

Regulatory Impact Statement: Increasing funding flexibility and strengthening monitoring and compliance

Agency Disclosure Statement

This Regulatory Impact Statement has been prepared by the Ministry of Education. It relates to four problems.

- The limited flexibility Government has to make changes to funding mechanisms and conditions of funding subsequent to the approval of tertiary education organisations' (TEOs') investment plans, which in turn has shortened the time frame over which funding can be approved.
- The limited scope the Tertiary Education Commission (TEC) has to set conditions on funding of investment plans to improve wider organisational performance.
- The information requirements of the TEC to verify tertiary education institution (TEI) use of funding and compliance with funding conditions, and to identify risks in relation to TEIs' financial and educational performance.
- The TEC also needs an appropriate way of funding large investigations of likely breaches of funding conditions by TEOs, given that matters within TEO control affect the need, the cost, and the outcome of an investigation.

Consultation on proposed legislation was undertaken via an exposure draft of the Bill. 26 distinct submissions were received from a range of TEIs, private training establishments (PTEs), Crown agencies, sector peak bodies, individuals and other stakeholders.

In response to sector feedback, the Minister has agreed to further policy design detail to address some of the sector's concerns and maintain predictability for the sector.

A gap in the analysis is that no systematic costings of monitoring, compliance and enforcement proposals were undertaken. However, the TEC, which will implement any proposals, advised that it did not expect the implementation costs to be sufficient to influence the choice of preferred option.

Our understanding of costs was informed by the cost of investigations the TEC has undertaken over the last few years. The analysis of investigation cost recovery options assumed that the costs of large investigations of TEO breaches of funding conditions will continue to vary significantly from year to year.

The extent of compliance costs to the sector to expand condition-setting powers depends on the nature of any additional conditions on funding that will be imposed. These are unknown at this stage, and nothing specific is currently envisaged – they will depend on policy changes the Government decides to make following the date of commencement. Any significant changes of policy will, by convention, have Cabinet scrutiny.

The options considered are not dependent on other legislative proposals, although one would require new Regulations. The analysis includes the TEC's experience in

administering the tertiary education system within the current scope of its powers to set conditions. The analysis also relies on legal advice produced by the Ministry of Education for the purpose of providing policy advice to the Minister for Tertiary Education, Skills and Employment.

There are no time constraints. The TEC will need to do operational work when implementing new conditions on funding. The nature of this work is context-dependent.

A handwritten signature in black ink, appearing to read 'Roger Smyth', with a stylized flourish at the end.

Roger Smyth
Group Manager, Tertiary Education

4 November 2016

Executive summary

As part of a range of improvements the Minister for Tertiary Education Skills and Employment is making to improve the flexibility and workability of the tertiary education funding and monitoring system, four options have regulatory impacts that will:

Improve the flexibility of tertiary education funding legislation

- expand the Minister's powers to set conditions on funding in mechanisms issued under section 159L of the Education Act 1989
- expand the scope of the TEC's powers to set conditions on funding approved through investment plans, which is the main way tertiary education funding is approved by the TEC

Strengthen monitoring, compliance and enforcement

- improve TEC's access to information about TEIs' compliance with funding conditions
- meet a proportion of the cost of high-cost investigations of TEOs.

These proposals will allow greater flexibility to make necessary changes during the period for which TEOs are approved for funding via plan approval. They will also give the TEC more ability to invest funding in a provider or industry training organisation with confidence. Such additional flexibility and greater confidence will allow the TEC to utilise the full extent of the plan approval period, which is currently limited by the Government so it can make necessary changes in a reasonable time-frame.

The proposals will therefore indirectly reduce compliance costs for well-performing TEOs that are likely to have periods for which funding is approved increased to three years, allowing an additional year before they need to complete another investment plan. However, depending on the nature of the conditions that are set, there may be costs to providers.

Risks that the powers will be over-used or impose unnecessary costs are proposed to be managed through consultation and reasonable-notice requirements before mechanisms are changed or new funding conditions are set.

The monitoring, compliance and enforcement proposals aim to improve the accountability of TEOs for their use of Government funds. The proposals would strengthen the information and reporting requirements on TEIs, and allow the TEC to recover a proportion of the costs of high-cost investigations where a TEO is found to be at fault.

Structure of the regulatory impact statement

Confidence in the monitoring and accountability system allows for greater flexibility of funding approval – allowing TEOs to innovate and respond to incentives that will lead to improved tertiary education outcomes. This regulatory impact statement therefore covers both issues and the four options proposed. Other unrelated legislative proposals will be treated in separate regulatory impact statements.

However, the flexibility of tertiary funding legislation proposals are assessed with different criteria to the monitoring, compliance and enforcement proposals. This is because monitoring and enforcement powers are different in nature to condition-setting powers, and some of the criteria are specific to consideration of monitoring, compliance and enforcement.

To avoid the different sets of criteria contributing to reader confusion, the regulatory impact statement considers the regulatory impact of proposals to improve the flexibility of the funding legislation in two parts, each in turn. The 'monitoring, evaluation and review' section at the end of the Regulatory Impact Statement covers all proposals.

Part One: Improving the flexibility of tertiary education funding legislation

Status quo and problem definition

Background and objectives

Tertiary education is delivered by providers (or arranged by industry training organisations) on the basis of “investment plans” approved for funding by the TEC, with funding calculated on the basis of funding mechanisms issued by the Minister. Under the legislation, the TEC may approve funding for investment plans for up to three years.

The information and expertise of TEOs is centrally important to the outcomes the system produces, leading the TEC to operate the funding allocation system as flexibly as possible, while being able to enforce accountability and maintain oversight.

The Government is working to improve the information available to TEOs, students, and employers about study choices and employment prospects. This will allow TEOs to better meet demand – to improve the responsiveness and outcomes of tertiary education. Alongside this, the Government is looking for improved administrative efficiency and reduced transaction costs. In summary, the relevant objectives are:

- increased flexibility of the funding approval and funding regulatory framework so that TEOs can meet demand
- improved clarity and predictability of the system for TEOs, the public, and the Government
- improved incentives for TEOs to meet demand and achieve outcomes for students and stakeholders
- appropriate Ministerial and TEC oversight of the funding approval and regulatory framework.

Achieving these objectives may require trade-offs, so that increased flexibility and improved clarity is balanced with appropriate levels of oversight, and flexibility and predictability are balanced appropriately, for example.

Insufficient flexibility has led to shorter-term funding approvals than allowed under the Act

Currently, the TEC is only approving investment plans for well-performing organisations for up to two years. This is because there is:

- Insufficient ability for the Minister to add new conditions of funding to funding mechanisms during the three-year maximum period. Adding new conditions during the three-year maximum period might be contemplated for the following reasons.
 - To target new funding through an existing mechanism to TEOs for a specific purpose, e.g. to encourage a focus on work-integrated learning for information and communications technology graduates.
 - To manage emergent undesirable behaviour discovered during the early part of a plan period. Broad-based funding systems such as tertiary education can be exploited by bad actors from time to time. However, operating a broad-based system enables better responses to demand signals.

- To respond to events. For example new conditions of funding were imposed as part of the Government's response to the education and training needs deriving from the Christchurch Earthquake in 2011. Should there be another such event, there may be a similar need to tailor conditions to the requirements of recovery.
- A lack of clarity about the Minister's legal power to update funding mechanisms. For example to increase funding rates as has been done each Budget. The Minister has updated mechanisms on the basis that TEOs will agree to the change in mechanism because they benefit from it. However, this will not always be the case.

The status quo is resulting in unnecessary compliance costs

The tertiary education system has operated generally well using the work-around solutions required to maintain flexibility (e.g. two-year funding terms and updating mechanisms only where TEOs will agree to the changes). The system has significant levels of predictability for TEOs – within the demographic and macroeconomic trends that drive changes in demand for tertiary education places.

However, the development and approval of investment plans requires significant planning by TEOs, as well as consultation with stakeholders. By undergoing this process every two years instead of every three years, as envisaged by the Act, well-performing TEOs incur additional compliance costs. Allowing reasonable changes to be made during the period of plan approval allows the Minister and the TEC to reduce compliance costs by utilising longer-term plan approvals.

Operation of a flexible system requires up-front confidence to invest

TEOs' performance across multiple dimensions (including financial, educational, collaborative/outreach and scope of activity) impacts on the TEC's ability to fulfil its statutory functions. This is because these organisations are funded by the TEC to deliver educational outcomes that contribute to the goals of the Tertiary Education Strategy (TES); yet they are autonomous bodies with considerable freedom to define their own directions.

TEOs respond to a range of incentives which are not always controlled by government. Where these organisations have stronger incentives to invest in programmes and activities that are not domestic or international tertiary educational priorities, it has the potential to impact on performance in delivering the Government's priorities. Alternatively, performance or quality problems that impact on domestic provision could have their roots in the wider activities of organisations.

The TEC's power to set conditions on funding through approval of individual organisations' plans relate only to the dimensions of funded programmes and activities, and cannot directly address wider incentives on organisations even if these represent an issue for the TEC achieving its statutory functions.

Confidence by the TEC that TEOs will respond to positive incentives that will result in strong outcomes for students and employers, will, in turn, generate longer-term funding approvals. Greater confidence in providers' performance means that the TEC would be able to allocate funding knowing that its risks can be managed. In turn, TEOs can become more accountable for their performance and respond more confidently themselves to demand signals from students and employers.

Robust monitoring

The TEC will also have confidence to invest where it has sufficient tools to manage issues when they arise and has robust monitoring in place. Part Two of this Regulatory Impact Statement considers improvements to the monitoring system.

Objectives

The Government's objectives set out in the problem definition above – of increased flexibility, improved clarity and predictability, improved incentives on TEOs and appropriate oversight – provide the basis for assessing which options should be recommended for each of two areas:

- the Minister's ability to make reasonable changes to funding mechanisms including making updates and adding funding conditions subsequent to plan approval
- the scope of the TEC's condition-setting powers and their confidence to invest – allowing TEOs to respond to positive incentives to produce good outcomes.

There is no statutory requirement to review the legislation and no immediate time constraints. The TEC is operating a new plan approval process during 2016, for the 2017-2018 period. Making changes before 2018 will allow the TEC to make more three year plan approvals for high-performing organisations for the subsequent round (to be operated in 2018 for funding from 2019).

Options and impact analysis

Minister's ability to make reasonable changes to funding mechanisms including adding new conditions to funding

The two key options considered are set out in the sections below.

Status quo

Under the status quo, the Government would continue to only make changes to mechanisms and conditions that are unlikely to be challenged, and therefore that can be agreed to by affected TEOs. Government would generally only make changes that advantage affected organisations and must only add conditions before funding approval takes place.

To make other changes following plan approval, such as adding a new condition on funding, the Minister may be able to withdraw the mechanism and replace it – resulting in the TEC operating new funding processes. However, this option has not been tested legally, and is not specifically referenced in current legislation. Even if this option were legally sound, only the most significant of changes would justify imposing the level of compliance costs it would involve.

The status quo does not address the problems of a lack of legal clarity about updates to funding mechanisms. In turn, it would not contribute to use of the maximum three year funding term available under the Act and thus reduce compliance costs.

While the work-around adopted has operated successfully so far, it does result in a more complex system than otherwise. For example, funding mechanisms are augmented by 'supplementary mechanisms', and new funding targeted at specific priorities are funded

through separate mechanisms even when an existing broad mechanism applies. This complexity reduces the clarity and predictability of the system for TEOs.

The lack of flexibility to use new conditions on funding to respond to events or manage emerging issues limits the level of oversight the Government is able to have throughout the plan period. It limits the scope to improve the incentives TEOs respond to if there are urgent new priorities, e.g. recovery from a major disaster.

Keeping the status quo would minimise impacts on TEOs. However, should the lack of flexibility to respond to events result in a pressing need to make changes, and the Government instead resorts to the possible option of withdrawing funding approvals and re-running funding processes, there would be a significant compliance cost.

To allow the Minister to add reasonable conditions and make other changes to an existing funding mechanism (recommended option)

This option requires legislative change to give the Minister a power to add conditions that the TEC must attach to funding, and to clarify that funding mechanisms can be changed during the term of plan approvals (and the change would then be applied to the funding approval of affected TEOs).

The option improves the flexibility of the system from an administrative point of view, and sets the scene for greater flexibility for TEOs through longer-term plan approval terms. It improves incentives on TEOs by strengthening the ability to more clearly target priority funding and respond to undesirable behaviour and performance, and maintaining a broad-based system that is better able to respond to demand signals.

This option would improve the system's clarity, but reduce predictability of the mechanisms and conditions that would apply during the term of plan approval. In practice, overall predictability may not reduce significantly because the changes this option enables either happen currently (through the use of supplementary funding mechanisms) or are available every one or two years due to the shorter duration of plan approvals that the TEC currently operates.

TEOs would bear the impacts of additional conditions on funding imposed during the funding period, or changes in the mechanism that would result in a change in funding as calculated. The impacts in the longer term may be similar to those of the status quo, as new conditions that may have a cost to organisations would be imposed at the start of a new funding period anyway. In addition, well-performing TEOs would benefit from longer plan approvals.

Conclusion and recommendation

The analysis of options shows that a legislative proposal balances the different criteria better than alternative options. This is set out in the following table:

Lack of flexibility to make changes to mechanisms and for the Minister to have the power to add conditions after plan approval

	Is the system sufficiently flexible?	Is the system clear and predictable?	Are the incentives for TEOs effective?	Is oversight adequate?
<i>Option one - status quo</i>	✓	✓✓	✓	✓
Option two (recommended) - allow the Minister to add reasonable conditions and make other changes to an existing funding mechanism.	✓✓✓	✓✓	✓✓✓	✓✓✓

Note: One tick is least aligned with the criteria, three most aligned.

Limitation of TEC's condition-setting power to funded programmes and activities

The three options considered are set out in the sections below.

Status quo

The TEC would retain the power to place conditions on funding, but restricted in scope to programmes and activities that receive funding approval in investment plans.

This option does not address the TEC's level of confidence that it can manage the range of incentives on TEOs. Some of these incentives could undermine the quality of outcomes organisations produce. To enable the TEC to manage risks, the TEC may need to hold TEOs to more restrictive outputs or shorter plan terms than would otherwise be the case.

The status quo has no impacts on TEOs beyond what they do now. However, if a major TEO exits the system or performs poorly, there would be short-term but significant impacts on students, employers and regions. This is because the supply of qualified graduates to industries and regions might reduce, students would experience uncertainty about completing their studies, and employers would have uncertainty about future training arrangements.

Expand TEC's condition-setting powers to enable the TEC to more effectively perform its monitoring functions and maintain oversight of the performance of the tertiary education system as a whole (recommended option)

This option requires legislative change because the scope of the TEC's condition-setting powers are set out clearly in the Education Act 1989.

The TEC would have more flexibility to use conditions on funding to address concerns that a TEOs' capability to deliver on its investment plan commitments will be negatively affected by other non-funded activities, or where non-funded activities may diminish the Crown's investment in TEIs.

Expanding the TEC's condition-setting power, but limiting it to its monitoring and oversight functions, increases the TEC's ability to improve the performance of the system. It would increase the TEC's confidence to approve flexible investment plans for longer terms, allowing TEOs more ability to innovate within the terms of their plan approvals, while the TEC has greater assurance it can pre-empt and respond to issues.

Restricting the scope to the TEC's monitoring and oversight functions provides a safeguard against possible intrusion by the Government into areas of institutional autonomy and academic freedom. The legislation still preserves and enhances academic freedom and the autonomy of institutions, subject to the need for accountability by institutions and the proper use by institutions of resources allocated to them.

The clarity and predictability of the system to TEOs would not be significantly affected.

Expand TEC's condition setting powers, with no limitation

This option is unnecessarily broad. While it strengthens oversight and supports the confidence of the TEC to approve flexible investment plans, it may result in ineffective incentives on TEOs due to potential intrusion into the autonomous affairs of organisations, e.g. how they govern themselves. The level of oversight is therefore unnecessarily expansive.

Conclusion and recommendation

The analysis of options shows that a legislative proposal, limited to the TEC’s statutory functions – of more effectively performing its monitoring functions and maintaining oversight – balances the different criteria better than alternative options. This is set out in the following table:

TEC’s power to impose conditions on funding

	Is the system sufficiently flexible?	Is the system clear and predictable?	Are the incentives for TEOs effective?	Is oversight adequate?
<i>Option one - status quo</i>	✓	✓✓	✓	✓
Option two (recommended) – expand TEC’s condition setting powers to cover all of its statutory functions.	✓✓✓	✓✓	✓✓✓	✓✓✓
<i>Option three – expand TEC’s condition setting powers, with no limitation</i>	✓✓✓	✓✓	✓	✓✓✓

Note: One tick is least aligned with the criteria, three most aligned.

Consultation

In 2014, Universities New Zealand wrote to the Minister for Tertiary Education, Skills and Employment requesting longer-term funding. Among a number of recommendations to clarify funding signals to providers, they recommended extending investment planning for universities from the current two year period to at least three years. The proposals being considered here provide flexibility to steer the system and respond to issues, allowing this to happen.

The Ministry of Education consulted on an exposure draft of the Education (Tertiary Education and Other Matters) Amendment Bill between 23 September and 14 October 2016. The Ministry received 26 individual submissions from a range of TEIs, PTEs, Crown agencies, sector peak bodies, individuals and other stakeholders.

Amending a funding mechanism and adding a new funding condition during a plan period

- Nine submitters from a range of sectors commented on these proposals with a mix of views, the balance being opposed to the changes. Those opposed were concerned that the changes increase flexibility for the Government at the expense of funding certainty for the sector. Submitters considered that the changes would create an uncertain funding environment where the Minister could frequently change mechanisms/conditions of funding, which would, in turn:
 - make future planning more difficult
 - inhibit flexibility and responsiveness across the tertiary sector
 - make raising capital more difficult
 - mean that funding changes could be made without adequate lead in time.

In response, the Minister has agreed to the following drafting changes:

- to add that the Minister can only vary a funding mechanism (or add a condition that the TEC must attach to funding) when it is reasonably necessary to do so
- to include a minimum lead-in time of either the beginning of the next calendar year, or three months (whichever is greater) before the variation can take effect.

Expanding the scope of the TEC's condition-setting power

- One submitter supported this proposal, eight opposed, and three opposed as it is currently drafted. The submitter supporting the proposal noted that the sector will operate more effectively and in the interest of students if TEIs are better assessed and monitored in terms of their capability and capacity.
- Those who opposed, mainly from the university and PTE sectors, were concerned this proposal gives the TEC inappropriate reach into the wider business of TEOs. In response, the proposal has been amended so that any broader condition must be “reasonably necessary” to enable the TEC to effectively monitor the performance of organisations and the tertiary education sector generally.
- The issue was also raised that reasonable notice before imposing conditions should be defined, as submitters found the term “reasonable notice” to be unclear.

In response, the Minister has agreed to the following drafting changes.

- Removal of the word “quality” from the draft clause. This change means that any broader condition must be reasonably necessary to enable the TEC to effectively monitor the performance of organisations and the tertiary education sector generally. This specifies the focus of the TEC’s condition setting power more clearly than the original drafting,
- The clarification that reasonable notice in clause 12 should be a period of at least 21 days.

Implementation plan

Subject to passage of legislative proposals:

- Following the next Budget, the Minister for Tertiary Education, Skills and Employment will issue new updates to existing funding mechanisms as required. The Minister must consult with those TEOs that are affected by the proposed update, and may consult other organisations.
- From the date of commencement, the Minister will also add funding conditions if required in response to any issues that emerge for which additional funding conditions are the best option. The Minister must consult with those TEOs that are affected by proposed conditions, and may consult other organisations. This power may not be used immediately, because 2016 is a new funding round, and it is possible new issues will not arise for some time after that.
- The next plan funding round is due in 2018. The TEC will develop the types of conditions on funding required for this plan round. The TEC has an operational policy capacity, and a Board that will agree conditions, based on analysis from the TEC’s staff led by its CEO.
- The TEC is likely to approve significantly more plans for the maximum term of three years in 2018 following the passage of provisions allowing greater flexibility. This will lower compliance costs, and create more flexibility and clarity of expectations for organisations.

There is no need for transitional arrangements.

Implementation risks

The proposals augment rather than replace existing regulations. The key risk is that the additional flexibility for the Government to steer the system and manage issues does not flow through into more flexibility for TEOs, or longer term approvals of funding.

The TEC has incentives to operate as flexibly as possible, consistent with it being able to manage risks including poor performance and the misuse of public funding. The TEC’s performance depends on the use TEOs make of their own information about delivering and arranging tertiary education that meets demand, because it is impractical for a Crown funding agency to make such micro decisions itself. Increasing the TEC’s confidence in managing issues and protecting public funding will strengthen incentives to operate flexibly. Such flexibility will keep compliance costs as low as reasonably practicable consistent with risk management.

As the outcomes of the system are delivered by third party organisations, there are times when it is possible for organisations to hide information from the TEC, which only becomes available to them following targeted audits. Incentives driven by the TEC's monitoring and enforcement of conditions would minimise this behaviour.

There is no scope to reduce or remove existing regulations as part of this specific set of proposals.

Part Two: Monitoring, compliance and enforcement proposals

Status quo and problem definition

New Zealand's tertiary education system is designed to deliver on the Government's tertiary education strategy, while giving tertiary education providers the flexibility to respond to changing skill needs, and deliver education in innovative ways. Providers' right to academic freedom and institutional autonomy is part of their credibility, and is protected under the Act. However, that freedom and autonomy need to be balanced by accountability. The credibility and integrity of the system require appropriate monitoring and enforcement. This protects the Government's investment in tertiary education and the interests of students and employers.

The TEC has the role of allocating tuition funding to TEOs, setting detailed conditions on this funding to ensure that it achieves the intended outcomes, and monitoring the performance of organisations against these conditions. The TEC can recover funding if a TEO fails to meet the conditions. Five TEC investigations proved breaches of funding conditions between early 2014 and early 2016, and showed that a significant amount of tuition funding was recoverable. Funding that has to be recovered is funding that could have been allocated to other TEOs that could have made proper use of it.

Improving TEC access to information about TEI compliance with funding conditions

As part of its monitoring role, the TEC can require regular reports from funded TEO, and can inspect records of a TEI identified as high risk, to make sure that funding is being used as intended.

The TEC also has a power under the Education Act 1989 to require non-TEIs (such as PTEs and industry training organisations) to keep certain records showing how they are using tuition funding and whether they are meeting funding conditions. The TEC can check these records at any reasonable time. This helps the TEC to check that the information it receives through regular reporting is accurate. The TEC does not have this power in relation to TEIs.¹

In the absence of this power, the TEC has tended to rely on negotiation to access records to verify reported information. From 2016, the TEC has made access to inspect records a condition of funding.

There are two problems with the current arrangements for verifying TEI information. The new funding condition is not a legislative requirement and remains untested. Therefore, it does not provide the certainty of legislation. Furthermore, it does not result in consistent requirements for TEIs and non-TEIs in terms of the form and availability of records – a

¹ Sections 159YD and 159ZE of the Education Act 1989 establish the relevant TEC powers with respect to non-TEIs.

difference in treatment that is difficult to justify. These problems make it less likely that financial and educational risks will be identified early.

Reasons for the status quo may include a perception, when the Act was passed, that TEIs were less likely to be non-compliant than PTEs. However, recent cases show that TEIs do sometimes breach funding conditions and receive more funding than they were entitled to. The proposed requirements do not duplicate the TEIs' record-keeping and reporting requirements under other legislation.

Meeting the cost to TEC of high-cost investigations of TEOs

If the TEC considers that a provider or industry training organisation may not have complied with funding conditions and an initial review does not alleviate these concerns, it can open a more comprehensive investigation.

There are two problems with the status quo. Firstly, investigations can have a material and unpredictable impact on the TEC's operating costs, despite costing a small proportion of the recoverable tuition funding they identify. Costs vary greatly between investigations, and from year to year. Secondly, TEOs at fault, whose behaviour is the main driver of the need for investigations and whose degree of cooperation can affect the cost of an investigation, are not accountable for some of the costs resulting from their decisions. They are, in terms of Treasury guidelines on cost recovery, "risk exacerbators".

Offsetting the costs of investigations from the TEC's baselines has the merit of administrative simplicity. In principle, a further benefit of a fixed budget is that it forces agencies to prioritise expenditure which can promote efficiency. However, because of the importance of ensuring that tertiary education funding is used for its intended purpose, the TEC would always prioritise the investigation of a provider or industry training organisation suspected of serious misuse of funding, regardless of budget pressures.

Objectives

The TEC needs the power to carry out its funding and monitoring functions effectively. This includes:

- the ability to access all information required to monitor all TEOs
- the funding to undertake investigations, and adequate levers to encourage TEOs to comply with funding conditions and cooperate with reviews and investigations.

The detailed criteria developed to evaluate the available options were:

- information is provided or interventions can occur in a timely fashion
- compliance costs to TEOs are as low as possible
- administrative costs to government are as low as possible
- high performance from TEOs is promoted
- agencies' powers are the minimum necessary to be effective
- agencies' powers are tailored to provider or industry training organisation type (if appropriate) and
- information is of good quality.

Options and impact analysis

Improving TEC access to information about TEI compliance with funding conditions

The status quo rates well in terms of most of the evaluation criteria. The areas of doubt are whether the funding condition providing for inspection of TEI records provides sufficient access to relevant records – that the existing powers can be tailored to different subsectors and provide quality information, and whether the information the TEC can obtain from TEIs is of sufficient timeliness, quality, and consistency.

Amending the legislation to give the TEC the same powers to specify and inspect TEI records that it has with respect to PTEs and industry training organisations would clarify that the requirements for TEIs and PTEs are the same, ensuring equity of treatment. The legislative change could also help to improve the quality and consistency of TEI records and the timeliness of TEC’s access to those records. In other respects, the legislative change option is similar to the status quo, but it might slightly reduce administrative costs and slightly increase compliance costs.

Table 1 summarises officials’ evaluation of the options against the criteria.

Table 1: Summary of criteria analysis – TEC access to TEI information

	Timely information & interventions	TEO compliance costs	Government administrative costs	TEO performance is promoted	Minimum necessary power	Powers tailored to TEO subsectors	Quality information
<i>Status Quo</i>	✓✓	✓✓✓	✓✓✓	✓✓✓	✓✓	✓	✓
<i>Option 1 – Legislative change</i>	✓✓✓	✓✓✓	✓✓✓	✓✓✓	✓✓	✓✓✓	✓✓

Note: One tick is least aligned with the criteria, three most aligned.

Meeting the cost of high-cost investigations of TEOs

The criteria relevant to this issue were those relating to compliance and administration costs, the promotion of provider or industry training organisation performance, and the question of whether the proposed TEC power is the minimum necessary to achieve the broader objectives.

Under the status quo, TEOs bear some of the cost of investigations, in responding to requests for information. However, they bear none of the cost to the TEC of purchasing third party investigation services, which is the major part of the cost of the investigation. For significant investigations, the TEC prefers to utilise third-party investigators with specialised investigative skills and a degree of independence from the outcome of the investigation. The costs of investigations tend to vary with the degree of cooperation by the provider or industry training organisation. Accordingly, the status quo has relatively low compliance costs and relatively high administration costs which, in some cases, are over \$200,000.

The status quo does little to promote provider or industry training organisation performance and does not enable the TEC to make TEOs at fault accountable for this part of the cost of their non-compliance.

Officials' evaluation of the options is summarised in Table 2, below.

Increase the TEC's funding for investigations

Option 1, an increase in the TEC's funding for investigations, would not alter provider or industry training organisation compliance costs or improve their incentives to perform and to cooperate with reviewers and investigators, but it would address the TEC's concern about how to fund investigation costs (which vary from year to year).

Use funding conditions as a way to recover costs

Officials considered two options for recovering investigation costs from TEOs using funding conditions, without new legislation. In Option 2, the TEC would recover the costs of specific investigations from providers found to be at fault. In Option 3, the TEC would withhold a portion of funding from all TEOs and pay it at the end of the year unless the provider or industry training organisation had been in breach of funding conditions. Further examination of these options suggested that neither is permitted by the current legislation. If they were implemented, either option would shift some costs from the TEC to TEOs at fault and could strengthen providers' or industry training organisations' incentives to comply with conditions and cooperate with reviewers and investigators.

Impose a levy on all TEOs

Option 4, a levy applicable to all provider or industry training organisation funding, would require legislation. The revenue would be held in trust to cover the costs of future investigations. This would shift investigation costs to all TEOs, rather than just those at fault. It would provide some incentive for the sector as a whole to encourage compliance and cooperation, since the amount of the levy would reflect the expected costs of investigations. On the whole, it would not have the effect of making TEOs at fault accountable for the full impacts of their actions.

Provide legislatively for the TEC to recover costs of investigations where a provider is found to have breached funding conditions

In Option 5, legislation would enable the TEC to recover a proportion of the costs of investigations, up to a maximum figure, where fault is proved (that is, where funding is found to be recoverable as a result of a breach of funding conditions). Regulations, subject to consultation with the sector, would put appropriate constraints on the TEC's ability to recover costs. The TEC would consider the likely impact of recoveries on the financial viability and educational performance of the provider or industry training organisation.

This legislative option would shift some of the cost of large investigations to TEOs that are proven to have breached conditions of funding. A likely scenario is that the TEC would bear the cost of an investigation up to a certain amount (possibly the average cost of an investigation), with the provider or industry training organisation bearing a maximum proportion of the cost that would take account of any possible impacts on their financial and educational viability.

The cost of investigations is small compared to the total amount of tertiary education funding expected to be recovered as a result. This suggests that cost recovery for TEC investigations

is unlikely to have significant negative impacts on TEOs. However, it would have the benefit of making TEOs more accountable for the consequences of breaches of funding conditions.

Table 2: Summary of criteria analysis – funding large investigations

	TEO compliance costs	Government administrative costs	TEO performance is promoted	Minimum necessary power
<i>Status Quo</i>	✓✓✓	✓	✓	✓
<i>Option 1 – Increased TEC baseline funding</i>	✓✓✓	✓✓	✓	✓✓✓
<i>Option 2 – Funding condition: cost recovery (found to be ultra vires)</i>	✓✓	✓✓	✓✓✓	✓✓
<i>Option 3 – Funding condition: withhold funding (found to be ultra vires)</i>	✓	✓	✓✓	✓✓
<i>Option 4 – Legislation change: levy</i>	✓	✓✓	✓✓	✓
<i>Option 5 – Legislation change: cost recovery</i>	✓✓	✓✓✓	✓✓✓	✓✓

Note: One tick is least aligned with the criteria, three most aligned.

Consultation

Public consultation was undertaken through an exposure draft of the Education (Tertiary Education and Other Matters) Amendment Bill between 23 September and 14 October 2016. Feedback from submissions provided mixed views on both the proposal to improve access to information, and the proposal for recovery of investigation costs.

Improving access to information

- Three submitters, including two unions, supported the aligning of record keeping and inspection requirements for TEIs with TEOs. One wānanga supported the inspection of records and another supported the principle of greater accountability.
- Four submitters, particularly non-TEIs but including one wānanga, opposed or raised concerns around the likely costs, the cost-benefit payoff of the proposal, and whether the proposal should be targeted to poor or non-compliant providers only.
- The Ministry considered that the likely costs are reasonable and justifiable given the amount of government funding at stake and that the proposal is necessary and should apply to all providers who receive government funding.

Recovery of investigation costs

- Six submissions from across the sector either clearly supported the proposal for recovery of investigation costs or supported it in principle. One submitter opposed the proposal as unfair as they believe TEC investigators do not always understand the sector well enough to evaluate it correctly and make the right findings. They highlighted the concern that TEOs would have to pay for some of the costs of such investigations, and the potential conflict of interest where the TEC as investigator is also the beneficiary of any cost recoveries.
- The main issue raised by some submitters was that the limits on the TEC's powers of cost recovery should be clarified.
- The Ministry considers that the proposed limits on the TEC's powers to recover costs largely address these concerns. For example, as only a proportion of the TEC's investigation costs will be recoverable, the TEC will still have an incentive to manage investigation costs.
- Future communications regarding the proposal will also point out that the detailed rules for cost recovery would be set out in Regulations that would be subject to consultation with the sector.

In addition:

- The proposed amendments relate to the use of tuition funding in accordance with funding conditions, and would not create powers to limit academic inquiry or freedom of expression.
- In exercising its powers, the TEC is required under the Act to preserve and enhance academic freedom and the autonomy of institutions².

² Section 161 of the Education Act 1989 refers.

In response to sector feedback, we have agreed to work with the Parliamentary Counsel Office to ensure the drafting of the Bill be amended to clarify that only actual and reasonable costs associated with the investigation of a demonstrated breach should be recoverable.

Conclusions and recommendations

Improving TEC access to information about TEI compliance with funding conditions

Option 1 is preferred. This involves legislating to place the same record-keeping and inspection requirements on TEIs as there are on non-TEIs such as PTEs.

Compared to the status quo, Option 1 would tend to strengthen the monitoring of TEI performance and achieve greater consistency in the treatment of TEIs and PTEs, without significant negative impacts on TEIs. However, recent funding conditions providing for TEC inspections of TEI records achieve part of this result without legislation.

Meeting the cost of high-cost investigations of TEOs

Option 5 is preferred. This involves legislating to enable the TEC (under regulations) to recover a proportion of the cost of high-cost investigations that result in recovery of funding (ie. where a breach of funding conditions is proved).

Only a small number of TEOs would be directly affected and, with the anticipated constraints on TEC cost recovery, the impact on those required to contribute to the cost of investigations would be modest. However, partial cost recovery for large investigations of TEOs found to be at fault would have the benefit of making TEOs more accountable for the consequences of breaches of funding conditions.

Implementation plan

Subject to the proposed legislation passing, the TEC will implement the legislative changes and communicate them to affected TEOs. In implementing the changes the TEC will consider the Government's interest in an effective network of tertiary education organisations, and in achieving value for the Government's investment in tertiary education. As such, the TEC has an interest in, and will, avoid imposing undue compliance costs.

Improving TEC access to information about TEI compliance with funding conditions

The TEC intends to set requirements for TEIs, in terms of the form of required records, that are similar to those that apply to PTEs. These will be incorporated into TEC's funding conditions for TEIs, as new funding agreements are negotiated. The negotiation process enables unintended impacts of proposed requirements to be identified and addressed.

For many TEIs, the new requirements will not involve any change to current practices. If the TEC requires changes to the form of records, the TEC will allow TEIs a reasonable period of time to make these changes. However, the TEC may inspect TEI records, based on any existing requirements, from the day the legislation is passed.

The new requirements would not duplicate existing record-keeping legislation or regulations so the change does not mean there is scope to reduce existing regulations.

Improved TEC access to TEI information would support effective enforcement of funding conditions.

Meeting the cost of high-cost investigations of TEOs

The proposal to enable the TEC to recover some of the costs of large investigations will require regulations setting out limits on what the TEC can recover. The proposed regulations and the TEC's implementation of them will be informed by Treasury guidelines on cost recovery and by consultation with the sector. Once the regulations are passed, the TEC will communicate them to TEOs and advise on its policy on the application of the regulations.

The TEC will discuss the timing of recovery of costs with any affected TEOs as required, just as it does in the case of significant funding recoveries. Costs may be recovered as an offset against additional funding. Since most TEOs that have received TEC funding wish to continue to receive it, this will generally be an effective enforcement strategy if required.

Monitoring, evaluation and review

The Ministry of Education and the Ministry of Business, Innovation and Employment monitor the performance of the TEC.

The Ministries consider the effectiveness of the overall regulatory framework, and its constituent parts, on an ongoing basis as part of general work to improve the performance and outcomes of the tertiary education system.