



**Briefing Note: Summary of advice on changes to the Partnership Schools funding model and further advice on the application process and timeline**

Date:	19 June 2015	Priority:	High
Security Level:	In Confidence	METIS No:	935614
To:	David Seymour MP, Parliamentary Under-Secretary to the Minister of Education		
Copy to:	Minister of Education, Hon Hekia Parata		
Approved by:	Lesley Hoskin	DDI / Mob	[REDACTED]

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## Introduction

### Purpose

1. This paper sums up the advice we have provided on the review of the Partnership Schools' funding model in three previous papers<sup>1</sup>. It reflects the feedback on those papers provided by you and your office.
2. This paper also provides further advice on the application process and timeline.
3. A final Education Report with proposed changes to the funding model, the contract and advice on the application process and timeline is due to the Minister of Education (the Minister) on 2 July 2015.

### Objectives

4. In the 2 July paper to the Minister, we will inform the Minister that you propose to make some alterations to the funding model that will:
  - move risk from the Government toward the sponsor so that there is a better incentive for the sponsor to reach desired outcomes in the most efficient way
  - reduce the start-up costs of new schools which will also increase the sponsor's incentives to secure external funding.
5. In particular, this will be done by:
  - moving to a true 'per-student' funding model rather than a 'per school' model
  - ensuring that the property funding flow is aligned with the current enrolment [Metis 924404 refers].

<sup>1</sup> "Partnership Schools work programme update – funding model, contract review and round three applications" [Metis 928289]; "Further advice on Partnership Schools property funding" [Metis 929555]; "Partnership Schools funding model review: further advice on the teaching and operating rate" [Metis 932173]

### Components of the funding model

6. On the basis of the work undertaken to date, the new Partnership Schools funding model would have four components:
- an establishment funding rate
  - a per student property rate
  - a teaching and operating rate
  - a professional development and resources rate.

### Establishment funding rate

#### Where we are up to

7. Partnership Schools have to provide a physical environment and resources to the standard required by the Education Review Office. The existing funding model provides the sponsor with:
- a set-up grant based on the maximum roll of the school, calculated according to the type of school. This grant is to cover administrative set-up costs; establishing a library; and purchasing curriculum material and other teaching resources
  - six months of property funding so that leases can be arranged and renovations completed before students enrol
  - six months' salary to employ a principal to set up the school and establish the teaching and learning programme.
8. State schools are not restricted in how they use their set-up grants, but the items below are some of the things that they commonly use the funding for:

Potential uses of set-up funding
<b>Administration grant</b>
<ul style="list-style-type: none"><li>• rental of a place to hold meetings until the school is built</li><li>• salary for office assistance in the period before the school opens</li><li>• heat, light, internet, and water in the period before the school opens</li><li>• software e.g. an accounting package; student management system</li><li>• consumables (e.g. photocopying paper) advertising and other costs involved with student enrolment and staff employment</li><li>• visits to other schools</li></ul>
<b>Learning and teaching resources</b>
<ul style="list-style-type: none"><li>• software licences</li><li>• textbooks, lap tops, iPads</li><li>• arts/lab/technology supplies</li><li>• wall charts; teaching models</li><li>• CDs/DVDs/ music</li></ul>
<b>Library and information centre</b>
<ul style="list-style-type: none"><li>• library books and other resources</li><li>• computers (in addition to above)</li></ul>

9. It is proposed that the set-up grant be replaced with a fixed contribution to these costs. The proposed fixed contribution is \$100,000 for primary schools and \$200,000 for secondary schools.
10. In addition to the fixed contribution, the new establishment funding rate would include six months of property funding and principal's salary, as is the case under the existing funding model. However, property costs would be calculated on the new property per-student rate (see below) for the number of students proposed to be enrolled in the school's first year of operation.<sup>2</sup>
11. The table below sets out a comparison between the current establishment costs and the proposed costs:

<b>Comparison of set-up funding under current and proposed models</b>			
<b>Rolls</b>	<b>Current</b>	<b>Proposed</b>	<b>Difference</b>
Primary 50	250,962	195,713	55,249
Primary 100	343,573	218,181	125,392
Secondary 100	721,038	435,176	285,862
Secondary 200	1,018,326	560,694	457,632
Secondary 300	1,267,557	638,153	629,404

12. You have proposed that sponsors could be invited to submit competitive tenders for establishment costs. [Metis 924404 refers]. How this will work will be considered as part of the application process.

### **Comment**

13. Like state schools, Partnership Schools have flexibility to use the funding provided to them for set-up costs to buy varying numbers of an item, or at higher or lower costs. Some of the items will be essential for the school to be able to function from the day it opens, but others can be added to over time. The nature of the Partnership School will also be a relevant factor in determining what the school needs in the establishment phase.
14. The fixed contribution gives potential sponsors certainty over the level of set-up funding they would receive. While the proposed amounts for the fixed contribution should be adequate, sponsors would have the option of supplementing this with their own funds or accessing third-party funding.
15. The proposed establishment rate achieves your objectives to reduce set up costs and increase incentives to secure external funding.

## **Property funding**

### **Where we are up to**

16. You have indicated that you are seeking a funding model with property funding that:
  - is consistent with real market costs / market rental costs

<sup>2</sup> Under the current funding model, property funding in the establishment phase is based on the school's maximum roll.

- is aligned with current enrolment / tracks actual enrolments (not maximum rolls)
  - is approximately the rental cost of a full state school with the same number of students in a similar area
  - allows Partnership Schools to use their property funding as they see best
  - reduces property costs
  - accommodates those sponsors in a position (due to funding by third parties) to provide property in excess of the funded level. In such cases they should be funded at the same level as any other Partnership School, with the additional resource seen as an extra contribution.
17. We have modelled a per-student rate for property by taking the Cash for Buildings amount for the school's maximum roll and dividing it by that roll number. The per-student rate for property will therefore be different for each school. By using a per-student rate the property funding will be sensitive to changes in student numbers.
18. You expressed concern that Cash for Buildings may not be consistent with market rental costs, which have considerable regional variation [Memo of 16 April 2015 refers].
19. We have therefore investigated using a regional rates approach based on Collier's 'New Zealand CBD Office 2014' report. The investigation showed that for most cities, Cash for Buildings provides less funding per square metre than a sponsor might expect to pay to lease office space. This reflects the fact that Cash for Buildings does not factor in the cost of land [Metis 929555 refers].

#### **Comment**

20. Cash for Buildings appears to be the best option for determining property funding for Partnership Schools. Converting it to a per-student rate based on current enrolments meets the objective of having property funding aligned with current enrolment and reducing property costs.
21. It may have the following effects:
- a sponsor may have to provide funding themselves or attract funding from a third party for a permanent site
  - in the early years when the school is building up its roll, the school may have to move sites as the school grows or lease a larger space in anticipation of future growth
  - there will need to be certainty that the schools have sufficient reserves to create a financial buffer to cover the possibility of falling or fluctuating rolls
  - sponsors may be locked into long term leases that they have to default on if rolls fall or do not rise as expected, or take higher cost short-term leases because they are uncertain about rolls.
22. Your objective of allowing Partnership Schools to use their property funding as they see fit will be served by continuing to allow sponsors to choose to rent or contribute their funding towards purchasing a property (pending decisions on the contract review for including claw-back provisions where Crown funding has been used).

## Teaching and operating rate

### Where we are up to

23. In the Education Report of 18 May 2015<sup>3</sup> you noted that we were working on options to address the viability of small Partnership Schools by developing a per-student teaching and operating rate that is proportionately higher for smaller schools, reducing progressively as school rolls increase toward the viability point, and flattening out once the viability point is achieved [Metis 928289 refers].
24. You have indicated that you wish to have a new funding model for Partnership Schools that is no more expensive than the existing model, with:
- a teaching and operating rate or rates that enable Partnership Schools of differing sizes and types to deliver an effective education
  - a per-student funding formula for the teaching and operating rate that allows small schools to be viable but does not over-fund larger schools
  - testing of the model for schools of various sizes and types to ensure that it is sustainable [Metis 928289 and 932173 refer].
25. At this stage we are considering three possible ways of determining a teaching and operating rate:
- an **averages model** based on 2014 state school data
  - a **marginal rates model using the current funding formula**
  - a **marginal rates model using the averages model formula.**
26. All three options adopt a per-student rate, and therefore address the objective of tying funding more closely to actual student numbers.

### *Averages model*

27. The Ministry has calculated rates based on average salary and operational costs for state schools. It constructs a teacher salary rate that is applied to the staffing entitlement of a state school of a particular roll size. It then adds an average operational grant figure for a decile 3 school of the same roll size. This figure is then divided by the roll to reach a per-student amount [Metis 932173 refers].

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<sup>3</sup> "Partnership Schools work programme update Metis 928289"

Teaching and operating rates based on average salaries and decile 3 operational funding			
Primary roll	Rate	Secondary roll	Rate
50	8,579	75	14,606
75	7,541	100	12,585
100	7,022	150	11,105
125	6,665	200	10,000
150	6,354	250	9,337
175	6,199	300	8,892

28. This model has the advantage that it would be easier to explain to the sector and the public. It addresses the issue that a single base funding rate under the current model may have favoured small secondary schools.
29. The disadvantage with this model is that, because it follows the stepped changes in the state school staffing and funding formulae, it results in total Partnership School funding dropping at the rate change points (see diagram on page 3 in Metis 932173). The model also results in increased funding for primary schools.

***Marginal rates model using the current formula***

30. Your office has for illustrative purposes applied a marginal rates approach to the existing funding formula [Memo of 12 June 2015 refers].
31. The marginal rate calculates the slope of the graph between each of the roll steps on which the modelling has been done. For example, for primary schools the slope of the graph between 0 students and the first data point at 50 students is \$7,676 per student. The marginal rate slope between 50 and 75 is the difference between the data points at 50 and 75. The marginal rate is the difference between the data point at 50 students and the next data point at 75 students. The calculation is as follows:
- data point at 50 students = \$383,800 ( $\$7,676 \times 50$ )
  - data point at 75 students = \$501,900 ( $\$6,692 \times 75$ )
  - difference between data points = \$118,100 ( $\$501,900 - \$383,800$ )
  - slope between data points (marginal rate) = \$4,724 ( $\$118,100 / 25$  students).

32. The table below sets out the results:

Marginal rates using the current formula					
Primary schools			Secondary schools		
Roll	Current formula	Marginal rate for current formula	Roll	Current formula	Marginal rate for current formula
50	7,676	7,676	75	18,866	18,866
75	6,692	4,724	100	15,504	5,418
100	6,200	4,724	150	12,142	5,418
125	5,905	4,725	200	10,462	5,422
150	5,709	4,729	250	9,453	5,417
175	5,568	4,722	300	8,781	5,421

33. Applying the marginal rates to the current funding formula has the advantage that Partnership Schools in the future would get the same funding as the current ones. The total amount of funding that schools receive increases steadily, without any drops at the change points.
34. The main disadvantage with this model is that it is based on the original regression analysis model. The model has proved very difficult to explain to the sector in simple terms. It provided a snapshot of funding based on 2011 data but, if it was re-calculated with updated data, it might produce very unpredictable changes. This is because it was based on decile 3 data which provides a very small sample size at particular points and a wide variation in the schools and teachers that may move into and out of decile three.

***Marginal rates approach applied to the averages model***

35. We have applied the marginal rates approach to the average per-student rate derived using the 2014 school data:

Marginal rates using the averages model					
Primary schools			Secondary schools		
Roll	Current formula	Marginal rate for current formula	Roll	Current formula	Marginal rate for current formula
50	8,579	8,579	75	14,606	14,606
75	7,541	5,465	100	12,585	6,522
100	7,023	5,469	150	11,105	8,145
125	6,665	5,233	200	10,000	6,685
150	6,354	4,799	250	9,337	6,685
175	6,199	5,269	300	8,892	6,667

36. Applying marginal rates to the averages model has the advantage that it is based on inputs that the sector can recognise (although the marginal funding concept adds a degree of complexity). It is relatively easy to update. It reduces the rates for small secondary schools and increases the rates for small primary schools.
37. Disadvantages are that there are outliers in both the primary and secondary rates at a roll of 150. We believe these reflect changes in base staffing entitlements at these points. There are also slightly higher per-student rates for larger schools (eg compare the \$6,667 at 300 secondary students for \$6,522 for 100 students).

**Comment**

***Choice between the models***

38. The two marginal rates options provide the best fit with the objectives. The marginal rates model on the current funding formula matches funding to existing rates but is difficult to explain and replicate. The marginal rates on the averages model provides a more user-friendly funding formula with more accurate costs at the lower end of the scale but the potential for increased cost.

***Numbers of rates***

39. Early discussions on a new Partnership Schools funding model with The Treasury and the Department of Prime Minister and Cabinet indicated that they would prefer the model to have a small number of rates.
40. Both marginal rates models would lend themselves to provide two rates: a higher "start-up" rate for the first 50 or 75 students respectively and then a constant per student rate, arrived at by averaging the marginal rates for the following five roll points.
41. This would result in the following rates:

<b>Per-student rates with marginal rates</b>		
<b>School and Roll</b>	<b>Current formula</b>	<b>Averages formula</b>
Primary roll 50 and below	7,676	8,579
Primary Roll 51 and above	4,725	5,247
Secondary; Roll 75 and below	18,866	14,606
Secondary: Roll 76 and above	5,419	6,941



42. Total teaching and operating rate funding on the roll ranges modelled using these rates is set out below:

<b>Comparison of current and averages formula with marginal rates</b>					
<b>Primary schools</b>			<b>Secondary schools</b>		
<b>Roll</b>	<b>Current formula</b>	<b>Averages formula</b>	<b>Roll</b>	<b>Current formula</b>	<b>Averages formula</b>
50	383,800	428,950	75	1,414,950	1,095,450
75	501,925	560,125	100	1,550,425	1,268,975
100	620,050	691,300	150	1,821,375	1,616,025
125	738,175	822,475	200	2,092,325	1,963,075
150	856,300	953,650	250	2,363,275	2,310,125
175	974,425	1,084,825	300	2,634,225	2,657,175

### **Professional development and resources rate**

43. This is \$276 per student. It was derived from the major appropriations for professional development and teaching resources. The rate will be reviewed after the third year of the contract. No changes are proposed at this time.

### **Further advice on application process and timeline**

44. You have indicated no change to the continued relevance of preferences and the evaluation criteria previously advised.

#### ***Government Preferences***

45. The Minister has indicated that she would like government preferences to be applied to the third round of applications [METIS 928289 refers].

46. We therefore propose to retain the following preferences from the second round of applications:

- Make effective use of the flexibilities offered by the model
- Are based in areas of roll growth
- Are large enough to be economically viable.

47. We propose to add the following preferences to a third application round:

- Provide innovative or alternative options for students.
- Bring together education, business and/or community sector partnerships.

48. We propose to not apply the following preferences used in the last round to a third application round:

- Cater for primary age students
- Offer innovative options for 0-8 year olds.

***Timeline***

49. Our goal is to conduct a process that allows for approved schools (if any) to open in 2016. We need to confirm through the application process if there are applicants who will be able to meet this. We will support the Authorisation Board to assess submitted applications accordingly.

50. An updated timeline is attached as appendix A.

51. The Ministry and the Authorisation Board have discussed applying increased oversight to the establishment process, with a view of introducing some checkpoints that the sponsor must meet throughout the process before gaining final approval to open. This could include such things as being able to evidence a minimum number of student enrolments, development of school property to a minimum standard, and/or (in the case of a secondary school) gaining NZQA Consent to Assess Against Standards.

## Appendix A Updated timeline

RFA in Market	Description	Target Date	Dependencies
Develop RFA	<ul style="list-style-type: none"> <li>Incorporates detail of the funding model applied to this round</li> </ul>	Friday, 31 July 2015	
RFA in Market	<ul style="list-style-type: none"> <li>4-6 week duration</li> <li>Assumes issued day after Cabinet approval</li> <li>Does not allow for any pre-tender market development activity (+1-2 months)</li> </ul>	Friday, 4 September 2015	Subject to Cabinet approval being received by 4 August
Assessment/Interview	<ul style="list-style-type: none"> <li>6-8 week duration</li> </ul> Covers <ul style="list-style-type: none"> <li>Short listing</li> <li>Interim advice to Minister</li> <li>Interviews</li> <li>Due Diligence</li> </ul>	Friday, 16 October 2015	Duration is subject to availability of Board to complete assessment process
Approval to negotiate	<ul style="list-style-type: none"> <li>Development of advice to Minister</li> <li>Assumes 4 weeks for approval including Cabinet endorsement/approval</li> </ul>	Friday, 13 November 2015	Subject to availability of Minister and Cabinet schedule
Negotiation	<ul style="list-style-type: none"> <li>Minimum 4 weeks</li> <li>Development of negotiation plan</li> <li>Execute negotiations</li> <li>Finalise contract schedules</li> </ul>	Friday, 11 December 2015	Duration is subject to availability of parties and complexity of negotiations
Execution of Agreements	<ul style="list-style-type: none"> <li>2-3 weeks</li> <li>Prepare advice to Minister, including Cabinet paper as required</li> <li>Contracts executed.</li> </ul>	Thursday, 24 December 2015	Assumes no Cabinet actions required
Establishment Period	<ul style="list-style-type: none"> <li>No fixed date but a minimum of four months is not unusual.</li> </ul>	TBC	Subject to the readiness of approved sponsors
Schools Open	<ul style="list-style-type: none"> <li>On agreed date committed by Sponsor</li> </ul>	2016	

