less funding available for the PTE transition to UFS in 2024. This focuses on supporting strategically important provision to adapt to the new incentives offered by the UFS, rather than maintaining overall viability of PTEs.

Following your decisions on the UFS rates, we will prepare advice for you and the Minister of Finance that seeks final agreement to the rates for 2023.

[1] Assessment and verification.

Recommendations

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

a. **note** that the modelling tool for the unified funding system rates is based on 2021 volumes (including mix of modes and provision) and does not attempt to predict behavioural shifts and resulting volume changes that could occur from 2023

b. **note** that there are existing processes that can be used to assist in mitigating and managing risks arising from significant volume and mode-split changes within the baseline, including through the Tertiary Education Commission's Investment Plan processes and decisions on mixes of provision

Proposed unified funding system rates for 2023

c. **note** that volume changes have created a funding shortfall of approximately $10 million if we apply the most recent version of the indicative rates that you agreed to in February [METIS 1281674 refers]

d. **note** that despite this shortfall, we have been able to model a version of the rates that is consistent with Cabinet's previous decisions and that strikes an appropriate balance in weighting components of the unified funding system without distorting incentives

EITHER

e. **agree** to the approach on setting final rates for the unified funding system for 2023 as shown in **Annex 2**, which adjusts the weighting relativities for three funding categories slightly and sets the learner component for learners with low prior achievement and disabled learners at $1,200

Agree / Disagree

OR

f. **indicate** if you would like to discuss any changes to the recommended rates for the final decision paper to yourself and the Minister of Finance

Yes / No

g. **note** that the proposed rates incorporate the 1.2 percent cost adjustment for 2022 that was approved in Budget 2021, which was not applied to the previous version of the rates provided to support decisions on the Pilot Training and Priority Engineering rates [METIS 1281674 refers], and partially offsets the volume changes in the end of year data

h. **note** that the 1.2 percent cost adjustment has been added to the total funding amount used to model the rates and due to how the ratios are calculated for the UFS rates it does not mean all the rates have been increased by 1.2 percent

i. **note** that we request your feedback on this paper by 14 March to enable all decisions on the unified funding system rates to be taken before the Budget moratorium on 11 April, and an announcement on the rates by mid-April

j. **note** that following your decisions on the unified funding system rates, we will prepare advice for you and the Minister of Finance seeking final agreement to the rates for 2023 (as per delegations agreed by Cabinet in December [CAB-21-MIN-0525 refers])

k. **note** the rates provided to you and the Minister of Finance for final agreement will not include any agreed cost adjustment for 2023 (as this will still be subject to Budget decisions) and this will need to be clearly signalled to the sector when announcements are made in April

Transitions for private training establishments

l. **note** that the national and regional skill priorities element of the strategic component is divided 70/30 between Te Pūkenga and private training establishments (totalling $25.9m and $11.1m respectively) and the Programme Development and Maintenance Fund is divided 60/30/10 between Te Pūkenga, private training establishments and wānanga (totalling $22.2m; $11.1m; $3.7m respectively)

m. **note** that private training establishment transitions funding will come from the private training establishment allocation of the Programme Development and Maintenance Fund

n. **agree** that the private training establishment transitions funding will be targeted to limiting funding reductions to 10 percent for priority and niche provision at providers with significant funding reductions and will be for 2023 and 2024, with a maximum of 50 percent less funding available the private training establishment transition in 2024 and an additional $1million ring-fenced for emerging transition issues

Agree / Disagree

o. **agree** to proactively release this education report after announcements of the unified funding system rates in April, with any redactions in line with the provisions of the Official Information Act 1982.

Agree / Disagree

Katrina Sutich
Group Manager
Te Ara Kaimanawa
Ministry of Education

09/03/2022

Gillian Dudgeon
Deputy Chief Executive – Delivery
Tertiary Education Commission

09/03/2022

Hon Chris Hipkins
Minister of Education

30/ 3 /2022

I would prefer to make this as a Budget announcement
so that B2022 funding increases can be incorporated.

Background

1. In December 2021, Cabinet agreed to the design of a new unified funding system (UFS) for vocational education and training (VET). Cabinet also agreed to delegate decisions on the final funding rates for 2023 to you and the Minister of Finance, and the remaining detailed policy decisions – including the transition approach – were delegated to you [CAB-21-MIN-0525 refers]. **Annex 1** provides the sequence of key decisions to determine the UFS funding rates.

2. Broadly Cabinet agreed to maintain funding for provider-based provision at 80-85 percent of current Student Achievement Component (SAC) rates, increase industry training rates by 40-90 percent and set funding for learners with low prior achievement and disabled learners between $1,100 and $1,300.

3. You have already made some key decisions to support modelling of the final UFS rates and settings for 2023, which form the basis of the scenarios developed for this advice. These include:

    a. **Initial modelling with broad parameters and incentives** – In October 2021, you signalled a preference for rates to be modelled around 'Scenario B: Moderate incentives' in *Education Report: Phase One modelling of the Unified Funding System* [METIS 1272025 refers]. This scenario made more significant increases to work-based rates to create stronger incentives for providers and employers to collaborate on work-based learning.

    b. **Creation of a new element and extramural rate** – In November 2021, you agreed to the creation of a new Programme Development and Maintenance Fund (PDMF) to meet the high upfront costs of primarily extramural programme development. You also agreed to setting an extramural rate at a fixed rate of $4,750 per full-time equivalent learner (FTEL) [METIS 1276629 refers].

    c. **A separate funding rate for Pilot Training and Priority Engineering** – In February 2022, you agreed to establish a new funding category in the UFS for Pilot Training and Priority Engineering set at approximately 85 percent of the average Student Achievement Component (SAC) rates [METIS 1280994 refers].

4. The most recent version of the indicative rates for the UFS that you agreed to in February are in Table 1 below [METIS 1281674 refers]. This was based on projected full-year 2021 enrolments of 115,000 FTELs and the value of UFS provision, including additional funding through Budget 2021, at $925 million. These rates had not incorporated the 1.2 percent cost adjustment for 2022 that was approved in Budget 2021.

Table 1: UFS delivery component rates based on indicative modelling

	Mode of delivery				
Funding categories	**Provider-based**	**Extra-mural**	**Work-based**	**Pathway to work**	**A&V**
Humanities, Business and Social Service Vocations (F1)	$5,415	$4,750	$5,149	$6,232	$1,500
Trades, creative, IT and health-related vocations (F2)	$8,664	$4,750	$7,099	$8,831	$1,500
Engineering, Health, Science and Primary Industry Vocations (F3)	$9,747	$4,750	$7,748	$9,698	$1,500
Pilot Training and Priority Eng. (F4)	$12,000	$4,750	$9,100	$11,500	$1,500
Specialist Low-volume, high-cost vocations (F5)	$16,245	n/a	n/a	n/a	n/a
Te reo and Tikanga Māori (F6)	$6,511	n/a	n/a	n/a	n/a

Proposed approach to setting final 2023 UFS rates

5. We are seeking your agreement to the final UFS rates now to allow rate announcements to occur in mid-April and for decisions before the Budget moratorium.[2] Our modelling to date has been based on enrolment data available to the end of July 2021 (projected to full year). We now have full-year 2021 data and greater clarity on the total appropriated funding for UFS in 2023. There have been some volume shifts in the actual full-year 2021 data that impact the UFS rates modelling. Our modelling now also incorporates the 1.2 percent cost adjustment for 2022 that was approved in Budget 2021.[3]

6. Full-year 2021 returns included 121,000 FTELs. If this volume was fully funded, subsidies would total $873 million at the current SAC and Industry Training Fund (ITF) rates. This figure, plus new funding received in Budget 2021 creates a $971 million funding pool for modelling the UFS.[4]

7. There were also some key shifts in volumes compared to volumes modelled in October 2021. This includes:

    a. **A significant fall in volume for provision reported to the Assessment and Verification mode**, from 4.0 percent of volume to 2.6 percent of volume. Assessment and Verification is the lowest rate in the UFS (fixed at $1,500) and with much of this provision now reported as work-based it comes at a greater cost to the system (work-based rates are significantly higher, are weighted by subject area category and attract learner component funding).

    b. **An increase in industry training volumes**, with approximately 6,500 more standard training measures (STMs) reported through the Industry Training Register (ITR). For modelling the UFS rates, industry training volume is relatively expensive compared to SAC volume given that the UFS will significantly increase rates for this provision.

    c. **A decrease in SAC provision**, with approximately 1,500 fewer equivalent full-time students (EFTS) reported through the Single Data Return (SDR) than expected. For modelling the UFS rates, this reduces the funding 'saved' by decreasing the provider-based rates from the SAC rates.

8. In the final modelling, we have also increased volume to allow for a range of approximately between 800 and 1,000 non-residents FTELs to be granted eligibility for UFS tuition subsidies (representing approximately 20 percent of current non-resident trainees and apprentices in 2021). This follows your agreement for officials to develop an applications-based eligibility exemptions process informed by Workforce Development Councils (WDCs) [METIS 1276773 refers].[5] While this is only a high-level estimate, we consider that it represents a reasonable allowance for exemption volumes consistent with our discussions on how the exemptions framework is likely to operate in practice. If the number

[2] While a decision on the UFS rates is intended to be fiscally neutral, the decisions will have consequential impacts on appropriation splits which we recommend taking before the Budget moratorium process commences on 11 April.

[3] We had previously not applied this to maintain consistency with previous versions of the rates.

[4] Taking account of how much will be appropriated in 2023 with the most recent estimates from the volume bid for Budget 2022, we estimate that $97.3 million of Budget 2021 funding should be accounted for in the modelling tool (an increase of $13.2m from $84.1 million in previous versions of modelling).

[5] There is uncertainty about the volume of non-residents that will be granted eligibility for tuition subsidies through exemptions in 2023 and beyond. 800 FTELs, at approximately 20 percent of current volume of non-residents, is our best estimate with available information given the impact of COVID-19 (on border settings and willingness of people to travel overseas) and immigration changes. A high proportion of existing non-residents in industry training are also likely to transition to residency through the one-off 2021 residency visa process.

of exemptions granted is greater than this level then this would be one of several factors that impact on overall volume in the system, which will need to be managed by the Tertiary Education Commission's (TEC's) investment processes.[6]

9. We have also assumed that absolute dollar total of the strategic component would remain at the same amount as previously indicated ($74 million). This would represent a slightly smaller proportion of total UFS funding (from 8.0 percent to 7.6 percent), reflecting the increase in total funding baselines in the model. This is consistent with our overall approach to the strategic component, which we envisage would be set at a particular level of funding, rather than automatically increasing or decreasing with total volumes of delivery in any given year.

Volume changes in full-year data have created a shortfall

10. While we have increased the overall pool of funding in the model by the full amount of new funding and the 1.2 percent increase in rates for 2022, the volume changes outlined above have still created a funding shortfall of approximately $10 million if we apply the most recent version of the indicative rates that you agreed to [METIS 1281674 refers]. Although the increase in volume also increases the total funding baselines within the modelling tool, this is outweighed by the fact that the increase was disproportionally concentrated in work-based provision (the funding rates for which will substantially increase under the UFS). The resulting shortfall will need to be made up to ensure the new rates are fiscally neutral.

Key variables in setting final 2023 rates

11. There are a range of different variables within the UFS that can be adjusted to ensure the rates stay within the parameters agreed by Cabinet and maximise the available funding.

12. The $10 million shortfall is just 1 percent of the overall value of provision in the UFS modelling tool. This means all the scenarios considered are very close to neutral in terms of the subsector or provider level impacts. Therefore, the key focus of the decision on the final rates and our modelling analysis is to ensure the rates create the right incentives.

13. In considering options for addressing the shortfall, we have looked at potential changes to the non-fixed components of the delivery component as well as changing the level of learner component funding for learners with low prior achievement and disabled learners. In balancing these variables, we have focused on ensuring that the relative level of components does not distort incentives, and on setting rates that are consistent with those indicated to Cabinet and the sector.

Variables we have not considered in modelling options

14. There are also several options to change the rates that we have *not* modelled, as these would be a more significant shift from previous decisions made by Cabinet on the UFS, or your previous decisions. These include:

    a. **Revisiting the funding ratios for different modes of delivery** – While these could be adjusted to reduce the total cost of UFS, the relative levels of funding were worked through carefully as part of earlier advice to balance several competing incentives and the fundamental basis for this advice has not changed.

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[6] We have also not attempted to model the impact of extending eligibility to work-based training to self-employed people and volunteers, as we cannot accurately predict this. We expect there to only be a small number in the short to medium-term as this is a shift that may occur over time as employers respond to the incentives of the UFS.

b. **Reducing fixed rates** – the rates for the Extramural ($4,750) and Assessment and Verification ($1,500) modes are as low as we think these rates can go while sustaining an appropriate level of this delivery in the system.

c. **Shifting specific subjects into lower funding rates** – we have not proposed changes to the subject groupings in the UFS. This is largely to retain the average provider-based rates for each funding category at between 80 and 85 percent of current SAC rates. We reviewed these groupings (that have been used in all previous versions of the modelling) and identified some areas that could justify a higher rate (e.g. early childhood education, enrolled nursing, care workers). However, moving these subject areas into a higher category would mean they get an increase on current SAC rates. We instead propose to monitor the adequacy of these rates and consider any future changes in line with provider responses and advice from WDCs.

Recommended UFS rates for 2023

15. We recommend the proposed rates set out below in Table 2. To make up for the $10 million shortfall, these rates adjust the subject weighting relativities for three funding categories (F2, F3 and F4[7]) and reduce the learner component rate for learners with low prior achievement and disabled learners. The three funding categories reduce by an average of $52 (0.5 percent) and the leaner component decreases by $166 (12 percent) from $1,366 to $1,200. Table 2 below also notes the differences compared to the rates you had previously agreed to in Table 1.[8]

Table 2: Final proposed UFS delivery component rates for 2023

	Mode of delivery				
Funding categories	**Provider-based**	**Extra-mural**	**Work-based**	**Pathway to work**	**A&V**
Humanities, Business and Social Service Vocations (F1)	$5,425 (+$10)	$4,750	$5,155 (+$6)	$6,240 (+$8)	$1,500
Trades, creative, IT and health-related vocations (F2)	$8,626 (-$38)	$4,750	$7,075 (-$24)	$8,801 (-$30)	$1,500
Engineering, Health, Science and Primary Industry Vocations (F3)	$9,711 (-$36)	$4,750	$7,726 (-$22)	$9,669 (-$29)	$1,500
Pilot Training and Priority Eng. (F4)	$11,881 (-$119)	$4,750	$9,028 (-$72)	$11,405 (-$95)	$1,500
Specialist Low-volume, high-cost vocations (F5)	$16,275 (+$30)	n/a	n/a	n/a	n/a
Te reo and Tikanga Māori (F6)	$6,589 (+$78)	n/a	n/a	n/a	n/a

16. These proposed rates represent a balanced approach to addressing the shortfall that:

a. sets the provider-based delivery component rates at a level that broadly supports the costs of this provision

[7] F2 is Trades, creative, IT and health-related vocations; F3 is Engineering, Health, Science and Primary Industry Vocations; and F4 is Pilot Training and Priority Engineering.

[8] The rates for F1 and F5 have increased slightly because of how the 1.2 percent Budget 2021 cost adjustment to rates has been applied to the available funding for the UFS in the modelling tool.

b. maintains relativities between subject rates that are broadly similar to current SAC rate levels

c. has clear distinctions between funding rates for different modes of delivery

d. introduces sufficient incentives to grow work-based delivery, and

e. sets the learner component rate at a level which creates incentives to support learners while maintaining an appropriate balance with delivery component rates.

17. We have proposed setting the F1 (Arts, Commerce and Social Service Vocations) rate at $5,425 to keep the work-based rate as close to the current apprenticeship rate ($5,716 in 2022) as possible. This is particularly important for social service vocations, including care workers. The proposed rates also maintain the F5 rate as this rate is already set at just below 80 percent of the average SAC rates and any lower may create issues for the viability of this provision.[9] It also means the rates we propose reducing (F2, F3 and F4) are still in line with Cabinet's agreement to retain the average rates at between 80 and 85 percent of SAC rates.

18. Further detail on the subsector impacts of these proposed rates, as well as the number of PTEs likely to see significant decreases in their funding under the UFS is in **Annex 2**.

Other approaches considered

19. In the process of finalising the above proposal we also modelled two approaches that use more extreme variable shifts to set the UFS rates. These are shown in **Annex 3** and varied the rates in the following ways:

a. Reducing the learner component rate to $1,100 to make up for the shortfall – this would see the learner component reduce by $266 (19 percent) and we consider $1,100 too low to act as a sufficient incentive.

b. Reduce all delivery component rates to make up for the funding shortfall – this would mean provider and work-based rates drop by an average of $103 (1.1 percent) across F1-F5 compared to the previous version of the rates you agreed. This results in some provider-based rates getting very close to dropping below 80 percent of current SAC rates and some work-based rates set too low to act as incentives.

20. Our recommended rates represent a more balanced approach that avoids the issues that these two alternative approaches create.

Implications for appropriated funding for 2023

21. As noted, the model determines UFS rates based on 2021 delivery levels (including modes) and the amount that this would cost if fully funded under current tuition subsidy levels, plus additional funding appropriated for the UFS in Budget 2021. The proposed rates are fiscally neutral at this level of volume and funding.

22. As part of our sensitivity testing on the rates, we have tested the rates against the available funding and volumes in the 2023 baseline. This indicates that the proposed UFS rates for 2023 can fund almost the same volume (99.8%) with appropriated funding under UFS as we could under the current funding system. However, this assumes that the mix of provision

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[9] The average of the SAC rates for F5 is below 80 percent due to change to H2 from $21,851 in 2022 to $16,275 in the UFS (75 percent of the average SAC rates). H2 is a degree-level rate where diplomas occasionally utilise degree-level courses and receive the higher rate. There are only 35 FTELs in this category in 2021 and so we do not propose increasing the rate 80 percent of the 2022 SAC rates.

and modes splits are the same as in 2021. Any projected shortfall above this is therefore a volume issue that should be considered as part of the current volume Budget bid.

23. The model does not factor in estimated changes in volume through to 2023 on the basis that changes to volumes or shortfalls in baselines (such as the projected shortfall in ITF baselines for 2023) should also be treated as a volume issue. The current Budget bid *Funding higher demand for tertiary education and training* seeks funding for 2023 volumes and is costed based on the proposed UFS funding rates.

24. The rates presented to you and the Minister of Finance for final agreement will not include any further cost adjustment for 2023, as that is still being considered as part of Budget 2022. When announcing the UFS rates to the sector in April, we will need to clearly signal these rates do not include a cost adjustment for 2023 and that this is still being considered as part of the Budget process. This will mean that the rates need to be revised up after Budget 2022 to factor in any inflation adjustment.

Transitions approach for private training establishments

25. In December, you agreed to a transitional period of no more than two years for PTEs and that this should be funded out of the PTE strategic component [METIS 1276773 refers]. We indicated the TEC would develop a detailed transition approach and report back to you on the cost and approach alongside rate finalisation.

PTE transitions funding will be targeted to priority and niche provision at providers with significant funding reductions

26. PTE transition funding will be focused on enabling strategically important provision to adapt to the new incentives offered by the UFS, rather than maintaining overall viability of PTEs. A targeted and principled PTE transition is a strong lever for achieving the objectives of the Reform of Vocational Education (RoVE). Balancing the need to ensure strategic provision transitions to the new system with the importance of investing strategic component funding on its original purpose has been a key consideration of this approach.

27. We propose that transition funding would support priority and niche provision at PTEs with significant funding reductions by limiting these funding reductions to 10 percent. To be eligible for transition funding, PTEs would have to meet the following criteria:

    a. PTEs must face a significant (equal to or greater than 10 percent) fall in funding, *and*

    b. either be delivering:

        i. Priority provision (e.g. primary industries, construction, engineering, early childhood education (ECE), hauora/whānau ora, healthcare), *or*

        ii. Niche provision – the only provider delivering a particular or specialist area of provision within the region or nationally.

28. The TEC will apply these criteria to identify which PTEs are eligible and allocate transition funding as part of indicative allocations. The TEC will exercise discretion over individual PTEs and respond appropriately, including in areas where additional transition funding may be justified. Any transitions funding will be subject to the TEC's normal funding allocation requirements, such as performance and quality.

29. The funding for PTE transitions will come from an under-allocation of the PTE portion of the PDMF. Based on current modelling this approach will cost $3.5 million in 2023, reducing to up to $1.8 million in 2024. Any future strategic component allocations will take account

of transition funding. In addition, we propose to under-allocate an additional $1 million for unexpected transition costs in 2023 to address any emerging risks to the PTE network of provision in 2023 and 2024.

30. PTEs would receive transition funding for 2023 and 2024, with at least 50 percent less funding in 2024. The full potential impact on PTEs will be assessed until funding allocation and recovery methodologies have been determined. PTEs will get further clarity on the transition approach in the April announcement.

Table 3: Impact of proposed approach to PTE transitions[10]

Funding reduction supported to be limited at 10 percent		**Not eligible for PTE transition funding**	
Funding reduction greater than 10 percent AND meets criteria for niche OR priority provision		*Funding reduction greater than 10 percent BUT does not meet criteria for niche or priority provision*	*Funding reduction less than 10 percent*
39 PTEs		42 PTEs	67 PTEs
PTE transitions support of up to $4.5 million in 2023 and $1.8 million in 2024		No PTE transitions support, but access to strategic component and PDMF	No PTE transitions support, but access to strategic component and PDMF
Strategic provision: construction, ECE, Engineering, Māori public health, trades, whānau ora.	*Niche provision:* Chinese medicine, child protection, education, emergency care, ICT, lab technician training, legal studies, maritime, medical transcription, naturopathy, outdoor education.[11]	*Areas of provision*: aviation, Christian studies, English language, hair and beauty, hospitality, outdoor education.	*Areas of provision*: agriculture, animal care, art and performance, Christian studies, construction (L3), ECE (L3), hair and beauty, hospitality, skydiving, social services, tourism.

The strategic component contestable funding for PTEs will complement transition funding

31. Funding for PTEs will also be available via the PDMF and national and regional skills priorities elements of the strategic component [METIS 1276773 refers]. The TEC will ensure this is aligned with transition funding, to provide both short and longer-term certainty and the best use of total funding.

32. The PDMF is divided 60/30/10 between Te Pūkenga, PTEs and wānanga. This allocates funding proportionate to each sub-sector's share of overall UFS funding (based on current allocations and resulting in $22.2m; $11.1m: $3.7m respectively for 2023) [METIS 1276629 refers].

33. The national and regional skills priorities element is divided 70/30 between Te Pūkenga and PTEs ($25.9m and $11.1m respectively for 2023). Te Pūkenga's funding will also support its charter requirements to sustain a national network of provision. Te Hono Wānanga funding proposals being developed with wānanga from Budget 2021 contingency include funding to support the role, function and unique contributions of wānanga in the sector.

[10] This will be updated to reflect your decision on the final UFS funding rates.

[11] In regions where this provision is the only provision of its kind.

34. Initial skill priorities to inform PTE applications for both elements of the strategic component will be released in May and confirmed in July based on advice from Regional Skills Leadership Groups (RSLGs) and WDCs due at the end of April and June. The application process will be straightforward and aligned as much as possible to the established investment plan process to reduce the administrative burden on providers. The TEC will work with PTEs to design this application process, including ensuring connection with RSLGs and WDCs.

Risks

35. The UFS will create significant change, including the risk of some unintended behaviours that we will need to monitor and manage. A detailed assessment of the most significant risks of the UFS are discussed in **Annex 4**, including a range of mitigations. This includes significant changes in volume and mode splits.

36. It is important to note the rates modelling is based on 2021 volumes and does not attempt to predict behavioural shifts and resulting volume changes that could occur from 2023. It assigns modes and subjects based on *current* behaviours which we are aiming to change through the UFS. It is not possible to predict the pace and scale of change and to factor this into decisions on the UFS rates, particularly given the uncertainty created by the impacts of COVID-19 and the end of the Apprenticeship Boost Initiative (ABI) and the Targeted Training and Apprenticeship Fund (TTAF).

37. There are existing processes in place to manage any significant volume changes (including shifts in mode) within the baseline and to mitigate the associated risks. We believe these volume risks can be managed through the TEC's Investment process, supported by advice from WDCs about mix of provision. This will allow the TEC to approve shifts in provision before they occur. This is particularly important to manage the proportion of work-based training occurring in the system. The TEC will keep you informed as the 2023 Investment round progresses.

38. The risks associated with PTEs discontinuing the delivery of niche areas of strategically important provision can be mitigated through transition arrangements, enabling PTEs additional resourcing and time to adapt their business models to the new incentives. We will closely monitor the adequacy of the UFS rates and consider any future changes in line with provider responses and advice from WDCs.

Longer-term technology solution for the UFS

39. The longer-term technology solution for the UFS will be ready to use for enrolments in 2025. This date is primarily driven by the ability of tertiary providers to respond to and implement the changes required for a new system. A longer-term solution will require significant change for tertiary providers, including shifting to one reporting system for all of UFS, but over time should offer greater simplicity and more accessible information. Implementation for the 2025 enrolments will also enable the solution to incorporate wider requirements from changes being made by the New Zealand Qualification Authority (NZQA) and be informed by the initial implementation of the UFS.

40. The longer-term solution will also fully enable the use of a single unit of funding, including technical rules alignment. This will be based on the UFS FTEL, which aligns funding rates across all UFS funding on the basis of average delivery of teaching and learning based on credits.

41. For 2023 and 2024 enrolments the TEC will manage a short-term technical solution that minimises change for providers but that enables providers to be funded by different modes, including within the same programmes.

42. Work on the longer-term technology solution includes:

    a. 12 to 18 months of design and build time, including significant sector collaboration and identifying change impacts for the sector;

    b. 6 months of end to end testing with providers; and

    c. at least 12 months of transition for providers to move over to the new systems, which will include providers changing systems and business models.

Next steps

43. Following your decisions on the UFS rates, we will prepare advice for you and the Minister of Finance that seeks final agreement to the rates for 2023, as per delegations agreed by Cabinet in December 2021 [CAB-21-MIN-0525 refers].

44. We seek your feedback on this advice by 14 March in order to meet timelines to make decisions before the Budget moratorium on 11 April and announcements on the UFS rates by mid-April. We will also develop a communications plan for the UFS rates announcements and will include further information on this in the final rates advice.

Annexes

Annex 1: Sequence of key UFS decisions

Annex 2: Modelling for recommended 2023 UFS rates

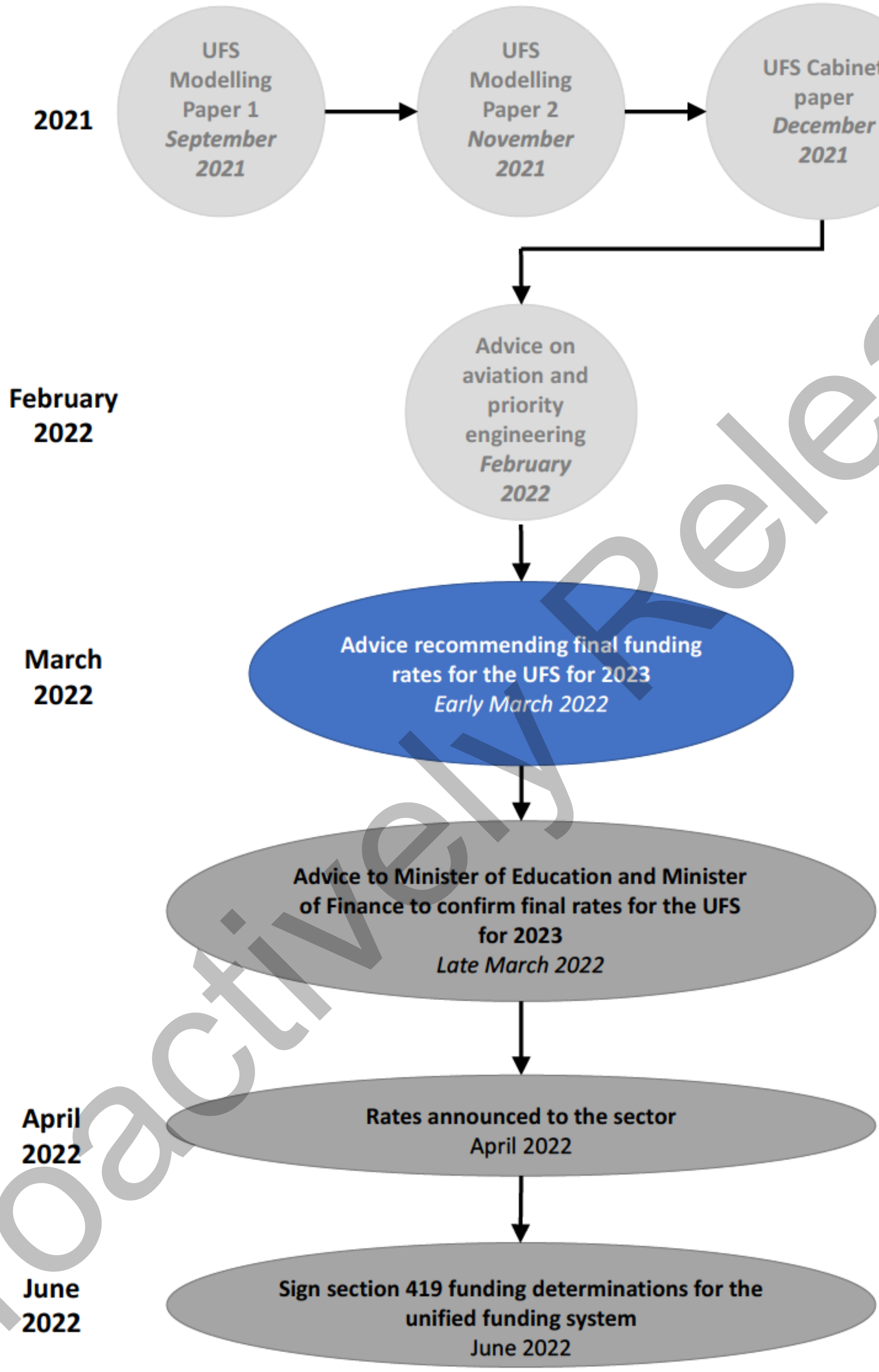
Annex 3: Modelling for alternative approaches for the 2023 UFS rates

Annex 4: Detailed assessment of risks and mitigations for the UFS

Annex 5: Subject category groupings with 2021 full-year volumes by mode

Annex 1: Sequence of key UFS decisions

Sequence of UFS advice supporting rate setting



Annex 2: Modelling for recommended 2023 UFS rates

This annex provides more detailed information the final modelling of the proposed 2023 UFS rates. This includes a break-down of the rates and how this compares to the most recent version of the indicative rates you agreed to [METIS 1281674 refers]). It also includes the subsector impacts and a summary of the impact on PTEs.

Proposed approach: adjust subject weighting relativities for F2, F3 and F4 slightly and a reduce the learner component rate

Learner component: 6.92%, $67.2 (-$8.5m / -11%)

	Funding rates /FTEL
Māori and Pacific learners to level 6	$137
Māori and Pacific learners level 7	$329
Learners with low prior achievement	$1,200 (-$166/ -12%)
Disabled learners	$1,200 (-$166/ -12%)

Strategic component: 3.81%, $37.0m

	Share	$ million
Te Pūkenga	70%	25.9
PTEs	30%	11.1

PDMF: 3.81%, $37.0m

	Share	$ million
Te Pūkenga	60%	22.2
PTEs	30%	11.1
Wānanga	10%	3.7

Delivery component – 85.46%, $829.5m (-$1.9m / -0.2%)

Subject rate			Mode of delivery				
			Provider based	Provider-based: Extramural	Work-based	Work-based: Pathway to work	Assessment & verification
	Ratio or Rate	Base rates	100% of base rate	Fixed rate of $4,750	$1,900 + 60% of base rate	$1,900 + 80% of base rate	$1,500
Humanities, Business and Social Service Vocations (F1)	1.0	$5,425 (+$10)	$5,425 (+$10)	$4,750	$5,155 (+$6)	$6,240 (+$8)	$1,500
Trades, creative, IT and health-related vocations (F2)	1.6	$8,626 (-$38)	$8,626 (-$38)	$4,750	$7,075 (-$24)	$8,801 (-$30)	$1,500
Engineering, Health, Science and Primary Industry Vocations (F3)	1.8	$9,711 ($36)	$9,711 ($36)	$4,750	$7,726 (-$22)	$9,669 (-$29)	$1,500
Pilot Training and Priority Engineering (F4)	2.2	$11,881 (-$119)	$11,881 (-$119)	$4,750	$9,028 (-$72)	$11,405 (-$95)	$1,500
Specialist Low-volume, high-cost vocations (F5)	3.1	$16,275 (+$30)	$16,275 (+$30)	$4,750	n/a	n/a	n/a
Te reo and Tikanga Māori (F6)	$6,511	$6,589 (+$78)	$6,589 (+$78)	n/a	n/a	n/a	n/a

Subsector impacts of recommended UFS rates

		Comparing proposed UFS rates to current 2021 funding under SAC & ITF			
		Current 2021 value of UFS provision	*UFS funding ($m)*	*Difference ($m)*	*Difference %*
Te Pūkenga	*Te Pūkenga subsidiaries excluding work-based (incl. Strategic and PDMF)*	$339.0	$327.2	-$11.8	-3.5%
	Transitional ITO provision[12]	9(2)(b)(ii) [redacted]			
	Total (incl. Strategic & PDMF)	9(2) [redacted]	[redacted]	[redacted]	[redacted]
Unassigned transitional ITO provision[13]		9(2)(b)(ii) [redacted]			
PTEs (incl. Strategic Component, PDMF and transitional ITO provision)[14]		9(2)(b)(ii) [redacted]			
Wānanga (incl. PDMF)		$94.9	$98.8	$4.0	4.2%
Universities		$28.0	$23.4	-$4.6	-16.4%
Total		**$863.0**	**$970.7**	**$107.6**	**12.5%**

9(2)(b)(ii) [redacted]

PTE impacts of recommended UFS rates[15]

Change in funding	Number of PTEs (UFS provision)	Total change $ million
Reduction of 50% +	3	-0.4
Reduction of 40% +	3	-1.5
Reduction of 30% +	2	-0.3
Reduction of 21% +	13	-3.9
Reduction of 16% to 20%	20	-3.4
Reduction of 11% to 15%	44	-9.2
Reduction of 6% to 10%	50	-3.2
Reduction of 0% to 5%	9	-0.2
Increase of 0% to 7%	7	0.6
Increase of 8% +	9	10.8
Total[16]	**160**	**-10.8**

[15] 9(2)(b)(ii). Also does not include Strategic Component or PDMF funding.
[16] Due to rounding, sums may not add to the totals.

Annex 3: Modelling for alternative approaches for the 2023 UFS rates

Alternative approach 1: Reducing the learner component rate to $1,100

Learner component: 6.4%, $62m (-$13.6m / -18%)

	Funding rates /FTEL
Māori and Pacific learners to level 6	$137
Māori and Pacific learners level 7	$329
Learners with low prior achievement	$1,100 (-$266 /-19%)
Disabled learners	$1,100 (-$266 /-19%)

Strategic component: 3.81%, $37.0m

	Share	*$ million*
Te Pūkenga	70%	*25.9*
PTEs	30%	*11.1*

PDMF: 3.81%, $37.0m

	Share	*$ million*
Te Pūkenga	*60%*	*22.2*
PTEs	*30%*	*11.1*
Wānanga	*10%*	*3.7*

Delivery component – 85.98%, $834.6m (+$3.2 /+0.4%)

Subject rate			Mode of delivery				
			Provider based	Provider-based: Extramural	Work-based	Work-based: Pathway to work	Assessment & verification
	Ratio or Rate	Base rates	100% of base rate	Fixed rate of $4,750	$1,900 + 60% of base rate	$1,900 + 80% of base rate	$1,500
Humanities, Business and Social Service Vocations (F1)	1.0	$5,445 (+$30)	$5,445 (+$30)	$4,750	$5,167 (+$18)	$6,256 (+$24)	$1,500
Trades, creative, IT and health-related vocations (F2)	1.6	$8,712 (+$48)	$8,712 (+$48)	$4,750	$7,127 (+$29)	$8,870 (+$39)	$1,500
Engineering, Health, Science and Primary Industry Vocations (F3)	1.8	$9,801 (+$54)	$9,801 (+$54)	$4,750	$7,781 (+$33)	$9,741 (+$43)	$1,500
Pilot Training and Priority Engineering (F4)[17]	2.2	$11,979 (-$21)	$11,979 (-$21)	$4,750	$9,087 (-$13)	$11,483 (-$17)	$1,500
Specialist Low-volume, high-cost vocations (F5)	3.0	$16,335 (+$90)	$16,335 (+$90)	$4,750	n/a	n/a	n/a
Te reo and Tikanga Māori (F6)	$6,511	$6,589 (+$78)	$6,589 (+$78)	n/a	n/a	n/a	n/a

[17] The 'F5' rate decreases slightly from the previous advice on the $12,000 estimated rate [METIS 1281674 refers] because we have now set this rate as a ratio of 2.2 to maintain relativities with the other rates. However, the rate is still higher than 85 percent of the 'M1' and 'N1' SAC 2022 rates.

Alternative approach 2: Retaining the learner component at $1,300

Learner component: 7.45%, $72.3m (-$3.3m /-4.4%)

	Funding rates /FTEL
Māori and Pacific learners to level 6	$137
Māori and Pacific learners level 7	$329
Learners with low prior achievement	$1,300 (-$66 /-4.8%)
Disabled learners	$1,300 (-$66 /-4.8%)

Strategic component: 3.81%, $37.0m

	Share	*$ million*
Te Pūkenga	70%	*25.9*
PTEs	30%	*11.1*

PDMF: 3.81%, $37.0m

	Share	*$ million*
Te Pūkenga	*60%*	*22.2*
PTEs	*30%*	*11.1*
Wānanga	*10%*	*3.7*

Delivery component – 84.9%, $824.4m (-$7m /-0.9%)

Subject rate			Mode of delivery				
			Provider based	Provider-based: Extramural	Work-based	Work-based: Pathway to work	Assessment & verification
	Ratio or Rate	Base rates	100% of base rate	Fixed rate of $4,750	$1,900 + 60% of base rate	$1,900 + 80% of base rate	$1,500
Humanities, Business and Social Service Vocations (F1)	1.0	$5,355 (-$60)	$5,355 (-$60)	$4,750	$5,113 (-$36)	$6,184 (-$48)	$1,500
Trades, creative, IT and health-related vocations (F2)	1.6	$8,568 (-$96)	$8,568 (-$96)	$4,750	$7,041 (-$57)	$8,754 (-$77)	$1,500
Engineering, Health, Science and Primary Industry Vocations (F3)	1.8	$9,639 (-$108)	$9,639 (-$108)	$4,750	$7,683 (-$65)	$9,611 (-$87)	$1,500
Pilot Training and Priority Engineering (F4)	2.2	$11,781 (-$219)	$11,781 (-$219)	$4,750	$8,969 (-$131)	$11,325 (-$175)	$1,500
Specialist Low-volume, high-cost vocations (F5)	3.0	$16,065 (-$180)	$16,065 (-$180)	$4,750	n/a	n/a	n/a
Te reo and Tikanga Māori (F6)	$6,511	$6,589 (+$78)	$6,589 (+$78)	n/a	n/a	n/a	n/a

Annex 4: Detailed assessment of risks and mitigations for the UFS

The table below sets out the detailed risks for the modelling:

Risk	Likelihood	Impacts	Discussion	Mitigations
The model under or overestimates total volume.	Moderate to High	The overall system cost in 2023 will vary depending on demand.	The model is based on data reported for 2021. It does not predict behaviour or shifts for 2023. There is uncertainty about how broader changes will impact demand. This includes COVID-19 related uncertainty, the end of the ABI and the TTAF and the new incentives created by the UFS.	Careful consideration of providers Investment Plans and mixes of provision to catch any shifts early. Managing any cost increases within baseline. Managing volume purchased. Significant increases in volume would require additional funding through Budget if you wanted to fund this. Significant decreases in volume may result in underspends.
The model does not accurately represent actual 2023 mode split.	Moderate	The overall system cost in 2023 will vary depending on the actual mode split. Depending on the direction of change cost may go up or down. Shifts from provider-based to work-based mode mainly reduces overall cost. Shifts from work-based to provider-based mode mainly increases overall cost.	The model is based on data reported for 2021. It does not predict behaviour or shifts for 2023. There is a degree of uncertainty about how the broader changes described above will impact how demand will be spread across modes.	Careful consideration of providers Investment Plans and mixes of provision to catch any shifts early. Managing any cost increases within baseline. Managing volume purchased. Significant shifts to more expensive modes may require additional funding through Budget if you wanted to fund them.

The model does not accurately represent actual 2023 subject split.	Low to Moderate	The overall system cost in 2023 will vary depending on the actual subject split. Depending on the direction of change cost may go up or down. Shifts from F3 downwards reduces overall cost. Shifts from F1 upwards increases overall cost.	The model is based on data reported for 2021. It does not predict behaviour or shifts for 2023. There is a degree of uncertainty about how the broader changes described above will impact how demand will be spread across subjects.	Careful consideration of providers Investment Plans and mixes of provision to catch any shifts early. Managing any cost increases within baseline. Manging volume purchased. Significant shifts to more expensive subjects may require additional funding through Budget if you wanted to fund them.
Providers may be incentivised to report all provision as higher value modes without changing actual delivery behaviour. *For example, reporting current provision that is in assessment and verification mode as work-based or provider-based extramural as provider-based.*	Moderate	Providers are funded for teaching and learning that is not occurring.	In the full-year data there was a shift in reporting assessment and verification. The mode dropped from 4.0 percent to 2.5 percent of overall reporting. If this represents genuine changes in how teaching and learning is delivered this would be a positive outcome. However, it is likely that at least some of the shift is in response to lower rates.	The TEC will provide clear mode definitions and guidance. The TEC will monitor any shifts. The TEC will work with providers who report a shift to check provision has had mode correctly assigned.
Providers may be incentivised to classify or reclassify existing provision to higher subject rates.	Moderate	Providers are funded for teaching and learning at the wrong rate for the delivery that is occurring.	There is a particular risk for what is currently industry training where subject classification has not previously occurred.	The TEC will provide clear subject classification definitions and guidance. The TEC will centrally assign subject classification to current industry training and test this with providers. The TEC will monitor any shifts and work with providers to correctly classify provision.

Rates are set at a level that result in large numbers of providers exiting the system without having time to adapt their business models to the new incentives.	Low	Learners are not appropriately supported to complete their study. Learner and employer choice are reduced. Competition is reduced. Some areas of provision may be lost at local, regional or national levels.	Some providers will see sharp decreases in their overall funding. This can be mitigated by changes to their business models but this will need time to occur. While we expect some providers to exit (and new providers to enter) the system, this needs to be carefully managed. If too many providers exit the system at the same time, continuity for learners is impacted.	Careful consideration of sector and provider level impacts of rate setting. Clear transitional arrangements. Careful consideration of the network of provision.
Rates are too low to support niche provision areas.	Moderate	Learner and employer choice is reduced. Appropriate skills are not available for some employers.	Some areas of provision are offered by only one provider or one provider in a region.	Careful consideration of providers Investment Plans and mixes of provision to catch any shifts early. Careful consideration of the network of provision. Additional support where required from the strategic component or from rate adjustments (for example moving a subject area up a rate).
Providers may be incentivised to stop offering level 3-7(non-degree) provision and focus on degree and above level provision to attract higher funding rates.	Low	Learners and employers have less choice in the system as a whole. Learners and employer may have to pay for higher level qualifications than required.	Many providers currently offer a mix of levels of provision. If the rates are too low they may choose to focus their offerings at degree and above.	Careful consideration of providers Investment Plans and mixes of provision to catch any shifts early. Clear government and WDC signals about the importance and relevance of sub-degree level provision. Monitoring relativities between vocational and higher education rates.

Annex 5: Subject category groupings with 2021 full-year volumes by mode

UFS category	SAC category	Average of 2022 SAC rates	Proposed provider-based UFS rate	% of 2022 SAC rate	Volume by mode (FTELs)					
					Provider-based	*Extramural*	*Work-based*	*A&V*	*Total*	*% of volume*
Humanities, Business and Social Service Vocations (F1)	A J	$6,589	$5,425	82%	20,817	10,611	9,414	2,227	**43,069**	**34.5%**
Trades, creative, IT and health-related vocations (F2)	B I P	$10,481	$8,626	82%	24,237	2,240	19,665	378	**46,520**	**37.3%**
Engineering, Health, Science and Primary Industry Vocations (F3)	C L V	$11,742	$9,711	83%	11,284	2,176	8,962	685	**23,107**	**18.5%**
Pilot Training and Priority Engineering (F4)	M N	$13,934	$11,881	85%	1,262	207	449	3	**1,921**	**1.5%**
Specialist Low-volume, high-cost vocations (F5)	S H	$20,951	$16,275	78%[18]	129	12	0	18	**160**	**0.1%**
Te reo and Tikanga Māori (F6)	N/A	$6,589	$6,589	100%	10,098	0	0	0	**10,098**	**8.1%**
	Total	**$11,714**	**$9,751**	**83%**	**67,827**	**15,246**	**38,489**	**3,311**	**124,874[19]**	**100.0%**
				% of volume	**54.3%**	**12.2%**	**30.8%**	**2.7%**	**100.0%**	

[18] The average of the SAC rates for F5 is below 80 percent due to change to H2 from $21,851 in 2022 to $16,275 in the UFS (75 percent of the average SAC rates). H2 is a degree-level rate where diplomas occasionally utilise degree-level courses and receive the higher rate. There are only 35 FTELs in this category in 2021 and so we do not propose increasing the rate to set at 80 percent of the current SAC rates.

[19] Note that this includes all 4,432 non-resident FTELs from the 2021 full-year value of provision.