MITCHELL POLICY PAPER

# VET funding in Australia

## Background, trends and future directions

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## About the author

**Professor Peter Noonan**

Mitchell Professorial Fellow, Peter Noonan has played a major role in shaping tertiary education policy in Australia through 25 years' experience working as a policy adviser, senior executive and consultant to federal and state governments, universities, higher education providers and TAFE institutes. He was a member of the Expert Panel for the Review of Australian Higher Education (Bradley Review) in 2008, and in 2010 undertook a Review of Post-Secondary Education in Queensland for the State Government. Peter's work as a Mitchell Institute Fellow is focused on the future of tertiary education in Australia including its interface with secondary education and the labour market. He is Professor of Tertiary Education Policy at Victoria University and an Honorary Senior Fellow at the Graduate School of Education at the University of Melbourne.

## About the Mitchell Institute

The Mitchell Institute is an independent think tank that works to improve the connection between evidence and policy reform. We actively promote the principle that education is fundamental to individual wellbeing and to a prosperous and successful society. The Mitchell Institute was established in 2013 by Victoria University, Melbourne, with foundational investment from the Harold Mitchell Foundation.

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# Executive summary

The vocational education and training (VET) system in Australia plays a central role in the development of skills for the Australian workforce and makes a critical contribution to workforce participation, productivity levels, individual's life chances and economic and social development. The level of public and private investment in VET is therefore an important public policy issue.

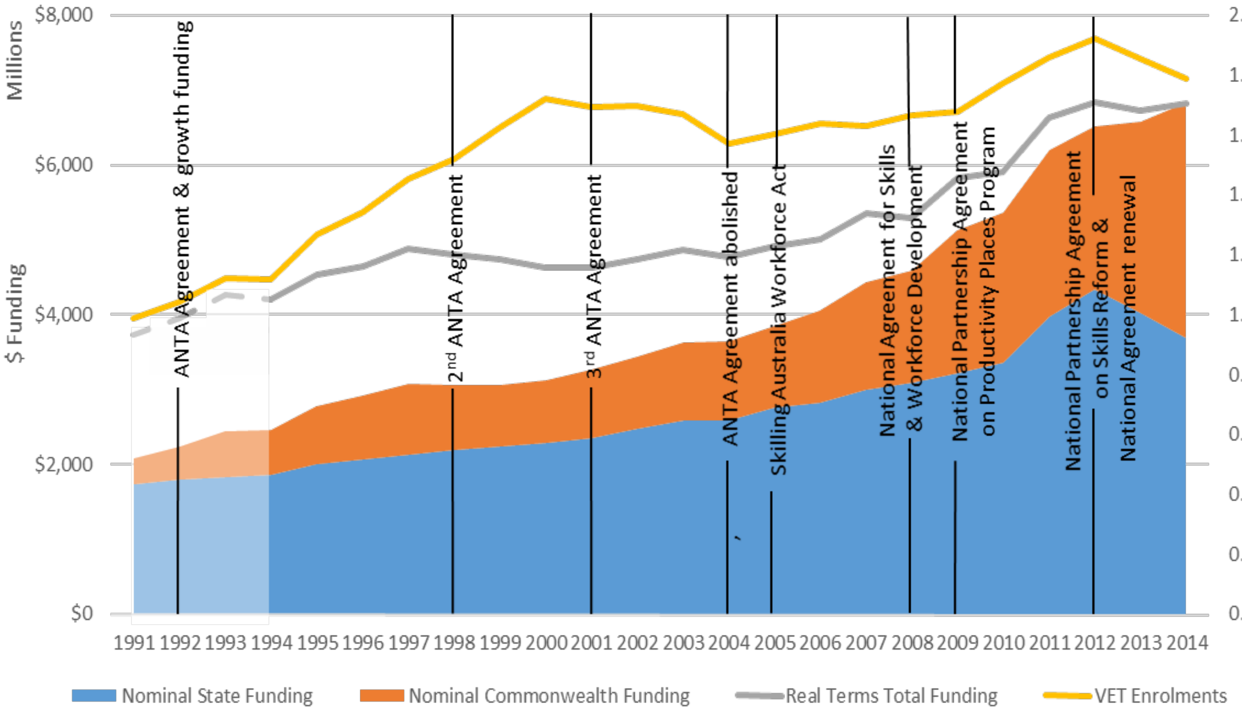
## Historical overview

Since 1974 the Commonwealth and state governments in Australia have jointly funded the development and expansion of Australia's VET system. They have done so in the following phases.

- **The development of the TAFE system (1974 – 1987)** - the Commonwealth and states jointly established and funded the Technical and Further Education (TAFE) system.
- **The emerging national system (1987 – 1991)** - the Commonwealth formalised TAFE Resource Agreements with the states. These agreements linked Commonwealth policy objectives to outcomes agreed with the states. The Commonwealth and the states cooperated on the development of a national VET system and undertook a review of future VET resourcing needs. To meet future resourcing needs, the Commonwealth proposed that it should take over responsibility for VET funding.
- **The first ANTA Agreement (1992 – 1996)** - the Commonwealth and the states jointly agreed to establish a national VET system through a new Australian National Training Authority (ANTA) reporting to state and Commonwealth VET Ministers. The ANTA Agreement was reached after the states rejected the proposal by the Commonwealth to take over responsibility for TAFE funding from the states. The Commonwealth agreed to fund growth in the VET system subject to the states maintaining expenditure on VET in the short term and outputs thereafter.
- **Renewals of the ANTA Agreement (1997 – 2004**) - the ANTA Agreement was renewed in 1997 and 2001. Each of these renewals was characterised by protracted negotiations over which level of government should fund ongoing growth in VET and by a propensity for the Commonwealth to fund specific VET policy objectives outside of the Agreement. A new ANTA Agreement had not been reached in 2004 when the Commonwealth unilaterally abolished ANTA.
- **Skilling Australia's Workforce Act (2005 – 2007)** - this Act gave effect to the abolition of ANTA and strengthened the Commonwealth's role in the national VET system while retaining the structure of the joint Commonwealth-state VET funding agreement.
- **National Agreements and National Partnership Agreements (2008 – 2016)** - within the structure of a new Intergovernmental Agreement on Federal Financial Relations (IGAFFR) the Commonwealth and the states entered into a series of National Agreements to raise the proportion of the workforce with VET qualifications through a VET student entitlement and skills reforms including the extension of income contingent loans through VET FEE-HELP. Loan payments by the Commonwealth grew rapidly and unsustainably leading to major changes to and a current review of the scheme. Through VET FEE-HELP and other Commonwealth programs, Commonwealth funding outside of the Agreements also increased significantly.

The following figure shows the effect of this collective investment from 1991 to 2014 (the period when comparable data is available).

**VET funding levels and shares and VET enrolments 1991 – 2014**




The figure shows that since 1991 real terms VET expenditure has fallen into four broad phases:

1. The initial phase of growth funding under the ANTA Agreement (1991 – 97)
2. A period of static funding (1997 – 2006)
3. Further growth in funding (2007 – 2012)
4. A further period of static funding where increases in Commonwealth outlays offset declines in state outlays (2012 – 2014).

The Commonwealth's share of public VET funding has grown significantly since 1991 when growth funding commenced.

Publicly subsidised enrolments are ultimately driven by public funding levels and as such the pattern of VET enrolments broadly follows the four expenditure phases.

## Issues

While much has been achieved through this collective investment, the tensions and weaknesses in a shared funding agreement have continually surfaced. These include:

- the difficulty of applying a uniform system of Commonwealth funding across multiple jurisdictions with differing budgetary needs and priorities;
- how both levels of government can benefit from reduced costs associated with increased efficiency;
- the frequent tendency of the Commonwealth to act as a direct funder outside of the agreement when it wishes to directly secure specific outcomes;
- growing differences between jurisdictions in funding for the same qualification and in eligibility criteria for the VET student entitlement, compared to nationally consistent pricing and eligibility criteria in higher education; and
- funding differences contributing to variation in participation levels and qualification completions.

These weaknesses have been magnified in the nature and structure of the current national partnership agreements governing VET. Under these agreements short term improvements in VET funding, participation and qualification completions were unevenly distributed between the states and have not resulted in an ongoing and sustainable VET funding base.

Publicly funded VET enrolments are 13 per cent higher than they were 10 years ago, an increase of just 200,000 enrolments, and have trended down since 2012. This compares to undergraduate enrolments which have risen 43 per cent over the same period and which continue to rise.

A further deterioration in VET funding levels is highly likely. The gap in funding between VET and the other sectors of education will widen, diminishing pathways for school leavers wishing to enter VET, potentially distorting choices between VET and higher education and limiting opportunities for workforce retraining and upskilling.

The issue of future responsibility for funding VET is again under consideration by the Council of Australian Governments. The Commonwealth is also undertaking a consultation and review process for the redevelopment of VET FEE-HELP.

A draft paper prepared by the Commonwealth for COAG proposes that it assume full funding for 'mainstream' VET qualifications by bringing together subsidies and income contingent loans (with deregulated fees) in areas of national skills priorities. Funding would be fully competitive with TAFE funded by the Commonwealth at the same rate as other providers. The states would retain responsibility for ownership and management of their TAFE systems and could fund TAFE but only to the extent required to ensure 'competitive neutrality' with other providers.

The draft paper makes an important contribution by proposing a more coherent funding system by linking course subsidies and income contingent loans into a single national pricing system (although the risks of fee deregulation operating with income contingent loans are not recognised as experience with VET FEE-HELP has shown).

However, the draft paper fails to address the underlying problems with the current Commonwealth/state funding model: declining overall investment in VET (with the exception of VET FEE-HELP) and increasingly uneven investment across the states and territories.

Further, the draft paper does not seem to have provided a sufficiently compelling policy rationale to persuade at least some states to withdraw from VET funding. Nor does it provide a sufficiently detailed explanation of how a nationally funded system would work, including the important role of TAFE as the public VET provider.

The worst outcome for VET would be an impasse at COAG and a default to the current flawed funding model.

## A way forward

The following steps are suggested as a process to guide future government decisions on funding responsibility for VET.

1. Develop a forward looking view about the nature of the VET system required by Australia in the 21st century as a highly innovative and adaptive economy and society.
2. Develop a clear understanding of the provider system required to deliver those outcomes – including the future role of TAFE as the public provider – and the role of other agencies including the national VET regulator.
3. Undertake a national assessment of future participation and resourcing requirements for VET- with a primary focus on the need to ensure that all young people have access to tertiary education across higher education and VET.
4. Agree on the range of qualifications that should be funded under a national VET system.
5. Develop a funding model for those qualifications by setting:
    i. an efficient or benchmark price for each qualification;
    ii. the balance between public and private contributions (to make up the total price).
6. Redesign VET FEE-HELP to extend it to all nationally funded VET qualifications while ensuring that the scheme is sustainable – including options for providers to help meet the costs of income contingent loans.
7. Determine the respective roles of the Commonwealth and the states. Options include:
    a. The Commonwealth could fully fund the course subsidy and meet the costs of income contingent loans (the costs of borrowings and unpaid debt).
    b. The Commonwealth and each state and territory jointly fund the course subsidy and meet the costs of VET FEE-HELP.
    c. The Commonwealth and the states could agree to each fund specific qualifications – for example the Commonwealth could fully fund Diplomas and Advanced Diplomas to ensure a consistent approach across VET and higher education – and fully meet the costs of income contingent loans for the qualifications they fund.

However, none of these options in themselves addresses the fundamental issue that clearly emerges from the analysis in this paper: declining levels of public investment in VET - particularly in some jurisdictions - and the consequences of the growing imbalance of investment in VET relative to schools and higher education. Addressing that issue is the threshold issue for COAG when it considers future options for funding VET in Australia.

Decisions on the future of VET should be taken as part of a redesign of funding of tertiary education in Australia across the VET and higher education sectors – a process in which the Commonwealth must take the lead.

# Introduction

## Background

The financing of education and training in Australia, with a particular focus on the tertiary education system, is a key part of the Mitchell Institute's work program.

The Mitchell Institute's tertiary education program is intended to inform policy development and public debate about financing issues in the higher education and vocational education and training sectors, and to develop options for a more coherent system for financing tertiary education across the sectors.

To date, seven reports and papers have been produced as part of this program:

- *VET funding in Australia and the role of TAFE* (Peter Noonan speech to TAFE Directors Australia Conference 2014)
- *Expenditure on education and training in Australia 2014* (Noonan, Burke, Pilcher and Wade, 2014)
- *Expenditure on education and training in Australia: update and analysis* (Noonan, Burke, Pilcher and Wade, 2015)
- *Financing tertiary education in Australia - the reform imperative and rethinking student entitlements issues paper* (Noonan and Pilcher, 2015)
- *Building a sustainable funding model for higher education in Australia - a way forward* (Noonan, 2015)
- *Feasibility and design of a tertiary education entitlement in Australia* (Chapman and Higgins, 2015)
- *A model for tertiary education funding in Australia* (Peter Noonan speech to *Australian Financial Review* Higher Education Summit, 2015).

The Institute is now preparing a final paper on the design of a long-term, comprehensive system for financing tertiary education in Australia, spanning the VET and higher education sectors.

## Purpose of this paper

The vocational education and training (VET) system in Australia plays a central role in the development of skills for the Australian workforce and through that role makes a critical contribution to workforce participation, productivity levels, individual's life chances and economic and social development.

The level of public and private investment in VET is therefore an important public policy issues. The Mitchell Institute has pointed to declining levels of public investment in VET. This paper has been specifically prepared to help inform consideration and debate about the future VET of funding in Australia.

VET is currently funded under a shared funding model between the Commonwealth and the states, while higher education is funded by the Commonwealth. A draft paper prepared by the Commonwealth Government for the Council of Australian Governments proposes that the Commonwealth now also assume responsibility for funding VET – a proposal that has attracted both support and opposition. The significant increases in outlays to VET providers under the Commonwealth's VET FEE-HELP scheme and the settings for VET FEE-HELP are another important consideration in VET funding policy.

The paper summarises the evolution of the VET shared funding model and assesses its effectiveness over time in terms of funding, participation and enrolments and the changing shares of Commonwealth and state funding particularly through VET FEE-HELP.

It concludes by outlining, in broad terms, options for future funding responsibility for VET. More detailed design options will be included in the Institute's forthcoming paper on tertiary education funding.

## Methodology

The author has participated in the early development of the VET funding system and subsequent research into VET funding in Australia. This paper draws on this knowledge and experience, and uses additional independent resources, including source documents and research papers. Discussions were also held with key individuals who have been involved in the development and negotiation of intergovernmental agreements, and with others who have expertise in VET funding. The Australian Parliamentary Library has been an invaluable source of information on the purpose and implications of various pieces of Commonwealth legislation governing VET funding.

Some individuals also provided feedback on drafts of the paper. Their comments have been taken into account however the author takes full responsibility for the content of this paper.

Jon Chew and Alec Webb from ACIL Allen Consulting prepared the graphs and figures analysing finance data. Kulja Coulston, Acting Communications Director at the Mitchell Institute, assisted with editing the paper and helped to navigate the thicket of VET funding agreements.

Data used to analyse current trends in VET financing is sourced from the National Centre for Vocational Education Research (NCVER) VET finance collection 2014 and the Department of Education and Training VET FEE-HELP statistical collection. The inclusion of VET FEE-HELP data in VET funding analysis presents a particular challenge; while FEE-HELP payments flow directly to providers, the annual costs to government are the cost of interest subsidies and provision for doubtful debt. In order to examine the roles of each level of government in publicly funded VET provision, VET FEE-HELP outlays to providers are included in some analysis in this paper. This is consistent with the treatment of VET FEE-HELP in the NCVER collection.

While this paper is focused on public funding currently captured through NCVER and ABS collections, it is recognised that some categories of state and Commonwealth VET funding are not currently captured in the NCVER collection. This paper does not capture private investment in VET other than fees received by public providers, or include the NCVER's recent Total VET Activity (TVA) collection, which was produced for the first time in 2015.

# Development of the Australian VET funding system

## The development of the TAFE system (1974 – 1987)

Under the Australian Constitution responsibility for education resides with the states and territories. However, the Commonwealth government has played an increasingly significant role in education funding and policy since the 1960s, when it began to provide funding for schools and higher education through specific-purpose payments to the states.

In 1973, as part of the Whitlam Government's election commitments the Commonwealth assumed full responsibility for the funding of higher education from the states and significantly increased funding for schools. In 1973 the Commonwealth also commenced a program of employer subsidies to support the uptake of apprenticeships[i] . At that time technical education (including apprenticeships) was provided through secondary technical schools and technical colleges in the states. It was not a discrete sector of education and did not receive specific Commonwealth funding.

However, after the Report of the Australian Committee on Technical and Further Education (Kangan Review) in 1974 the Commonwealth played a critical role in the development of Technical and Further Education (TAFE) as a new and distinct sector of post school education[ii].

The Commonwealth commenced a program of funding through the states to implement the recommendations of the Kangan Review. Although state based, TAFE quickly developed a distinctive national character and purpose based on the philosophy articulated in the Kangan Report of accessible vocational education for young people and 'second chance' adult education.

The Commonwealth's primary funding role in the development of TAFE was through capital investment to refurbish dated facilities and to establish new TAFE campuses and institutions. The Commonwealth also provided recurrent funding to the states, to compensate them for revenue lost when they agreed to abolish tuition fees, and to assist with the running costs of their TAFE systems.

The Commonwealth also funded small, but important, programs in areas such as TAFE teacher education, curriculum development, staff development and research. These programs helped to give TAFE its national character. TAFE funding continued to receive priority under the Fraser Government (relative to schools and higher education) partly because of years of neglect of the sector but also because of its role in industry development and redressing growing levels of unemployment particularly amongst young people[iii].

Over time a range of other TAFE initiatives were separately funded by the Commonwealth through specific-purpose payments to the states. These were designed to achieve particular Commonwealth policy objectives, particularly those related to redressing youth unemployment such as the Participation and Equity Program (PEP), an initiative of the Hawke Government in 1983.

In 1985, following the Report of the Committee of Inquiry into Labour Market Programs (the Kirby Report), the Commonwealth also commenced funding the off the job costs of training for the new Australian Traineeship System (ATS). The Commonwealth directly contracted public and private providers for traineeship delivery rather than funding the states for delivery through TAFE.  The Commonwealth also extended its program of employer subsidies to encourage the uptake of traineeships[iv] These were important precedents in terms of future Commonwealth direct funding interventions in the apprenticeship and traineeship systems, and the opening up of public funding for providers other than TAFE.

## The emerging national VET system (1987 – 1991)

From 1987, the Commonwealth as part of the process of economic reform in Australia, and with the active support of trade unions and employer bodies, embarked on a process to raise and broaden the level of workforce skills through the restructuring of industrial awards to broad skills based categories.

After the 1987 Federal election, the Commonwealth integrated its previously separate portfolios and agencies responsible for TAFE policy and funding and industry training and apprenticeship into a single new department.

In 1988, the Commonwealth consolidated its TAFE state recurrent funding programs into a formal resource agreement with each state. These agreements directly linked Commonwealth policy objectives to Commonwealth TAFE funding to the states. Some states, particularly NSW, objected to the Agreements as they considered it an intrusion into state policy sovereignty over TAFE. However, the Commonwealth ultimately prevailed and established the model under which future Commonwealth funding for TAFE (and subsequently VET) was to be allocated.

By the end of the decade, the Commonwealth became concerned about the capacity of the TAFE system to meet growing workforce skills needs flowing from the award restructuring process and at the Commonwealth's declining share of current funding for TAFE (as this diminished its policy influence). In the context of major reforms aimed at expanding participation in higher education, the Commonwealth was also concerned at the potential for an imbalance between higher education and TAFE[v] particularly given the deterioration in the financial position of some states.

The Commonwealth – with the support and active involvement of the states – was also seeking to drive the establishment of a national VET system incorporating TAFE and non-government VET providers. The key elements of this system included national recognition of VET qualifications, based on national industry standards, and national recognition of training providers – including TAFE – to support the development of a 'training market' in Australia. The Commonwealth recognised that its capacity to drive the establishment of a national system depended heavily on its level of investment in VET and its potential leverage from that investment.

In 1990, at the initiative of the Commonwealth, the Ministerial Council responsible for Vocational Education and Training commissioned a report The Training Costs of Award Restructuring (the Deveson Report). After analysis of potential future demand and projected increased industry expenditure the Report proposed:

> *that governments should set themselves a target – a training guarantee – of a five per cent per year increase in real terms in public sector training provision. This would imply an increase from around $1.6 billion in 1990, to reach $2.0 billion in 1995*[vi]*.*

The Commonwealth was keen to support the recommendations of the Deveson Committee but was reluctant to increase its investment in TAFE when there was a risk that the states would reduce theirs. Consequently, in 1992, the Commonwealth indicated that it would provide an extra $100 million for TAFE but, in the context of broader options to rationalise Commonwealth/state responsibilities, proposed that the Commonwealth take over full responsibility for funding TAFE while leaving the states responsible for managing their TAFE systems.

## The first ANTA Agreement (1992 – 1996)

After protracted negotiations, and despite strong support from the Victorian Government, the Commonwealth failed to get a sufficient number of states to agree that it should take over responsibility for TAFE funding.

As an alternative, in 1992 the Council of Australian Governments (COAG) formally agreed to establish a national VET system through a formal intergovernmental agreement (the ANTA Agreement). Under the ANTA Agreement, the states retained their responsibilities for managing and funding VET provision in each state. To secure ongoing growth in VET – while guarding against cost shifting by the states – the Commonwealth agreed to increase its expenditure on VET by a further $70 million per year for three years (on top of the $100 million provided in 1992). Commonwealth funding was also indexed to reflect cost increases. The Commonwealth also maintained its TAFE capital works program. The states agreed to maintain their expenditure on VET in the first year of the agreement, and outputs thereafter.

The Agreement established the Australian National Training Authority (ANTA), which independently oversaw the development of the national system and ensured that the terms of the Agreement were met. ANTA reported to a Ministerial Council, chaired by the Commonwealth Minister. In broad terms, under the ANTA Agreement the states met two-thirds and the Commonwealth one-third of the cost of VET provision in each state. An annual agreement based on projected enrolments and expenditure was entered into between each state and ANTA. These agreements were developed through ANTA and approved by the ANTA Ministerial Council, on the advice of ANTA. Commonwealth funds could not flow to the states without this approval. Commonwealth growth funding was allocated to the states on a population-share basis, with some adjustment for states facing high levels of population growth.

Under the formal requirements of the ANTA Agreement, it was intended that the states would transfer their VET funding to ANTA to be pooled with Commonwealth funding and then allocated back to each state to fund an agreed profile of activity. This provision highlighted the concern in the Commonwealth that the states not substitute Commonwealth funding for state VET funding. However, this was not seen as either sensible or practical by the states. ANTA recommended, and the subsequent Review of the ANTA Agreement supported, an alternative that would see the states establish specific bank accounts to hold state and Commonwealth funding – but this arrangement was not consistently implemented either. However, ANTA closely monitored state compliance with the terms of the funding agreement.

The Commonwealth retained some of its own VET programs including support for apprenticeships and traineeships. ANTA administered a number of these programs (including the TAFE capital works program) and others were administered by the relevant Commonwealth Department. The Commonwealth also continued to separately administer a range of labour market programs including some that overlapped with the VET system. These programs operated outside of the ANTA and state administrative arrangements and included, in 1994, the establishment of the National Employment and Training Taskforce (NETTFORCE) a major initiative which was designed to expand and improve the uptake of apprenticeships and traineeships through industry and community-based 'training companies'.

The NETTFORCE initiative highlighted the willingness of the Commonwealth to act outside of the formal processes of Commonwealth/state decision making and administration when it felt it could secure better outcomes by investing in, and establishing its own, administrative arrangements in VET. While this led to some tensions between ANTA and state training systems on one hand, and the Commonwealth on the other, funding for additional apprenticeships and traineeships flowing from NETTFORCE's activities were eventually accommodated within the ANTA funding arrangements.

Prior to the 1996 Federal election the Commonwealth also committed to a $70 million extension to growth funding for 1996 and 1997.

The ANTA Agreement was formally reviewed in 1996.

The Report of the Review of the ANTA Agreement (Taylor Review) concluded that:

> *The addition of Commonwealth growth funding through its initial injection of $100 million in 1992 and subsequent annual increases of $70 million per annum in the years 1993 to 1996 has increased in real terms the amount of recurrent funding available for VET. Real term recurrent funding, from Commonwealth and State/Territory Governments combined, grew by 14 per cent between 1991 and 1994 and is likely to grow by a further 6 per cent between 1994 and 1996.*
>
> *At the same time activity increased significantly. Student contact hours grew by 22 per cent between 1991 and 1994 (enrolments by 18 per cent). Between 1994 and 1996 student contact hours are expected to grow by a further 9 per cent[vii].*

The ANTA Agreement therefore served its initial and primary purpose. The key elements of the national VET system – national recognition of VET providers and qualifications – were put in place. Participation levels in the system grew steadily as both levels of government in each state and territory increased their share of investment in VET.

However, the Taylor Review anticipated an emerging tension inherent in the Agreement where the states could reduce their expenditure and maintain or increase their outputs; while the Commonwealth was expected to at least maintain or, in the states view, preferably continue to increase its expenditure.

As the Review pointed:

> *The system of shared funding and resource allocation must be sustainable over time, including when there are no (or limited) Commonwealth growth funds and State/Territories wish to consider utilising efficiencies in their VET systems to reduce their VET funding as a contribution to overall budget savings. Arrangements to share efficiency gains between the parties may then need to be more explicit. A move to negotiated shares of recurrent funding between States/Territories and the Commonwealth may then be appropriate[viii].*

## Renewals of the ANTA Agreement (1997 – 2004)

As the Taylor Review anticipated, after the initial injection of Commonwealth growth funding, the renewal of the ANTA Agreement every three years became increasingly problematic, particularly when the Commonwealth did not commit to any further growth in funding.

These tensions were first evident in 1997, when the Commonwealth announced a $20 million funding reduction in funding to the states through the ANTA Agreement (relative to 1997 levels) to take effect in 1998. These savings reflected the broader budget savings measures introduced by the Howard Government in the 1996 federal budget.

The Commonwealth guaranteed funding at the reduced level in real terms for the five years from 1998 but to drive further growth in the system set a ‘growth through efficiency’ target for the states to increase enrolments by 500,000 – this was to be achieved through bilateral agreements negotiated through ANTA.

The states strongly objected to these measures but in May 1997 eventually agreed to a second ANTA Agreement.

The Commonwealth also used the ANTA policy and funding framework to develop and implement its New Apprenticeship policy. This policy further extended the coverage of and participation in apprenticeships and traineeships already underway through the NETTFORCE initiative and saw rapid increase in apprenticeship and traineeship intakes, fuelled in part by liberalising eligibility for access to funding and employer incentives.

While the Commonwealth share of VET funding through the second 1997 ANTA Agreement declined, the states’ share increased over the period of the Agreement. However, the Commonwealth’s expenditure on its own programs outside of ANTA grew rapidly, particularly through employer incentives associated with the New Apprenticeships initiative[ix].

This signalled a continuing preference for the Commonwealth government to achieve some specific policy objectives by directing its additional investment in VET outside of the ANTA Agreement.

A third ANTA Agreement was reached at the end of 2001. Under the 2001 ANTA Agreement the Commonwealth maintained its 2000 base funding in real terms, and provided for cumulative of growth funding of $50 million in 2001, $76 million in 2002 and $104 million in 2003 (relative to the 2000 base). This additional funding was contingent on the states/territories meeting the Commonwealth's growth funding on a 'dollar for dollar' basis[x], reinstating a financial input requirement.

## Abolition of ANTA (2004)

In the 2003-04 budget context the Commonwealth proposed a new ANTA Agreement under which the Commonwealth would maintain its level of base funding and the growth funding allocated in the past three years as well as additional funding for mature age workers and people with disabilities. However, the Commonwealth again made its additional funding conditional on matching funding by the states (including for the first time indexation) and on specific policy reforms.

When the states failed to agree to these requirements, the Commonwealth withdrew its offer and rolled the 2003 funding levels over for 2004. It then itself competitively tendered out the additional funding it had offered[xi] the states.

Finally, in 2004, without consultation with the states, the Commonwealth government announced that ANTA was to be abolished and its functions transferred to the Commonwealth. This decision was part of a general rationalisation of Commonwealth statutory authorities. But in the case of vocational education and training, a further objective of the Commonwealth may have been to gain direct influence over VET policy and outcomes through direct government-to-government negotiations and agreements with the states and by direct funding and policy interventions.

The growing recourse to direct interventions was highlighted by the Howard Government's announcement in the 2004 election campaign that it would establish 24 Australian Technical Colleges (ATCs) as schools running VET programs outside of the state VET (and schools) sectors and that it would establish an Institute of Trade Skills Excellence to identify high quality and industry preferred training providers outside of the established VET provider accreditation and quality assurance system.

## Skilling Australia's Workforce Act (2005 – 2007)

The Skilling Australia's Workforce Act 2005 gave effect to the abolition of ANTA while preserving broad federalist architecture of the ANTA Agreement, through the ongoing role of the VET Ministerial Council and continuation of the shared VET funding framework. The Commonwealth's own policy objectives were embedded in the Act, which also provided the Commonwealth Minister with more direct powers in relation to Commonwealth funding.

The states were required to continue to report financial expenditure on VET and to maintain outputs, but without strict financial input requirements.

Commonwealth funding outside of the shared funding agreement continued to grow through a range of programs, principally to support the apprenticeship system and also to establish the ATCs and the Institute of Trade Skills Excellence.

As a further extension of direct Commonwealth funding in 2007 the Commonwealth directly funded two new programs: 30,000 work skills vouchers to assist those aged over 25 to gain year 12 or equivalent qualifications; and 6000 $500 vouchers for apprentices to obtain business related skills. These programs required the Commonwealth to establish its own purchasing system for providers wishing to participate in them, and further reinforced the tendency of the Commonwealth to directly fund new initiatives outside of the shared funding framework with the states.

## National Agreements and National Partnership Agreements (2008 – 2016)

In 2008, following the election of the Rudd Labor Government the Commonwealth and the state/territory governments established a new Intergovernmental Agreement on Federal Financial Relations (IGAFFR).

The purpose of the Agreement was to clarify responsibility for service delivery in areas of joint Commonwealth and state funding, improve accountability and focus on outcomes[xii].

Under the Agreement, Commonwealth payments to the state/territories could include:

- Specific Purpose Payments which could include National Agreements in areas of specific service delivery
- National Partnership Agreements to support specific outputs or projects to deliver agreed reforms or for incentive payments to the states when reform was achieved.

Importantly neither payment could impose financial or other input controls on the states and territories.

Under the IGAFFR the Commonwealth and states entered into a National Agreement for Skills and Workforce Development in 2008 (2008 NASWD). This Agreement marked a return to a collaborative and shared model for national VET policy and funding (the working party for the development of this Agreement was chaired by a senior state official).

Consistent with the ANTA Agreement, the NASWD outlined the shared Commonwealth/state policy objectives for VET with a strong focus on improving workforce skills levels. A central objective of the 2008 National Agreement was, by 2020, to halve the proportion of working age Australians without Certificate III and above, and to double the number of higher level qualifications.

Despite these national targets under the NASWD the states were only required to maintain enrolments and completions at 2009 levels between 2009 and 2012 with no financial input requirements (which was consistent with the IGAFFR). The Commonwealth agreed 'to provide funding contributions to states and territories to support their training systems', but the states were only required to 'determine resource allocation within their state' and to 'oversee expenditure of public funding on training within their state'[xiii]. Under the 2008 NASWD the Commonwealth committed to maintain its base expenditure on VET (plus indexation) but rolled some of its separate VET funding programs into the NASWD.

In 2008 the Commonwealth entered into a separate but complementary National Partnership Agreement (NPA) on Productivity Places Program (2008 NPAPPP) with the states[xiv].

This policy had been announced by the Australian Labor Party in its 2007 election campaign to fund industry-based training on a co-contribution basis between the Commonwealth (50 per cent); the states (40 per cent); and employers (10 per cent). In its initial conception, the Productivity Places Program (PPP) was to operate outside of the existing Commonwealth/state funding agreement with places to be determined by the Commonwealth on industry advice. Unsurprisingly, the states rejected this approach as the program conflicted with the principles of the new federal financing framework and required them to jointly fund VET places in areas where they had no control.

To quickly implement the PPP, the Commonwealth directly funded and administered the program in 2008 while the new arrangements for VET funding were under negotiation. It then entered into the NPAPPP at the end of 2008 with all states except Victoria (which negotiated for its share of the PPP funding to be rolled into a separate Partnership Agreement without the requirements placed on the other states, as Victoria had committed to a demand-driven student entitlement funding model).

The NPAPPP in effect provided additional funding to help the states meet the targets outlined in the 2008 National Agreement. Notwithstanding the requirements of the IGAFFR, under the NPAPPP the states (except Victoria) were required to provide 40 per cent of the costs of an enrolment with detailed agreements and state implementation setting out enrolment targets for each state and funding shares between the Commonwealth, the states and enterprises. However additional funding allocated through the NPAPPP was time limited and unlike earlier growth funding commitments by the Commonwealth under the ANTA Agreements not included in the VET funding base. As a consequence, funding under the NPAPPP has already ceased.

COAG also agreed to a 2009 National Partnership Agreement on TAFE Fee Waivers for Childcare Qualifications under which the Commonwealth compensated the states for revenues forgone to implement the previous Labor Government's election commitment to abolish fees for childcare courses.

The NASWD was renewed in 2012. In 2012 the Commonwealth and the states also entered into a separate National Partnership Agreement on Skills Reform (2012 NPASR). Through the NPASR, $1.7 billion of additional funding was scheduled to flow to the states and territories during 2012-17 funded in part by a redirection of funding from the NPAPPP. Funding to the states was contingent on the states' commitment to, and implementation of, agreed skills reforms and their commitment to meeting completion targets set by the states and agreed with the Commonwealth Sixty-five per cent of additional Commonwealth funding was linked to the implementation of skills reforms, including access to a national training entitlement for eligible groups and access to an expanded system of income contingent loans through VET FEE-HELP and 35 per cent of funding for the achievement of agreed outcome targets set at a state level[xv].

However, when the NPASR ceases in 2016/17, Commonwealth funding to the states for VET delivery will fall by nearly $500 million in 2017-18 based on forward estimates in the 2015-16 Commonwealth budget, with ongoing VET funding to the states provided only through the NASWD[xvi].

## Other Commonwealth programs (2007 – 2016)

In addition to increased outlays through the national agreements, the Commonwealth also significantly increased expenditure on its own VET programs over the period of the agreements, as set out below.

### VET FEE-HELP

As noted in the introduction, debate and media coverage about VET funding in 2015 was dominated by growing evidence of inappropriate practices by some VET FEE-HELP providers. However in the context of the broad analysis of VET funding in this paper it is important to note that while VET FEE-HELP is not a source of funding for most VET providers or VET students.

VET FEE-HELP outlays have primarily flowed only to a relatively small number of Registered Training Organisations (RTOs), with six providers accounting for 50 per cent of outlays and 207 providers accounting for the balance. The majority of Australia's 1800 RTOs that received public funding do not rely on this scheme as a revenue source. VET FEE-HELP is also not available at Certificate I-III levels. VET FEE-HELP was available on a trial basis for some Certificate IV qualifications but will not be available in the future[1].

VET FEE-HELP was first introduced by the Howard Government in 2007 to provide for equity of treatment for students in full-fee VET Diploma and Advanced Diploma programs with students in full-fee higher education programs. However, the availability of VET FEE-HELP was initially highly constrained as providers needed to have in place a credit transfer agreement with a higher education institution; in effect VET FEE HELP was only available for VET courses with higher education articulation pathways in place.

In the NPASR, the Commonwealth also agreed to extend VET FEE-HELP to subsidised VET Diplomas and Advanced Diplomas, for eligible providers. VET FEE-HELP was initially extended to Victorian providers in 2009 to assist with the implementation of that state's Victorian Training Guarantee in relation to both the state-subsidised courses and non-subsidised courses where fees were not regulated by the state.

VET FEE-HELP was extended to state-subsidised and non-fee-regulated courses in other states as they committed to VET reforms under the NPASR. Following an early review of VET FEE-HELP, the requirements for a VET FEE-HELP provider to have in place a credit transfer agreement with a university was removed. This made it far easier for new providers to be registered for VET FEE-HELP and for existing providers to expand their offerings under VET FEE-HELP. VET FEE-HELP pilots for Certificate IV programs were also established with the states on a limited basis.

For state-subsidised courses, fee benchmarks were agreed with the states of $4000 in 2010 and $5000 in 2011. The states also agreed to share in the costs of borrowings and 'impairment' resulting from any student non-repayment of debt as a result of the extension of VET FEE-HELP. However, these prudential and cost sharing measures were not required for non-subsidised and non-fee regulated VET FEE-HELP programs. Unsurprisingly, it has been in this area that there has been dramatic growth in VET FEE-HELP and most evidence of excessive fees and unethical provider behaviour as provider owners and investors bear little or risk from the consequences of these practices.

The Commonwealth Department of Education and Training statistical summary report released in 2015 highlights the rapid growth in VET FEE-HELP:

- *The number of students eligible for VET FEE-HELP increased by 90 per cent between 2013 and 2014, from around 123,000 to approximately 234,100.*
- *The number of students accessing VET FEE-HELP loans increased by around 103 per cent between 2013 and 2014, from just over 100,000 students to nearly 202,800.*
- *The total value of VET FEE-HELP loans accessed in 2014 ($1757 million) was more than double the amount accessed in 2013 ($699 million).*
- *Since VET FEE-HELP was first made available to students in 2009, a total of $3.1 billion in VET FEE-HELP loans has been accessed by VET students.*
- *As at 31 December 2014, there were 254 providers approved to offer VET FEE-HELP[xvii].*

The explanatory memorandum on amendments to the legislation governing VET FEE-HELP noted that while some of this growth could be explained by a demand-driven scheme in an area previously unassisted by government, some of the growth derives from 'the unscrupulous or opportunistic behaviour of some providers and their agents' with characteristics including 'aggressive marketing, inappropriate targeting of vulnerable people, and widespread use of inducements'[xviii].

To address these inappropriate practices, in 2015 the Commonwealth government introduced a range of measures to protect students' interests[xix]. The Commonwealth capped loan levels for individual providers at 2015 levels, and announced a review of the VET FEE-HELP policy settings.

It is expected VET FEE-HELP payments will fall as a consequence of measures introduced by the Commonwealth. The effectiveness of the measures to protect students and restrain expenditure has yet to be tested, however anecdotal evidence suggests that they are having a significant effect on at least some providers.

VET FEE-HELP and its extension were important reforms. VET FEE-HELP provides equity of treatment for VET students with higher education students by ensuring they can access income contingent loans with no requirement to pay upfront fees. This is an important provision for VET students because even regulated fees in subsidised courses have increased significantly in recent years.

**VET FEE-HELP as a revenue source**

VET FEE-HELP revenue should in theory be regarded as student contributions with the annual cost to government reflected in the cost of interest subsidies and provision for 'impairment' rather than a Commonwealth outlay.

However, VET FEE-HELP is a source of immediate and direct revenue for providers who share none of the risks or costs of debt repayment. Modelling undertaken by Chapman and Higgins for the Mitchell Institute highlights the relationship between fee levels and effective subsidy levels for individuals (and providers)[xx]. These subsidies comprise the difference between the CPI rate and the long-term government bond rate (as the government has to borrow at higher interest levels than the level at which student debt is indexed) and the amount of debt not repaid. As Chapman and Higgins demonstrate, higher fee levels result in higher effective subsidy levels.

Where excessive fees have been charged, and inappropriate enrolments undertaken, Commonwealth payments to VET FEE-HELP providers are never likely to be repaid, representing a 100 per cent course subsidy from the Commonwealth to the provider.

However, even where enrolment and delivery practices are of high quality, public subsidies through FEE-HELP flow to providers if fee levels are well in excess of rates of return. This issue should be central to the review of VET FEE-HELP recently announced by the Commonwealth.

### Capital funding

The Commonwealth also provided over $500 million in capital funding to VET providers through the states and territories as part of its major investment in capital across the education sectors. This capital funding flowed from the Education Investment Fund established by the Howard Government and from the 2008 and 2009 stimulus packages following the Global Financial Crisis.

### National Workforce Development Fund and Industry Skills Fund

The Commonwealth also established and provided $500 million in funding for five years for the National Workforce Development Fund (NWDF) on a co-contribution basis with employers outside of the partnerships agreements, giving effect to the original intention and design of the Productivity Places Program. Funding under the NWDF flowed to VET providers with some states actively facilitating projects for NWDF funding and with Industry Skills Councils acting as brokers. Outcomes funded under the NWDF could be counted towards outcomes targets under the NPASR.

This fund was abolished in the 2014 federal budget and has been replaced by a more limited and targeted Industry Skills Fund.

### Recent decisions

The 2014 budget also saw a reduction in funding for a range of the Commonwealth's own VET programs and the establishment of a Trade Support Loans scheme as an income contingent loan scheme for apprentices which, in selected areas, replaced the former Tools for Your Trade Payment for apprentices.

The recent December 2015 Mid-Year Economic and Fiscal Outlook (MYEFO) has seen further reductions in funding for the Industry Skills Fund, and the Skills for Education and Employment program (which was designed to provide language literacy and numeracy training for the unemployed).

## Funding trends and their impacts

The analysis below takes historical perspective from the commencement of Commonwealth growth funding in 1991 across the different Commonwealth/state agreements. It considers in more detail the impact of the National Partnership Agreements since 2008 as they constitute the current framework for public funding of VET.

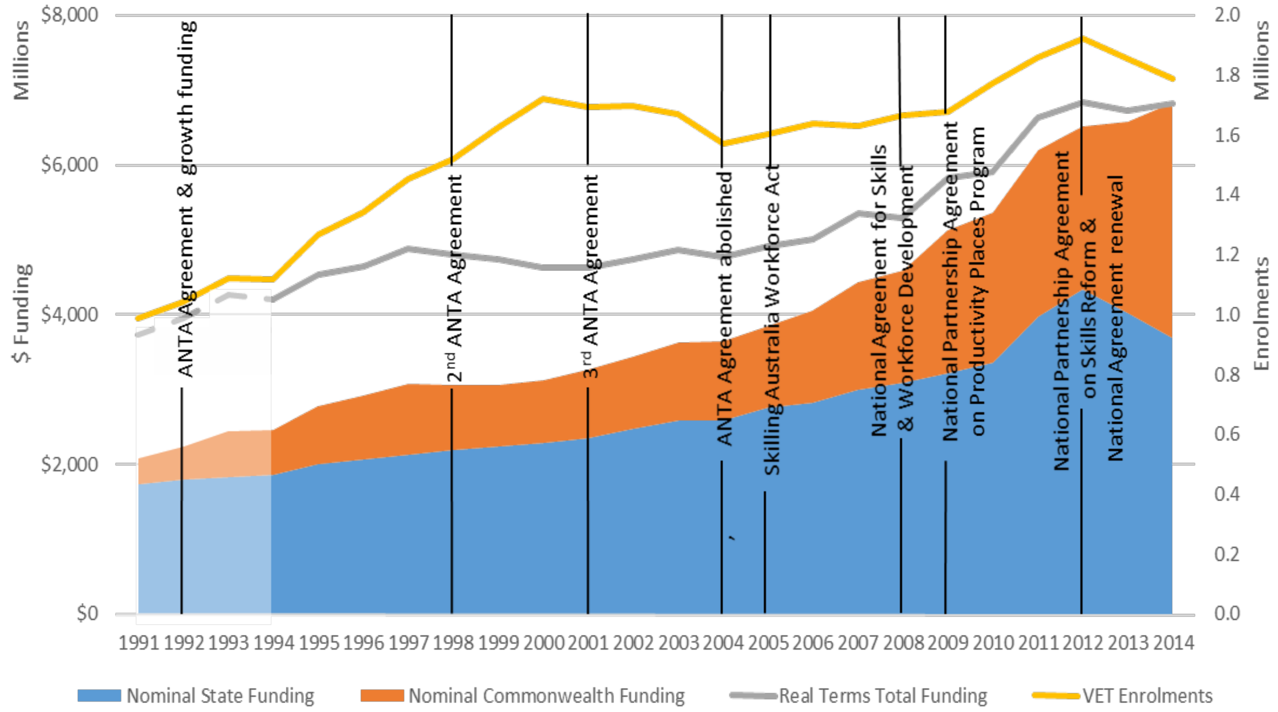
Funding trends between the VET and higher education sectors over the past decade are also analysed for comparative purposes.

### Commonwealth/state agreements 1991 – 2014

Figure 1 below maps the different agreements and major Commonwealth programs against:

- Change in overall levels of VET funding by governments in real and nominal terms between 1991 – 2014.
- Changes in the share of Commonwealth and state funding between 1991 – 2014 (Commonwealth funding includes funding allocated through the different Commonwealth/state agreements and the Commonwealth's own programs including total VET FEE-HELP payments to providers).
- Changes in VET enrolments between 1991 – 2014[1].

**Figure 1: VET funding and enrolment trends 1991-2004**




Source: ACIL Allen Consulting

*1 This figure has been prepared using NCVER enrolment data for the period 1991 – 1994 and NCVER Finance Data for the period from 1997 – 2014. Finance data for the period 1991 -1994 was sourced from the 1996 Review of the ANTA Agreement. It is recognised that finance data over this period may have been collected and reported on a different basis and should not be interpreted as representing precise levels of government expenditure in any one year or on a linear basis. Rather it shows broad trends in expenditure and shares of expenditure. The data includes Commonwealth outlays to non-government providers under VET FEE-HELP but does not include outlays to government providers which is reported as fees and charges in the NCVER finance report. This reporting issue is under discussion with NCVER. It is also recognised that the use of enrolments represents only a proxy for activity levels in VET due to variable course lengths, the potential for individuals to be enrolled in more than one course and provider, changes in course types and levels and improvement in the reporting of enrolments over time.*

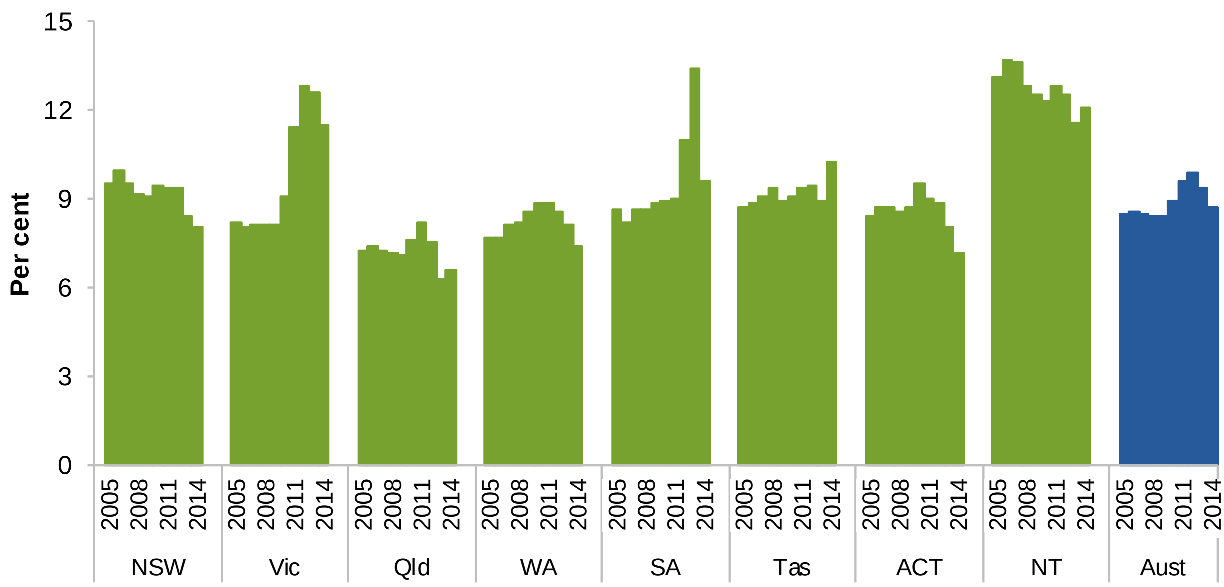
Figure 1 shows that:

- Real terms VET expenditure falls into four broad phases:
    - the initial phase of growth funding under the ANTA Agreement (1991-97);
    - a period of static funding (1997-2006);
    - further growth in funding (2007 -2012); and
    - a further period of static funding where increases in Commonwealth outlays have offset declines in state outlays (2012- 2014).
- Publicly subsidised enrolments are ultimately driven by public funding levels and as such the pattern of VET enrolments broadly follows the four expenditure phases.
    - The exception to this is the period of reported enrolment growth between 1998 - 2001 when expenditure levelled off but enrolments increased significantly. This may be explained by improved state reporting and real efficiency improvements, substantial growth in 'New Apprenticeships' fuelled in part by broadening of eligibility for Commonwealth employer incentives and the 'pipeline' effect of enrolment growth as the overall capacity of the system expanded.
- Publicly funded VET enrolments are only 200,000, or 13 per cent, higher than they were 10 years ago and have trended down since 2012.
    - This compares to undergraduate enrolments which have risen 43 per cent over the same period and which continue to rise.
- The Commonwealth's share of public VET funding has grown significantly since 1991 when growth funding commenced.

## VET participation rates

Figure 2 is taken from the 2016 Report on Government Services by the Productivity Commission. It highlights changes in participation rates for 15-64 year olds in publicly funded VET from 2005-2014[2].

**Figure 2: VET participation rates 2005 – 2014**




Source: Report on Government Services 2016 Productivity Commission

[2] Territory participation rates were included in the Report of Government Services 2016

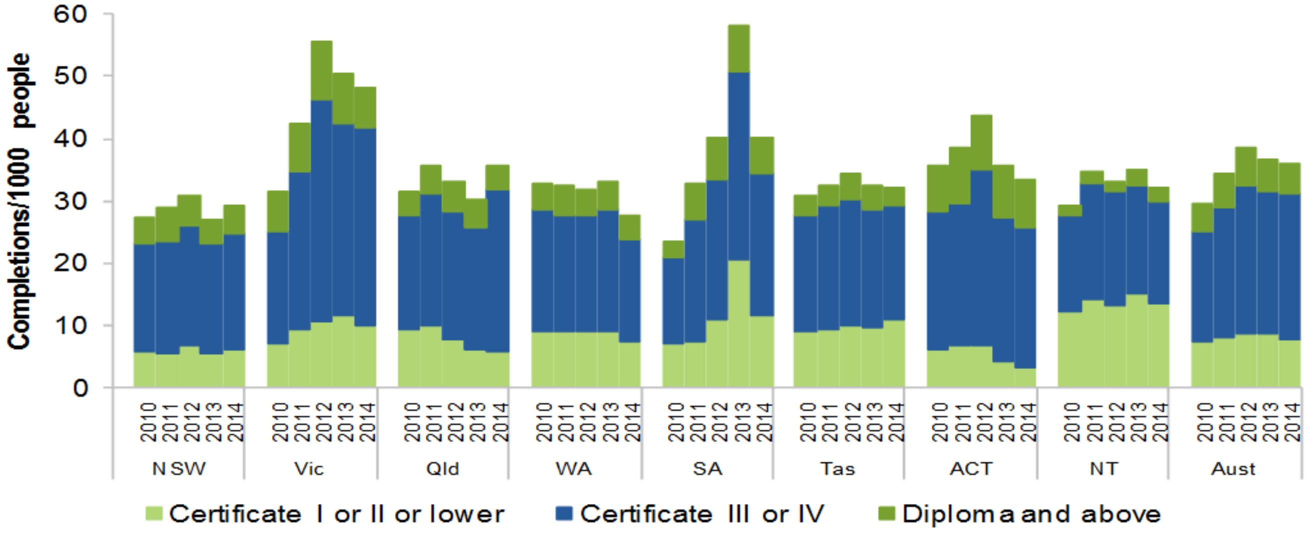
Figure 2 broadly reflects the pattern of public expenditure and enrolments from 2005 outlined in Figure 1 with increases in participation between 2008-11 not sustained and participation rates in VET now in decline in all jurisdictions and nationally.

There are also major differences in participation levels between jurisdictions which cannot be explained by labour force or demographic factors; for example, between NSW and Victoria.

## Qualification completion rates

Figure 3 is also taken from the 2016 Report on Government Services. It shows the number of VET qualifications completed per 1000 people from 2010 to 2014.

**Figure 3: Qualifications completed by all students aged 15–64 years, per 1000 people**




Source: Review of Government Services 2016

The major changes in participation levels between jurisdictions is also reflected in qualification completion levels between jurisdictions and in the level of qualifications between jurisdictions that cannot be explained by labour market or demographic factors – for example the incidence of Diploma and above qualifications in Victoria compared to NSW and the incidence of Certificate II and lower qualifications in South Australia compared to Queensland.

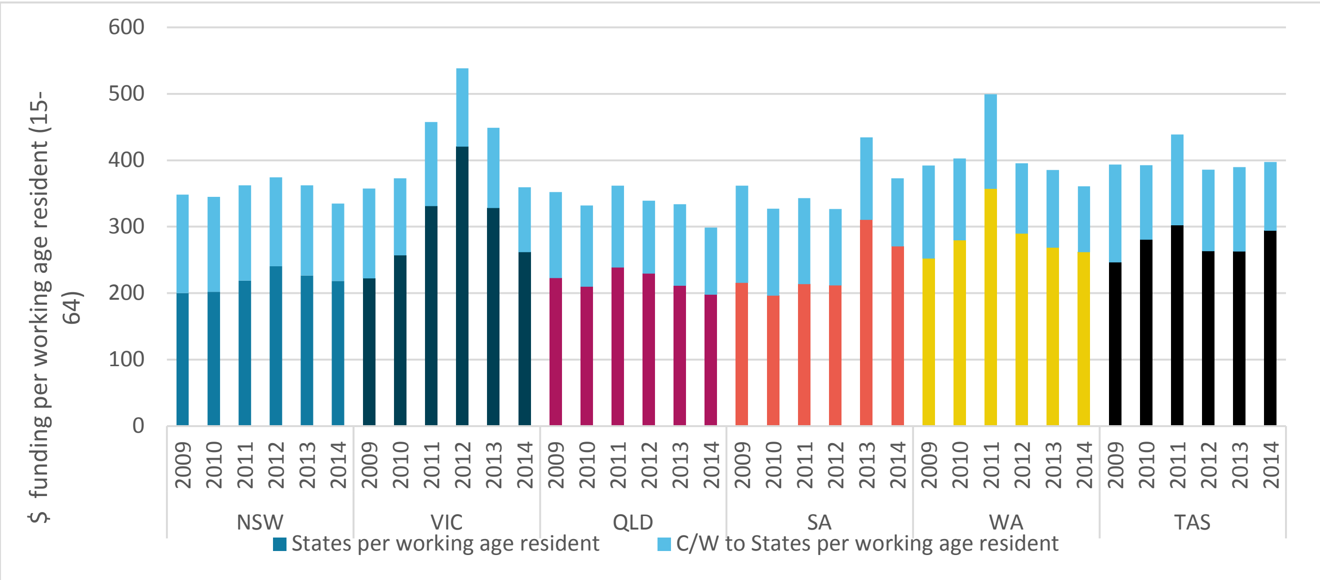
## National agreements funding levels and shares 2009 – 14

Figure 4 shows total government VET funding under the various national agreements by jurisdiction from 2009 – 2014 (excluding fees and charges and VET FEE-HELP)[3].

For comparative purposes, Figure 4 shows public VET expenditure calculated on the basis of funding per working age resident, recognising that this is at best a broad benchmark and that there is no necessary 'right' funding level for VET (given variations in state labour markets, industry composition, population growth, age profiles school retention rates and participation levels in higher education).

[3] There is a reduction in Commonwealth funding to the states in 2014 however this reflects the timing of payments under the NPASR

**Figure 4: VET funding levels and shares by jurisdiction 2009-14** [4]




Source: ACIL Allen Consulting VET Finance 2014 NCVER

Figure 4 shows:

- That State funding is now falling in absolute terms and in proportional terms relative to Commonwealth expenditure per working age resident.
- The general increase in state funding 2010 and 2012 shown in Figure 1 masks substantial variations in funding between the states with most of the increase in state funding in those years accounted for by Victoria and to a lesser extent South Australia.
- This is consistent with the major variations in participation levels and qualification completions between the states.
- Relative funding shares between the Commonwealth and the states vary significantly between jurisdictions.

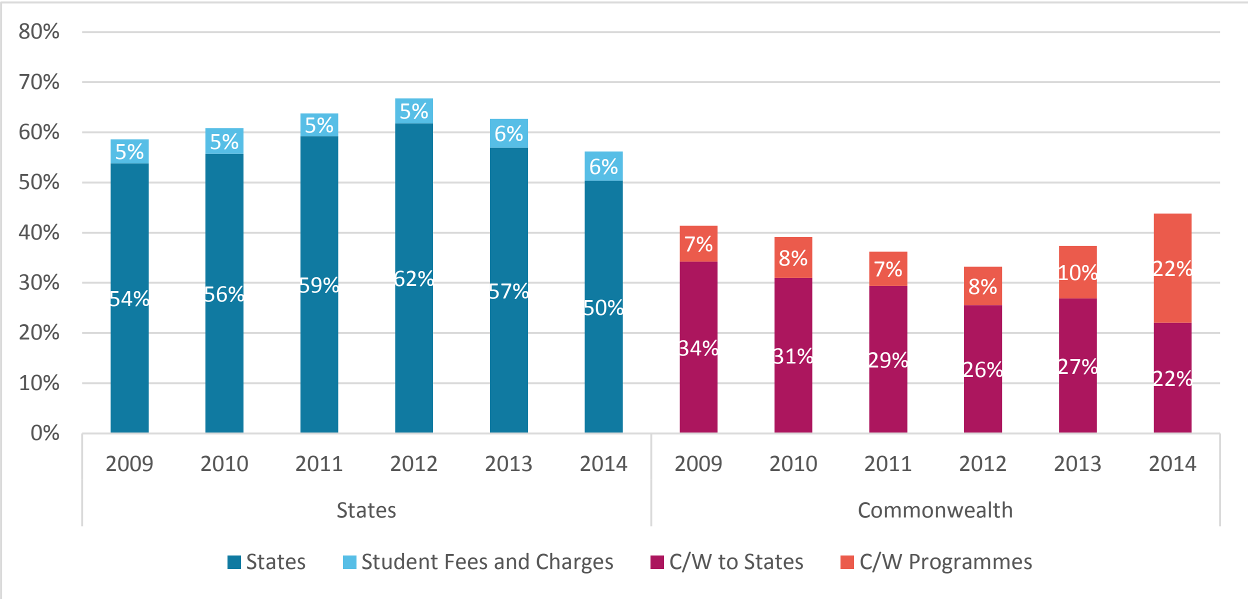
## Commonwealth/state funding shares 2009 – 14

Figure 5 shows the share of total VET funding by the Commonwealth and state governments and also student fees for subsidised courses (as these form part of the price paid by the states). Since 2009 Commonwealth programs include VET FEE-HELP outlays to private providers. Student fees and charges are included in VET FEE-HELP payments to public providers[5].

[4] The territories have been excluded from this analysis due to the extreme differences in population and geographic size and in the case of the Northern Territory cost.

[5] Fees and charges may be understated as fees charged by private providers for subsidised courses are not collected and VET FEE-HELP revenue for public providers may not be fully recognised in the year in which students enrolled.

**Figure 5: VET funding shares by major source 2009-2014**




Source: ACIL Allen Consulting VET Finance 2014 NCVER

Figure 5 shows:

- In 2014, Commonwealth funding for VET including VET FEE-HELP was 44 per cent of total VET funding and will exceed 50 per cent of total funding in 2015 (noting that a proportion of VET FEE-HELP revenue will be repaid by students in subsequent years).
- The Commonwealth share would be even higher if expenditure was included for areas such as employer incentives for apprenticeship and the national apprenticeship support centres ($635 million in 2015-16).
- However, the Commonwealth share may decline based on current forward estimates and reductions in VET FEE-HELP.

### Efficiency

In the past, VET participation and enrolments have increased through improved efficiency, particularly in the period between 1999-2000. However, the Report on Government Services 2016 notes that:

> *Since 2005, government real recurrent VET expenditure has increased 4.1 per cent, while the number of government funded annual hours has increased 51.8 per cent. As a result, government real recurrent expenditure per annual hour has declined 31.5 per cent over the past 10 years — from $16.64 in 2005 to $11.40 in 2014 — at an average annual rate of decline of 4.1 per cent*[xxi].

## Comparative funding between the education and training sectors

### Higher education

The development and implementation of the national VET agreements analysed above overlapped with the Review of Australian Higher Education (Bradley Review). The implementation of the recommendations of the Bradley Review have underpinned significant additional funding for higher education through the introduction of uncapped, demand-driven funding for Commonwealth supported places (CSP) and between 2009 and 2013 a higher level of indexation of funding for those places.

The process of independent review and advice through the Bradley Review included modelling of future demand for tertiary education[xxii] and costing of the review's recommendations.

While recommendations to further improve funding levels flowing from the 2011 Review of Base Funding (Lomax Smith) were not implemented by the Commonwealth, decisions by the Government to impose an efficiency dividend on universities and proposals in the 2015 federal budget for a 20 per cent reduction in CSP funding (together with fee deregulation) have not passed the Senate (funding levels are specified in legislation).

At present, higher education is funded on an uncapped enrolment driven basis with funding levels set in legislation.

In the context of its recommendations for the introduction of demand-based funding for higher education, the Bradley Review identified the risk that:

> *It appears too, that some states and territories face major fiscal constraints, which may lead them to reduce their investment in VET in the near future, leading to skewed and uneven investment between the sectors over time if a demand-based funding model is adopted for higher education*[xxiii]*.*

The Bradley Review further argued that:

> *moving to a demand-based approach to funding higher education cannot be done in isolation from VET. Changing higher education funding but leaving VET funding untouched would compound existing distortions*[xxiv]*.*

The Review Panel argued that 'the case is stronger than ever for primary responsibility for regulation and funding of tertiary education to be located at the national level'[xxv] citing support from the former Queensland Premier Anna Bligh and the earlier proposals by the Hawke and Keating governments for this model.

While the Rudd and Gillard governments moved quickly to implement the Bradley Review recommendations in relation to national regulation of VET and higher education, the Review's suggestions relating to a national tertiary education funding system were overlooked.

Rather, decisions on the implementation of the demand based funding system in higher education and the student entitlement in VET (and their associated targets) proceeded through separate processes.

### Schools

As with the Bradley Review, the architecture of the future framework for schools funding including the Schooling Resources Standard (SRS) flowed from a major independent review with consequential significant stakeholder and public support. The implementation of the SRS together with the Commonwealth Government's commitment that no school would be 'worse off' drove and underpinned a major process of multi-lateral and bilateral agreements for additional funding for schools with all states except Western Australia and Queensland (with those states now receiving additional Commonwealth funding) and the non-government schools sectors.

All states have now moved, or are moving, to enrolment driven funding based around funding levels negotiated between the Commonwealth and the states and with non-government schools.

While differences remain between the Federal government and national opposition on levels of schools funding, the arrangements beyond 2016-17 are uncertain. However, the additional funding base for schools flowing from the relevant National Partnership Agreements have continued to flow into the agreements governing schools funding, whereas in VET, additional Commonwealth and state funding resulting from the Partnership Agreements have not been built into the VET funding base.

## Assessing VET demand and costs

Unlike the major public and independent processes associated with higher education funding in 2008 and school funding in 2011-12, the development of the VET student entitlement was undertaken through the complex and confidential processes associated with the development of intergovernmental agreements (as were earlier National Partnership Agreements for schools funding).

As the architecture of the National Agreements precluded financial input requirements from the states, and decisions on the implementation of VET student entitlement was left to the states, there appears to have been no comprehensive national modelling of the costs of the implementation of the student entitlement (although modelling was undertaken in some jurisdictions).

In 2011 the Australian Workplace Productivity Authority (AWPA) undertook a comprehensive assessment of future VET resourcing needs as part its report *Skills for prosperity a roadmap for vocational education and training*[xxvi]. AWPA reported that its modelling:

> *shows the requirement for an additional $310 million per annum, accumulating, from $8286 million in 2008, so that total funding rises to an estimated $10,283 million in 2015 and to almost $12 billion in 2020. This is an average increase in funding of just on 3 per cent per annum over the period, about the same rate that funding rose in real terms from 2003 to 2008*[xxvii].

AWPA recommended that Australian governments commit to increased VET funding to these levels together with a new investment framework for VET. However, AWPA's advice does not appear to have been formally considered either by the Commonwealth or the relevant VET Ministerial Council.

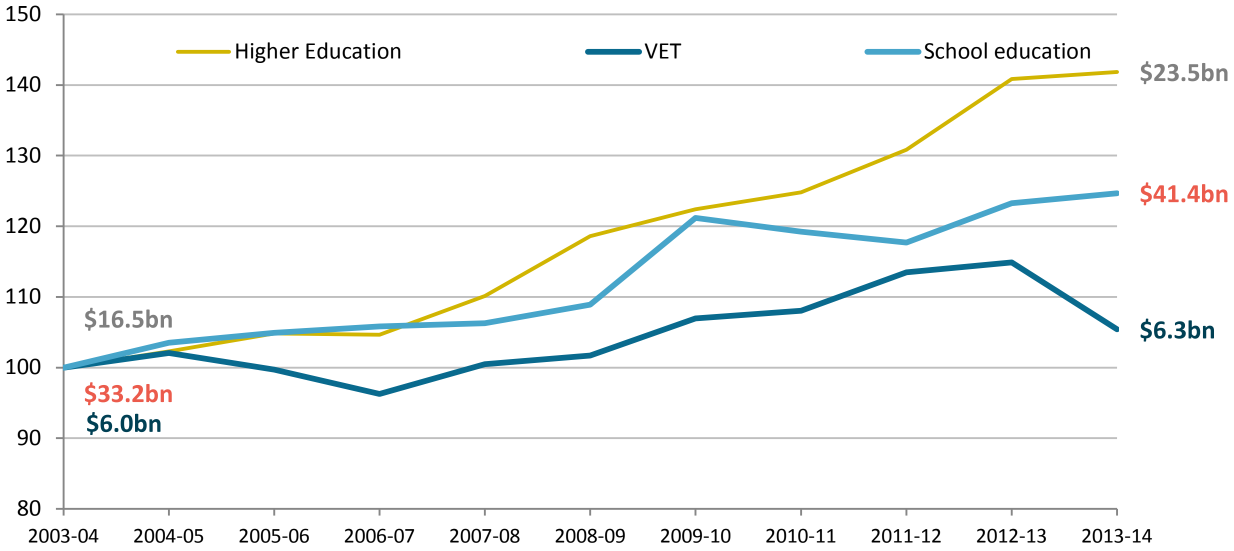
Rather, each jurisdiction undertook its own analysis of the costs of the VET entitlement commitment and balanced its capacity to implement the entitlement against available resources and competing priorities – including the emerging costs of the implementation of the Gonski recommendations and the rising costs of the demand driven higher education system.

There has not been a fully independent review of VET funding since the Deveson Report in 1991 and the independent statutory role of ANTA in advising the VET Ministerial Council on future resourcing needs was lost when ANTA was abolished in 2004 (AWPA did not have a formal advisory role in relation to the VET Ministerial Council).

### Expenditure between the sectors

Expenditure between schools, VET and higher education over the past decade can be assessed by looking at total expenditure across these sectors since 2003-04, using Australian Bureau of Statistics data as previously reported by the Mitchell Institute and replicated in Figure 6 below. Note that this data reflects total expenditure by public sector entities including by universities on research activities and not just government expenditure on courses and therefore should be considered to represent only broad trends in funding between the sectors.

**Figure 6: Expenditure by education sector 2003-04/2013-14.**




ACIL Allen Consulting analysis based on Australian Bureau of Statistics data
Note: School expenditure includes all expenditure on government schools (including private contributions) and government expenditure on non-government schools.
CAGR = Compound Average Growth Rate
Index (2003-04 = 100)

Source: Mitchell Institute Expenditure on Education and Training in Australia 2015

Figure 6 broadly illustrates the outcomes of the processes summarised above. Highly visible and independent reviews in the higher education and schools' sectors that attracted public interest, strong stakeholder support and ultimately strong government commitment have led to sustained increases in expenditure through those sectors in higher education from 2011-12 (when demand based funding was fully implemented) and in schools from 2012-14 when the progressive implementation of the outcomes of the Gonski review added to additional funding flowing from the earlier schools national partnership agreements.

In VET the absence of similar external reviews and stakeholder support combined with its traditionally lower community and political value has seen a decline in public funding.

Both universities and schools now have access to enrolment driven funding linked to per student funding rates whereas VET funding in all jurisdictions is capped with eligibility rules, subsidy and fee levels used to manage VET budgets within those caps. Indexation levels for schools and higher education have to date also been far higher than those applying to VET.

On current budget outcomes and forward estimates, the gap between expenditure on VET and expenditure on schools and higher education will widen over the next few years except for the possible short term effect of VET FEE HELP payments and revenue.

## Conclusion

It is now over 40 years since the Commonwealth began a funding partnership with the states to raise the quality and status of technical and vocational education, and 25 years since COAG first agreed to a formal shared funding agreement as an alternative to the Commonwealth assuming full responsibility for funding the emerging national VET system.

Much has been achieved through this funding partnership. However, the tensions and weaknesses inherent in a shared funding agreement have continually surfaced over the period of the agreement. These include:

- the difficulty of applying a uniform system of Commonwealth funding across multiple jurisdictions with differing budgetary needs and priorities;
- how both levels of government can benefit from reduced costs associated with increased efficiency;
- the frequent tendency of the Commonwealth to act as a direct funder outside of the agreement when it wishes to directly secure specific outcomes;
- growing differences between jurisdictions in funding and consequently participation levels and qualifications completion levels;
- growing differences between jurisdictions in funding for the same qualification and in eligibility criteria for the VET student entitlement compared to nationally consistent pricing and eligibility criteria that apply in higher education (eligibility is essentially determined by institutions and without regard to prior qualifications) [xxviii].

These weaknesses have been magnified in the nature and structure of the current national partnership agreements governing VET. Under these agreements short term improvements in VET funding, participation and qualification completions were unevenly distributed between the states and have not resulted in an ongoing and sustainable VET funding base. A further deterioration in VET funding levels is highly likely. The gap in funding between VET and the other sectors of education will widen and diminish pathways for school leavers wishing to enter VET, potentially distort choices between VET and higher education and limit opportunities for workforce retraining and upskilling.

The problem of diminishing public investment in VET is not just a function of the shared funding model. It also reflects the historical problem of the poor standing of technical and vocational education evident as far back the delayed Commonwealth national intervention in technical education relative to its early investment in universities and schools.

This is not a problem isolated to Australia. Issues associated with funding levels for the further education sector in the United Kingdom are similar to those in Australia although governed under a unitary rather than shared funding system. However, the lack of clear responsibility and accountability for VET funding in Australia and the loose nature of the current Commonwealth/state funding agreements compounds the problem of the low priority historically accorded to VET.

# Future options

## The current state of play

The issue of future responsibility for funding VET is under consideration by the Council of Australian Governments. The Commonwealth is also undertaking a consultation and review process for the redevelopment of VET FEE-HELP.

COAG's consideration of VET funding follows a thorough analysis of the current arrangements for VET funding and canvassing of options in the Commonwealth's Federation Reform Discussion Paper. In the context of broader reforms to the Australian Federation, South Australian Premier Jay Weatherill's proposed in his July 2015 National Press Club speech that the Commonwealth assume full responsibility for funding tertiary education including VET[xxix].

Premier Weatherill joins other Labor leaders who have supported the Commonwealth assuming responsibility for VET funding including former Victorian Premier Joan Kirner, Prime Ministers Hawke and Keating and former Queensland Premier Anna Bligh. The option was also recommended by the 1996 Commonwealth Commission of Audit but not considered by the Howard Government. It was suggested again by the Bradley Review but not considered by the Gillard or Rudd Governments. In its 2013 election policy the Australian Labor Party committed to direct Commonwealth funding of TAFE by redirecting funding from the states if they did not agree to maintain TAFE funding in real terms[xxx].

In his speech to the 2015 TAFE Directors Australia conference the Coalition Minister for Education and Training Simon Birmingham expressed the view that:

> *The failure to move to a unified, Commonwealth-led system in 1992 can be viewed as a missed opportunity; one which would have increased the efficiency and harmonisation of the Australian VET system*

He went on to say that

> *By placing control of all of the funding levers — the setting of fees, payment of subsidies, and lending of income-contingent loans — with one level of government, we would promote accountability in the system and could create a more effective market, driven by students rather than providers, than we've seen to date.*
>
> *We could also better link the VET system and higher education, welfare services, and employment. We would be able to provide greater equity in the way the courses are funded[xxxi].*

The peak industry bodies in Australia including the Business Council of Australia, the Australian Chamber of Commerce and Industry and Australian Industry Group; as well as the peak VET bodies including TAFE Directors Australia and the Australian Council of Private Education and Training have all in recent times expressed concern about public investment levels in VET.

A draft paper prepared by the Commonwealth for COAG proposes that it assume full funding for 'mainstream' VET qualifications by bringing together subsidies and income contingent loans (with deregulated fees) in areas of national skills priorities. Funding would be fully competitive with TAFE funded by the Commonwealth at the rate as other providers. The states would retain responsibility for ownership and management of their TAFE systems and could fund TAFE but only to the extent required to ensure 'competitive neutrality' with other providers.

The Victorian and NSW Ministers responsible for VET have strongly stated their opposition to the proposal advanced by the Commonwealth in part because of their concern about the capacity of the Commonwealth to effectively run a national VET funding system given the significant issues associated with VET FEE-HELP.

The Opposition spokesperson for VET Sharon Bird has stated her opposition to a Commonwealth takeover of VET primarily because of her concern about the treatment of TAFE under the draft paper prepared for COAG[xxxii].

Most recently, the newly appointed Minister for Vocational Education and Skills Scott Ryan while indicating that the issue was a matter for COAG indicated that his personal inclination was that a Federal takeover did not necessarily lead to better outcomes. He predicted that COAG 'would not be heading down that path'[xxxiii].

The draft COAG paper argues for a national VET funding system in terms of administrative and market efficiency including the potential for downward pressure on prices, improved quality driven by competition and competition between VET and higher education for similar courses. It also identified benefits for students and employers in not having to 'grapple with multiple funding regimes' for providers in terms of being able to operate for efficiently in multiple jurisdictions.

The draft paper makes an important contribution by proposing a more coherent funding system by linking course subsidies and income contingent loans into a single national pricing system (although the risks of fee deregulation operating with income contingent loans are not recognised as experience with VET FEE-HELP has shown).

However, the draft paper fails to address the underlying problems with the current Commonwealth\state funding model: declining overall investment in VET (with the exception of VET FEE-HELP) and increasingly uneven investment across the states and territories. Rather, the draft paper appears to open the door to further funding reductions by highlighting the potential for price competition to improve efficiency (with any efficiency dividend most likely accruing to the Commonwealth as budget savings).

The draft paper also overstates the efficiency and administrative benefits of a national funding system. Few if any students and most employers have to grapple with the different funding regimes in different states although this is a major issue for some national employers and training providers operating across two or more jurisdictions.

The more significant issue under the VET student entitlement model in terms of national consistency is the highly variable pricing and subsidy levels between the states for the same qualification and differing eligibility criteria for the VET student entitlement and the effect of these inconsistencies on participation, quality and outcomes (compared to the consistent funding regime applying to higher education).

The market based funding and deregulated fee model proposed in the paper also fails to consider the Commonwealth's own experience with VET FEE-HELP and the substantial problems experienced in some jurisdictions with demand and market based in terms of quality, pricing and budget overruns.

The VET provider system is also far more diverse and complex than when the Commonwealth proposed assuming responsibility for TAFE funding in 1991. In 1991 there were only a relatively small number of individual TAFE institutions (mainly in Victoria) operating as statutory entities that would have been directly funded by the Commonwealth. Most TAFE institutions would have been funded through 'head offices' as part of statewide TAFE systems. Regardless of their governance TAFE funding was allocated through highly centralised and prescriptive funding agreements based in the main on planned delivery and funding levels. There were also a relatively small number of non-government providers mainly operating in traineeship delivery or through contracted provision in defined areas in some states.

While there is an evident trend in most states towards rationalisation of TAFE institutions into single statewide providers or towards statewide systems there are now 1800 VET providers receiving VET funding with significant differences in size, scope of registration, delivery models, ownership and governance model and levels of reliance on public funding. Funded enrolments have almost doubled and accredited courses have extended into additional industries and occupations.

This transformation of the VET provider system poses formidable challenges and risks in the development of a national VET funding system particularly if that system was to operate on a market basis.

There are also substantial and complex transitional issues to be considered including the shift from one funding, contractual and accountability system to another and the need to ensure continuity of provision to continuing students and certainty about future offerings and pricing for providers and intending students.

The states will be particularly sensitive to the risk of having to continue to maintain funding for TAFE to ensure its ongoing role as the public VET provider and having to deal with the potential consequences of poor design and oversight of the VET market in terms of meeting skills needs in state, regional and local labour markets. VET is also more the loss of their capacity to address statewide as well as local and regional skills needs in the move to a national funding system - particularly one substantially based on nationally determined market settings.

States currently providing higher levels of funding per working age population are not likely to agree to a national system that would result in their higher funding level being transferred to the Commonwealth and then reallocated to other states using the current population share distribution formula.

The difficulty of obtaining agreement by all of the states and territories to a new and untried funding system may preclude agreement to a fully Commonwealth based scheme – as has occurred with Victoria and Western Australia maintaining state-based VET regulators.

Finally, the draft paper deals with VET as a discrete market rather than considering the interface between VET and higher education and the effect of uncapped demand driven funding in higher education and capped and increasingly constrained VET funding

The draft paper itself does not provide a sufficiently compelling policy rationale for the states to withdraw from VET funding. Nor does it provide a sufficiently detailed explanation of how a nationally funded system would work and how the complex transitional arrangements might be addressed.

The worst outcome for VET would be an impasse at COAG and a default to the current flawed funding model. The case for a decisive move towards a national VET funding system is as compelling now than when it has been raised in the past.  Its a logical extension of the national regulation of VET and the growth in the role of the Commonwealth's funding.

The threshold issue is whether a national VET funding system is synonymous with a Commonwealth funding system with the states withdrawing from VET funding all together (as in higher education) or whether a national funding system can retain an ongoing role for the states but through a different shared funding model which has regard to and addresses the weaknesses in the current model.

## A way forward

The following steps are suggested as a process to guide future government decisions on funding responsibility for VET.

1. Develop a forward-looking view about the nature of the VET system required by Australia in the 21st century as a highly innovative and adaptive economy and society.
2. Develop a clear understanding of the provider system required to deliver those outcomes – including the future role of TAFE as the public provider – and the role of other agencies including the national VET regulator.
3. Undertake a national assessment of future participation and resourcing requirements for VET with a primary focus on the need to ensure that all young people have access to tertiary education across higher education and VET.
4. Agree on the range of qualifications that should be funded under a national VET system.
5. Develop a funding model for those qualifications by setting:
   i. an efficient or benchmark price for each qualification;
   ii. the balance between public and private contributions (to make up the total price).
6. Redesign VET FEE-HELP to extend it to all nationally funded VET qualifications while ensuring that the scheme is sustainable – including options for providers to help meet the costs of income contingent loans.
7. Determine the respective roles of the Commonwealth and the states. Options include:
   a. The Commonwealth could fully fund the course subsidy and meet the costs of income contingent loans (the costs of borrowings and unpaid debt).
   b. The Commonwealth and each state and territory jointly fund the course subsidy and meet the costs of VET FEE-HELP.
   c. The Commonwealth and the states could agree to each fund specific qualifications – for example the Commonwealth could fully fund Diplomas and Advanced Diplomas to ensure a consistent approach across VET and higher education – and fully meet the costs of income contingent loans for the qualifications they fund.

While option b maintains a shared funding model it would operate on a tightly defined co-contribution basis at the qualification level. Instead of uniform agreements under which Commonwealth funding is provided on a population share basis - regardless of the level of state funding - differentiated bilateral agreements would be instituted where the level of Commonwealth investment was directly related to the level of state investment. This avoids the problem inherent in the current model where one jurisdiction can reduce funding and benefit from efficiency improvements while expecting the other jurisdiction to maintain or increase its funding.

Option B draws on some of the features of the National Disability Insurance Scheme (NDIS) which is funded in its establishment phase on the basis of a joint contribution between the Commonwealth and the states to an agreed price for the various service categories.

However none of these options in themselves addresses the fundamental issue that clearly emerges from the analysis in this paper: declining levels of public investment in VET - particularly in some jurisdictions - and the consequences of the growing imbalance of investment in VET relative to schools and higher education. Addressing that issue is the threshold issue for COAG when it considers future options for funding VET in Australia.

Decisions on the future of VET should be taken as part of a redesign of funding of tertiary education in Australia across the VET and higher education sectors – a process in which the Commonwealth must take the lead.

# Endnotes

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[xvii] Commonwealth Department of Education and Training *2014 VET FEE-HELP Statistical Report – Summary*

[xviii] Department of Parliamentary Services (2015). *Higher Education Support Amendment (VET FEE-HELP Reform) Bill 2015* Bills Digest *http://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/bd/bd1516a/16bd060*

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[xx] For a detailed analysis of subsidies at different qualifications levels and under various see Chapman, B and Higgins, T. (2015). *Feasibility and design of a tertiary education entitlement in Australia,* Mitchell Institute, Victoria University.

[xxi]Productivity Commission (2016). *Report on Government Services 2016.*

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[xxiii] Bradley, D. Noonan, P. Nugent, H. and Scales, B. (2008). *Review of Australian Higher Education* Commonwealth of Australia, p.183.

[xxiv] Bradley et al, p.185.

[xxv] Bradley et al, p.182.

[xxvi]Skills Australia (2011). *Skills for prosperity a roadmap for vocational education and training* https://docs.education.gov.au/system/files/doc/other/skillsprosperityroadmap-2011.pdf

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