
New South Wales Auditor-General's Report

Performance Audit

Vocational Education and Training Reform

Department of Education and Communities



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In accordance with section 38E of the *Public Finance and Audit Act 1983*, I present a report titled **Vocational Education and Training Reform Department of Education and Communities**

A handwritten signature in black ink, appearing to read 'Grant Hehir'.

Grant Hehir
Auditor-General
29 January 2015

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Executive summary

Background

The NSW Government recognises the need for an educated, skilled workforce to drive a productive economy, support workforce participation and grow industry and business. Its goal is to increase the proportion of working-aged people with post school qualifications at Certificate III level and above, from 55.8 per cent in 2010 to 83.7 per cent in 2020, an increase of 50 per cent.

Over the last decade, the Commonwealth has contributed to Vocational Education and Training (VET) reform through a series of National Partnership Agreements. The most recent of these, the 2012 National Partnership Agreement on Skills Reform (NPASR), required an entitlement for subsidised training. Governments will pay the subsidy to Registered Training Organisations (RTOs) that attract and train students. Governments agreed to provide greater competition in an accessible, transparent, efficient and quality training sector that is responsive to the needs of students, employers and industry. Under NPASR, the Commonwealth will pay New South Wales \$561.6 million over five years from 2012–13 for delivering the reform, including the goal of increasing the number of people completing post-school qualifications by an average of around 16,000 (14 per cent) each year.

Governments used the flexibility provided under NPASR to implement the reforms in different ways. Victoria began before NPASR commenced, setting up a demand-driven system in 2008 with low barriers to RTO entry. Five years later 100 per cent of the VET market was contestable, training 207,000 (72 per cent) more students at a cost of an extra \$764 million (65 per cent). Since 2013, Victoria has sought to reduce VET expenditure, improve quality and value for money and fund the rationalisation of the public provider TAFE. Other States have also sought to cap expenditure and ensure quality and a reduced but ongoing role for TAFE. Governments subsidise different qualifications for different student groups for different amounts.

New South Wales is the latest State to implement the reform. The Minister for Education announced the Smart and Skilled reform in 2012, which introduced a VET entitlement from 1 January 2015. The VET reform aims to get more people trained while maximising public value for the government's investment. Unlike Victoria, New South Wales intends the reform to be budget neutral.

In 2013–14, the NSW Government spent \$2,185.5 million subsidising VET for around 500,000 student enrolments. TAFE accounted for over 85 per cent of the VET spending and 77 per cent of the student enrolments. The Government expects the VET reform to gradually reduce that proportion but for TAFE to continue to be the major provider.

Apart from meeting its commitment to introduce an entitlement without spending more, the government's other major policy objectives under NPASR are to:

- sustain TAFE in a competitive market
- introduce consumer driven contestability
- ensure VET is available across the State and to disadvantaged groups
- provide high quality training.

This audit assessed the effectiveness of the Department of Education and Communities' (the Department) framework for VET reform and whether it has the potential to achieve these objectives. More details on the audit objective, scope and focus are outlined in Appendix 1.

We undertook the audit before the new VET Smart and Skilled reform commenced on 1 January 2015.

Conclusion

The Department's framework for VET reform has the potential to effectively achieve the government's immediate objectives for the reform, which are associated with meeting its commitments under the National Partnership Agreement for Skills Reform without spending more.

We found that the government is addressing VET reform objectives in the following order of priority:

- no extra cost (budget neutrality)
- TAFE viability
- quality VET
- access to VET for regions and equity groups
- more contestability
- student choice.

Overall, we conclude that a more balanced approach, by putting more emphasis on increased contestability and student choice, is more likely to maximise the public value for the government's investment in VET.

In addition, the VET reform framework does not address the government's longer-term goal to increase the proportion of working-aged people with post-school qualifications at Certificate level III and above by 50 per cent by 2020. New South Wales is most unlikely to reach this State Plan goal on current trends. The VET reform's budget neutral objective, its pricing structure and the incentives for efficiency mean that it is unlikely to generate the funds needed to meet this State Plan goal.

It is appropriate that the framework separates responsibility for purchasing and providing training. However, this separation is incomplete. The government continues to provide TAFE with direct non-contestable funding. The budget for this direct funding is not subject to clear purchaser oversight, nor is it clear how long it will continue or what TAFE will deliver for it. In addition, the benefits of the VET reforms depend on achieving the efficiency outcomes of the TAFE reforms. While the Department has addressed benefits management principles in its documentation, it does not have a benefits realisation plan and register to ensure that it can demonstrate which VET reform benefits have been achieved in four years' time.

The Smart and Skilled reform is a complex initiative. The Department is developing the key systems, tools and processes necessary to purchase and manage training in 2015 and to inform students' choice of provider. The implementation of the Smart and Skilled reform and its enabling systems has been delayed and remains on a tight timetable. The Department has used suitable project management controls to ensure that the Smart and Skilled reform commenced on its revised 1 January 2015 launch date.

Recommendations

The Department of Education and Communities should:

1. by April 2015, finalise accountability arrangements for TAFE's non-contestable funding and specify what it expects each TAFE Institute to provide and report on for its direct funding (page 27)
2. by April 2015, expedite State Training Services' training and reorganisation to ensure its people have the capabilities to monitor and regulate training, protect students and ensure value for money (page 29)
3. by April 2015, add information about the demand for qualifications on the Smart and Skilled website for students looking for courses (page 33)
4. by July 2015, ensure that the NSW Skills Board has adequate resources to meet its statutory responsibility to provide oversight of the reform and independent strategic advice to the Minister for Education (page 26)
5. by July 2015, publish a benefits realisation plan so it can monitor and review its progress in reforming the VET sector (page 32)
6. by July 2015, establish six-monthly public reporting metrics, and publish initial data and information on:
 - 6.1. trends in training activity by provider type, industry, equity group and region to identify gaps and changes in VET delivery
 - 6.2. progress against NSW 2021 targets
 - 6.3. RTO quality indicators, such as graduate employment outcomes and student and employer feedback
 - 6.4. trends in efficiency gains and the cost of delivery
 - 6.5. what TAFE provided for its non-contestable funding (page 35)
7. by July 2015, publish a State Training Plan for the next four years that:
 - 7.1. identifies the actions it will take to capture efficiencies and build a sustainable VET system capable of supporting the NSW goal of a more highly skilled population
 - 7.2. sets targets for the number of VET enrolments and completions each year needed to support this goal
 - 7.3. identifies the State's investment priorities and planned funding for VET (page 42)
8. during 2015, to inform the 2016 review of VET pricing:
 - 8.1. collect robust data on the cost of training delivery
 - 8.2. assess whether qualification pricing should be weighted to reflect public value
 - 8.3. assess the impact of the partial implementation of the 2013 IPART recommendations on pricing for VET in relation to the efficient price for student fees and the decision not to define the fee as a maximum and allow RTOs to charge up to 50 per cent less (page 24).

Response from the Department of Education and Communities



Mr Grant Hehir
Auditor-General of New South Wales
Audit Office of New South Wales
GPO Box 12
SYDNEY NSW 2001

DGL15/48

Dear Mr Hehir

I write in response to your letter of 15 January 2015, providing me with a copy of your report on the Performance Audit of the Vocational Education and Training reform in New South Wales.

Please find attached a copy of the Department of Education and Communities' formal response for inclusion in the published report.

The performance audit was helpful and gave the Department the opportunity to reflect and note its achievements in the design and implementation of this complex reform.

I am pleased to inform you that the Department accepts all of the report's recommendations which will assist with the evaluation and improvement of Smart and Skilled. Smart and Skilled has set the foundation for a high quality and sustainable training system and will continue to deliver value to the public of New South Wales.

I would like to thank the review team of the Audit Office of New South Wales for their work and also recognise the officers within the Department who provided assistance.

Yours sincerely

A handwritten signature in black ink that reads 'Michele Bruniges'.

Dr Michele Bruniges AM
SECRETARY
DEPARTMENT OF EDUCATION AND COMMUNITIES
21 January 2015

DEPARTMENT OF EDUCATION AND COMMUNITIES' RESPONSE

BACKGROUND TO SMART AND SKILLED

Smart and Skilled is a reform of the NSW Vocational Education and Training (VET) system that aims to expand the skills of the NSW workforce to meet future demands for jobs.

Through this reform the NSW Government has established arrangements that enable eligible individuals to access government subsidised training up to and including Certificate level III through TAFE NSW and approved private and community training providers. The reform also subsidises higher-level training from Certificate IV to Advanced Diploma, and prevocational and part qualifications in priority industry areas.

The NSW Government has introduced new price and fee arrangements and established a priority skills list developed through extensive industry consultation. Smart and Skilled has a range of mechanisms to protect consumers and ensure quality training provision. The Smart and Skilled reforms were introduced following significant research and broad consultation with industry, providers and the community. Smart and Skilled incorporates advice of the independent NSW Skills Board.

Smart and Skilled provides a VET system that is more accessible and more efficient in meeting the needs of students, employers and industry.

DEPARTMENT'S RESPONSE TO RECOMMENDATIONS

The Department accepts all recommendations in the audit report. It has commenced implementing the recommendations and expects to achieve them in the prescribed timeframes.

DEPARTMENT'S RESPONSE TO THE AUDIT CONCLUSIONS

The Department is pleased the report confirms that Smart and Skilled has the potential to achieve the NSW Government's immediate commitments to VET reform under the National Partnership Agreement for Skills Reform.

The report also indicates that Smart and Skilled is addressing the NSW Government's VET reform objectives of greater student choice, quality and accessible training, and viability of TAFE NSW as public provider. The Department will continue to increase its focus on public value through the planned review of Smart and Skilled and the adoption of your recommendations.

The Department welcomes the finding that while Smart and Skilled is a complex initiative, the Department's implementation is well managed with appropriate governance and project management systems that enabled its successful launch on 1 January 2015.

You conclude that the NSW framework for VET reform appropriately separated the responsibilities of purchaser and provider. We note that the separation of the Department and TAFE NSW is recent and the Statement of Owner Expectations for TAFE NSW sets out the objectives for TAFE NSW successful transition to a more contestable VET market.

A Memorandum of Understanding (MOU) between the Department and TAFE NSW is being concluded which will govern the accountability for non-contestable funding provided to TAFE NSW.

DEPARTMENT'S RESPONSE TO THE KEY FINDINGS

The Department accepts the conclusions drawn in the report, with the comments provided below as further context and interpretation.

1. The Department's framework for VET reform

The Department's framework for VET reform has the potential to support the Government's immediate outcomes and meets the State's commitments under the National Partnership Agreement on Skills Reform.

You observe that NSW does not have a fully demand-driven entitlement because of restrictions on the number of subsidised places a registered training organisation (RTO) can offer to ensure budget neutrality.

As you acknowledge, NSW has taken a cautious approach to implementing the VET reform, taking into account the lessons learnt from Victoria and other states. The Department's design of Smart and Skilled is informed by and carefully balances the Government objectives of student access and equity, choice, maintaining a sustainable public provider and budget neutrality.

Through in-depth consultation and with strategic advice from the NSW Skills Board, the Department developed a Skills List that prioritises the future and ongoing skills needs of the State. We will constantly monitor student demand and industry needs through our reviews of Smart and Skilled and analysis of VET markets.

We are pleased that Smart and Skilled will enable over 60,000 more people to train in 2015 with NSW Government subsidised support.

2. The roles and responsibilities of funder, purchaser and providers

The report observes that the Government appropriately separated the roles of purchaser and provider so that it could introduce a transparent, flexible and competitively neutral VET system. The Government separated TAFE NSW from the Department and established TAFE NSW as a distinct financial entity in 2014.

The report notes that despite the separation there is some ambiguity in the accountability for TAFE NSW non-contestable funding. The TAFE NSW *Statement of Owner Expectations* is clear that the Managing Director of TAFE NSW will report regularly on the performance of TAFE NSW against its specific budget accountabilities to the Department of Education and Communities. The Department is concluding an MOU with TAFE NSW which will document the accountability requirements for this funding.

The report also finds that it is not clear whether the NSW Skills Board has adequate resources to meet its statutory responsibilities. The Department is fully committed to work closely with the NSW Skills Board to ensure the adequacy of its resources so that it can fulfil its functions under its Act.

You observe that the reorganisation of State Training Services was impacted by the Department's implementation of the *Government Sector Employment Act* in 2014. State Training Services is continuing to work on the realignment of its functions and Smart and Skilled was successfully launched on 1 January 2015.

3. Systems to capture and communicate information to manage and regulate VET in 2015

The Department is pleased with the finding that while Smart and Skilled is a complex initiative, the Department's implementation is well managed with appropriate governance and project management systems that enabled its successful launch on 1 January 2015.

As you observe, the Department is progressing well in developing systems and information needed to manage and regulate the training market in 2015 and has prioritised critical tasks to allocate training places, take enrolments, and report on training activity in the market.

The Department is committed to publicly report on the state of VET in NSW every six months and report on the benefits realised from the reform.

4. The Department's plans to contribute to the Government's long-term training outcomes

The key findings state that the Department is on track to meet its obligations under the National Partnership Agreement on Skills Reform and has achieved encouraging results for Aboriginal and female students, and people in regional NSW. You report that we have reached most of the goals for these target groups as outlined in *NSW 2021: A Plan to Make NSW Number One*.

Your report notes that the *NSW 2021* goal for 83.7 per cent of the population to have post school qualifications at Certificate level III and above by 2020 is ambitious. You observe that it will require substantial efficiency improvements or more funding to provide clear signals to RTOs about their plans for the sector and how and where growth will occur.

As per the recommendation in the report, the Department will include yearly targets with interim action plans for the number of VET enrolments and completions needed to support this goal in the State Training Plan to be published by July 2015.

Background

1. Vocational education and training reform

1.1 Subsidised VET in New South Wales

In 2013–14, the Department of Education and Communities (the Department) spent \$2,185.5 million on subsidised vocational education and training (VET) for around 500,000 enrolments. Students typically do VET after leaving school. Exhibit 1 shows how the various levels of qualification relate to job opportunities. In this report we refer to levels one to three as entitlement qualifications and four to six as higher qualifications.

Exhibit 1: Examples of VET qualifications and occupations

Level		Occupations related to qualifications in aged care, agriculture and plumbing
Entitlement	1	Certificate I and II – Foundation skills – skills required for participation in workplaces For example, literacy and numeracy
	2	Certificate II – knowledge and skills for work in a defined context and further learning For example, community worker, farm worker, building and plumbing labourer
	3	Certificate III – theoretical and practical knowledge and skills for work and further learning For example, aged carer, farmer, plumber (apprenticeship)
Higher	4	Certificate IV – theoretical and practical knowledge and skills for specialised work and further learning For example, residential care officer, farmer/farm manager, plumber
	5	Diploma – specialised knowledge and skills for skilled/paraprofessional work and further learning For example, enrolled nurse, farmer/farm manager, plumber
	6	Advanced Diploma – broad knowledge and skills for paraprofessional/highly skilled work and further learning For example, enrolled nurse
Apprenticeships and traineeships are differentiated from other qualifications by the student's employment status.		

Source: Department of Education and Communities 2014.

In 2013–14, the Department allocated 85.4 per cent of VET funding directly to TAFE, which has been responsible for planning and delivering most subsidised training in New South Wales for many years. Eleven per cent of the VET funding was contestable to subsidise Registered Training Organisations (RTOs) for apprenticeships, traineeships and a shortlist of priority qualifications. Of this, the Department distributed 2.75 percentage points to TAFE and 8.25 percentage points to around 750 private RTOs. One per cent of the non-contestable funding was provided to Adult Community Education (ACE) colleges as grants. The remaining VET funding covers the Department's administrative costs.

Exhibit 2 gives an overview of VET enrolments in 2013 that the Department subsidised or that TAFE delivered on a full fee basis. Governments across the country lack good information on full fee training provided by private RTOs and are seeking to remedy this as part of the current reforms. The exhibit shows a six per cent increase in enrolments driven by an expansion of TAFE's full fee higher qualifications.

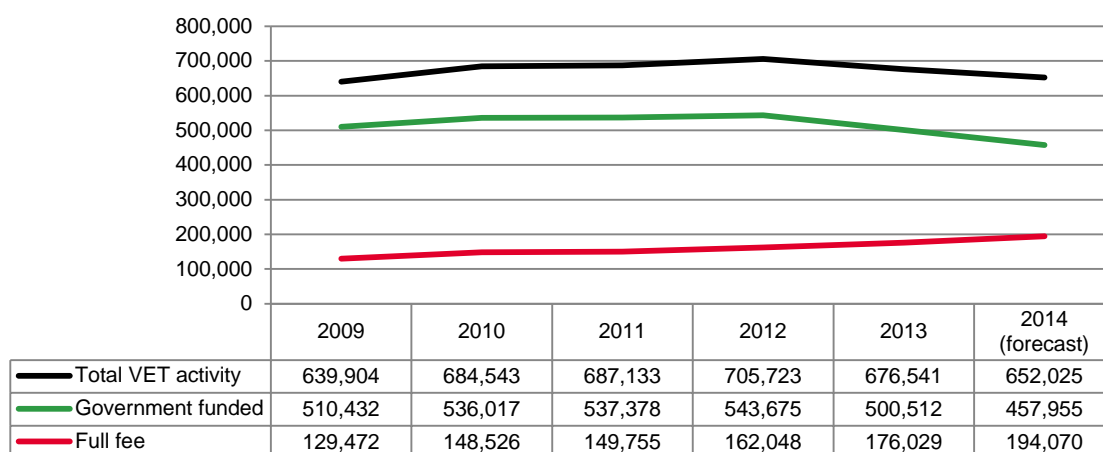
Exhibit 2: VET enrolments by qualification in 2013 compared to 2009

Enrolments	Government subsidised		Full fee TAFE only
	TAFE	Non—TAFE	
Certificate III and below – includes non-AQF	290,746 -2%	99,179 -12%	105,544 +6%
Certificate IV and above	94,344 +6%	16,243 +24%	69,831 +166%
Total	385,090 0%	115,422 -8%	175,375 +39%

Source: National Centre for Vocational Education Research 2014.

This audit examines subsidised VET reform, but notes that full fee training is growing. The Department is not responsible for funding or monitoring full fee training, although this contributes to the State's goal of increasing the proportion of the population with qualifications.

Exhibit 3: NSW VET enrolments: 2009 to 2013 (actuals); 2014 (forecast)

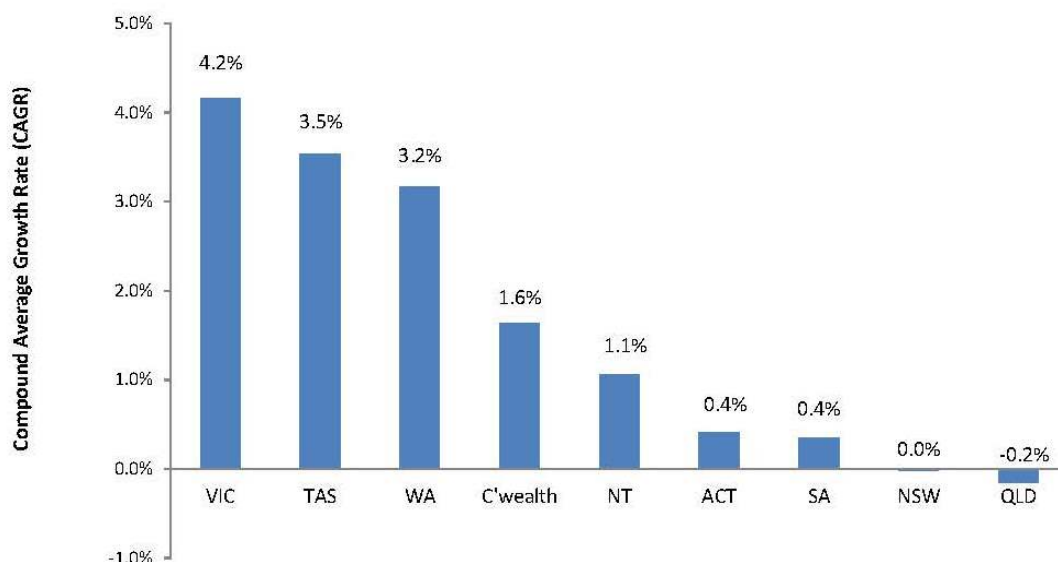


Source: National Centre for Vocational Education Research 2014.

1.2 VET funding trends across Australia

Over the last decade, public spending on training has varied from State to State with some making large investments. New South Wales training expenditure has not increased.

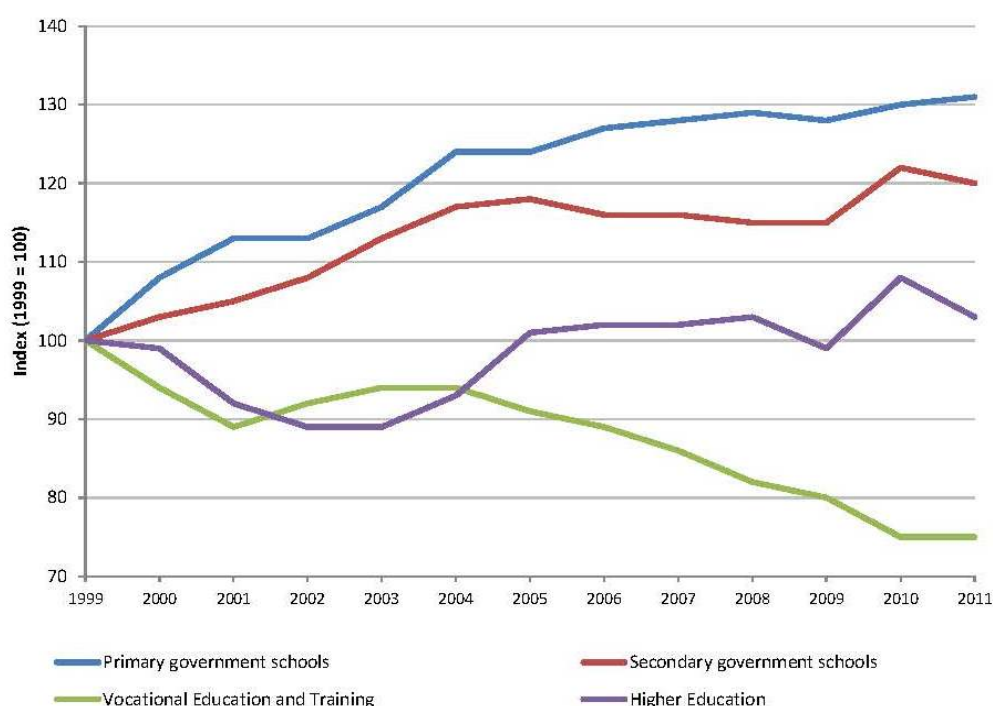
Exhibit 4: Growth in VET expenditure 2003–04 to 2012–13



Source: ACIL Allen 2014 based on Australian Bureau of Statistics data 2014.

Nevertheless, government spending per student is falling across the country as student numbers grow faster than public funding. VET students are paying more for their training. Exhibit 5 shows that, while government spending on school and university students increased, it fell by a quarter for VET students between 1999 and 2011.

Exhibit 5: Australia-wide recurrent public expenditure per student 1999 to 2011



Source: Australian Workforce and Productivity Agency, Future Focus: 2013 National Workforce Development Strategy.

1.3 National reform of VET

Governments across Australia have recognised for some time the need for a skilled workforce to enable economic growth and individual opportunity. Over the last decade, they have entered into a series of National Partnership Agreements for VET reform.

The governments agreed to the current National Partnership Agreement on Skills Reform (NPASR) in 2012. It runs until 2016–17 and provides for Commonwealth funding to help States and Territories introduce greater competition in the VET sector, with the aim of fostering a more accessible, transparent, efficient, quality training sector that is responsive to the needs of students, employers and industry.

In return, States and Territories agreed to:

- create an entitlement for working age Australians to a subsidised training place for entry level training up to and including a Certificate level III qualification. Governments will pay the subsidy to RTOs that attract and train students
- increase student access to income contingent loans (ICL) for higher qualifications
- improve transparency by reporting comprehensive information on VET activity, student outcomes and RTO performance
- strengthen VET quality by enhancing their capacity to develop and review RTO performance and the validity of student assessments
- improve public RTO efficiency and competitiveness
- increase the number of students completing qualifications by 375,000 nationally by 2017 with particular focus on Certificate III and higher qualifications and completions by indigenous, disabled, regional and remote students.

1.4 VET reform in other States

States used the flexibility provided under NPASR to implement the reforms in different ways. Progress is summarised in Exhibit 6.

Exhibit 6: Progress of VET reform by jurisdiction between 2007 and 2012

State	Start date	Program	Change between 2007 and 2012*			Non-TAFE % of 2012 spend	Uncapped Entitlement
			Spend	Students	Spend per hour		
Victoria	2008	Victorian Training Guarantee	65%	72%	-22%	41%	Yes
South Australia	2012	Skill for All	-10%	35%	-39%	24%	No
Queensland	2013	Great Skill, Real Opportunities	17%	18%	-12%	19%	No
Western Australia	2014	Future Skills	26%	39%	-6%	20%	No
Tasmania	2014	Skills for Work	4%	7%	-19%	9%	No
New South Wales	2015	Smart and Skilled	5%	6%	-12%	9%	No
Nationally			23%	29%	-18%	23%	

Source: Productivity Commission 2009 and 2014.

Note: * 2012 is the most recent comparative data available.

Victoria started its reforms before the NPASR. In 2008, it introduced an uncapped entitlement for all working-age Victorians to train for one subsidised Certificate III at the RTO of their choice. Victoria has done more than other States to increase VET activity, spending, contestability and student numbers.

By 2012, all subsidised VET in Victoria including higher qualifications was contestable. Victoria made it easy for new RTOs to enter the market, deregulated fees and reduced the per student subsidy to public TAFE Institutes to be more in line with that provided to private RTOs. The VET sector grew rapidly as private RTOs responded to, and stimulated, demand. Victoria was spending an extra \$500 million (65 per cent) to train 290,000 (72 per cent) more students than it had in 2007. Victoria's participation rate was the highest in Australia with 16.1 per cent of adults in training compared to the national average of 11.9 per cent.

By June 2014, private RTOs delivered 57 per cent of subsidised training and those TAFE Institutes that were slow to adapt were in financial difficulties. Five of the 17 TAFE Institutes were at high risk of being financially unsustainable in the short-term and eight were at medium risk.

Victoria is refocusing its reform. It recognises that the growth in VET expenditure was unsustainable and sometimes lacked focus. RTOs shifted costs by attracting State funding for training that employers had previously provided.

Victoria has kept its entitlement uncapped but frequently adjusts the level of subsidy to reduce expenditure, limit over servicing and target spending on areas of job growth and industry need. It has introduced entry barriers and stronger investigative, monitoring and contractual management to address poor quality RTOs. The government has provided TAFE funding to assist structural adjustment. It reduced State VET expenditure by \$111 million in 2013.

Other States have not introduced an uncapped entitlement but have limited the supply of training places. Most increased student fees significantly and restricted the qualifications to be subsidised and the number of subsidised training places.

1.5 VET reform in New South Wales

New South Wales is the last State to implement the entitlement requirement of NPASR.

The Commonwealth agreed to provide up to \$561.6 million of funding over five years. In return, New South Wales agreed to:

- introduce a VET entitlement for entry-level training up to Certificate III
- improve VET quality, efficiency, information and reporting
- ensure access and equity
- support and improve the competitiveness of TAFE
- increase the annual number of people completing post-school qualifications by around 16,000 (14 per cent). This is a less ambitious target than the State's own goal of increasing the proportion of working-aged people with post-school qualifications at Certificate level III and above by 50 per cent by 2020.

In 2012, the New South Wales Minister for Education announced that the Smart and Skilled reform would launch a demand-based entitlement to subsidised training up to a Certificate level III within two years. The government decided that the Department would implement it with no additional funding by restricting the eligible qualifications, and regulating prices and student fees. The financial cap arrangements were announced in 2014.

The other major policy objectives were to:

- ensure TAFE remains a strong and viable public provider of VET by becoming more competitive
- introduce more consumer driven contestability between public and private RTOs
- set a bar for quality so that only the best providers deliver subsidised training
- ensure VET is available across the State and to disadvantaged groups.

The Minister for Education later announced the government would provide separate, transparent funding to TAFE for the:

- delivery of higher qualifications not covered by the Smart and Skilled Entitlement
- higher costs of providing VET to communities that would otherwise miss out. This is referred to as Community Service Obligation (CSO) funding
- higher salary, infrastructure and reporting costs associated with TAFE's public ownership. This is referred to as Operational Base Funding (OBF).

In October 2013, the government delayed the launch of the entitlement until 1 January 2015, to allow time to resolve new funding, governance and legislative arrangements for the transition to a purchaser-provider framework for VET.

The NSW Government:

- separated TAFE from the Department on 1 July 2014 to support contestability and a purchaser-provider approach
- established the NSW Skills Board in November 2013 to oversee the reform of the VET system and to provide independent advice to the Minister for Education.

Within the Department, State Training Services (STS) is the unit responsible for coordinating and managing the VET reform. Prior to the implementation of Smart and Skilled from 2014, the Department focused on regulation of apprenticeships and traineeships and funding and managing priority qualifications. Its expanded responsibilities now include:

- developing and managing a sustainable, contestable market for subsidised VET that is high quality and meets the needs of New South Wales
- acting as secretariat and research arm for the NSW Skills Board.

More details of the chronology of reform in New South Wales are included in Appendix 2.

1.6 What is the audit about?

The audit assessed the effectiveness of the Department of Education and Communities' (the Department) framework for VET reform. We asked whether the Smart and Skilled framework has the potential to achieve the outcomes sought by government to:

- ensure TAFE viability in a competitive market
- strengthen the NSW skills base and remain budget neutral
- introduce a VET entitlement
- provide VET to regions, thin markets and disadvantaged groups.

The audit did not examine:

- the Department's decisions around the allocation of Smart and Skilled contracts to individual training organisations
- public and private RTOs' readiness for the Smart and Skilled reform
- VET that is provided outside of the Smart and Skilled reform including school-based and full fee training
- TAFE reform.

We may comment on these where they affect our findings or to provide context.

Appendix 1 contains more information on the audit objective, scope and focus.

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Key findings

2. The Department's framework for VET reform

Finding: The Department's framework for VET reform has the potential to support the government's immediate outcomes. We found that these outcomes are being addressed in the following order of priority:

- no extra cost (budget neutrality)
- TAFE viability
- quality VET
- access to VET for regions and equity groups
- more contestability
- student choice.

All, except budget neutrality, meet the State's commitments under the National Partnership Agreement on Skills Reform.

The framework involves a series of compromises to meet these not wholly compatible objectives and will introduce a highly regulated market in the first year (2015). More, but not all, publicly subsidised training is contestable by public and private RTOs. This means that the Department funds RTOs according to their performance in enrolling and training students. To avoid additional expenditure, the Department has put a financial limit on the level of training activity an RTO can deliver.

The Department selected these RTOs through a competitive tender process. It supports local training by allocating funding by region and providing extra funding support (paying a loading) to RTOs that train students from regional and remote areas and equity groups. It has set prices for the qualifications on the NSW skills list, which are made up of the government subsidy paid to RTOs and the fee the student pays. It has guaranteed TAFE a share of allocated places and will directly fund TAFE to support its higher cost structure while it adjusts to a more competitive environment. The experiences of other States around cost, quality and the viability of TAFE informed this approach.

The Smart and Skilled reform will fund up to 46,000 more students in 2015 through increased student fee revenue. However, not everyone with a Smart and Skilled 'entitlement' will be able to access a subsidised training place at a particular point in time. New South Wales does not weight the subsidy for training to reflect the relative public value of different qualifications.

The framework does not fully address the overarching government goal of increasing the skills base of the NSW people. The VET reform's budget neutral objective, its pricing structure and the incentives for efficiency mean that it is unlikely to generate the funds needed to meet the State Plan goal to increase the proportion of working-aged people with post-school qualifications at Certificate level III and above by 50 per cent by 2020.

2.1 The policy objectives and the major design features

New South Wales' later implementation of VET reform allowed it draw on the experience of other States. The government opted for a staged implementation in recognition of the experiences of other jurisdictions. It added policy objectives and constraints that focussed on budget neutrality and maintaining TAFE viability. The list of objectives is summarised in Exhibit 7.

To balance these objectives, the Department is making more VET funding contestable in a highly regulated market. It will fund those RTOs chosen by students, but not everyone with an entitlement will get a place or a place at their preferred provider. The Department will restrict spending by allocating a capped number of training places to pre-approved providers chosen for their capacity, capability and performance to deliver quality training. The

Department will regulate prices to ensure budget neutrality, TAFE viability and training quality. It will consider deregulating fees once it has established effective systems to monitor RTO performance. This will be one of the reviews included in its evaluation framework for the Smart and Skilled reform.

Higher fees will fund more places, but the efficiency mechanisms to increase VET activity and achieve the State Plan goal of increasing the population with a post-school qualification by 50 per cent by 2020 rely on the IPART methodology of setting an efficient price for delivery. As the government has not fully implemented the IPART recommendations, the VET reforms will not generate the funds needed to meet this goal.

To the extent an RTO can produce training at a lower cost than TAFE (and the Victorian experience suggests that they will be able to do that to a substantial degree) it will be reflected in higher RTO profits as RTOs cannot change the price or the fee.

Exhibit 7: Smart and Skilled objectives and design response

Objective	Design Response	Constraint on meeting the objective
No extra cost	Limit VET expenditure by allocating funding caps per region per RTO. Increase student fees. Fund the extension of contestable training by reallocating existing TAFE budgets. Adopt new VET Budget and funding model to support effective budget management. Prevent cost-shifting to government as employer based RTOs are ineligible to get funding for training they had previously provided.	TAFE viability – Guarantee TAFE a share of contestable and non-contestable funding and enable it to compete for the remaining contestable funding. Discussed in Section 2.2.
TAFE viability	Allocate a significant share of VET non-contestable funding directly to TAFE for OBF, higher qualifications and CSOs. Base the regulated price on an efficient TAFE and private provider costs. Limit contestability for foundation training to TAFE and ACE.	Consumer driven contestability – reallocate VET funding from TAFE reform efficiencies to the Department so it can purchase more from private RTOs. Discussed in Section 2.3.
Quality VET	Regulate subsidy and fee to avoid price competition. Pre-approve RTOs based on capacity, capability and performance to deliver quality training in NSW. Use quality framework to monitor and improve RTO performance with rigorous quality criteria, enhanced monitoring and reporting, student complaints process and consumer protection. Reorganise STS to support its new role to manage training across the State.	No extra cost. Limited competition and student choice. Discussed in Section 2.2.
Access to VET	Allocate regional caps to address regional needs. Pay a loading to RTOs training regional students. Pay a loading and compensate RTOs that train disadvantaged students for fee concessions and exemptions. Pay CSOs to TAFE and ACE that train in thin markets where there is no other RTO willing to train for the set price.	No extra cost. Discussed in Section 2.4.
More contestability	Fund RTOs for their performance in enrolling and training students. Use allocations to increase the diversity of RTOs in each market and treat Sydney as a single market.	No extra cost – the Department caps the number of subsidised students that an RTO can enrol. TAFE viability – Fixed fees prevent price competition. Discussed in Section 2.2.
The Entitlement and student choice	Provide 2015 'entitlement' for entry-level qualifications <ul style="list-style-type: none"> Qualifications up to Certificate level III All apprenticeships and selected traineeships. 	No extra cost – restrict the number of training places. Discussed in Section 2.5.

Source: Audit Office research 2014.

2.2 More contestability and quality VET at no extra cost

In 2015, the government will reallocate some of TAFE's direct funding to the Department to purchase training from TAFE and private RTOs. The Department is adopting a cautious purchasing approach for the first year. This is consistent with its objectives to increase contestability and quality while maintaining TAFE's role as the major provider at no extra cost.

More of the VET training budget is now contestable. In 2013–14, approximately 11 per cent of the total VET budget of \$2,185.5 million was contestable. In 2014–15, approximately 19 per cent of the total VET budget of \$2,310 million is contestable.

The Department requires public and private RTOs to apply to deliver entitlement training using a common process. This is the first time TAFE Institutes have had to compete for this work.

The Department is not using price to direct funding. Instead, it is allocating subsidised training places through a competitive tender, assessing RTO's organisational capacity and capability, past performance and capacity and capability to deliver particular qualifications in specific regions.

This approach is a reaction to difficulties experienced by other States that opened their training market more quickly. When Victoria introduced VET reform in 2008, it increased competition by reducing barriers to new RTOs and accepting those accredited by the national regulator, the Australian Skills Quality Authority (ASQA). Victoria almost trebled the number of subsidised RTOs from 201 in 2008 to 556 in 2012. It increased VET activity dramatically, but there were widely reported failures. Several high profile RTOs closed, leaving students out of pocket and employer groups complained that the standard of training had fallen. This is not necessarily a quality issue but a normal market reaction to competition and changing economic circumstances. The VET framework should have mechanisms to protect consumers when this happens.

We understand the Department's cautious approach, but it is possible to have high standards without creating a restricted market as New South Wales has done. Having a restricted market is not optimal. Contestability research shows that you need the threat of new entrants to drive the benefits of competition.

ASQA has found that only 20 per cent of RTOs are fully compliant with national training standards. As jurisdictions recognise that ASQA accreditation alone is not an adequate assurance of quality, they are introducing their own quality regimes including pre-qualification systems and contract management. Since 2012, for example, Victoria has introduced comprehensive pre-contract assessment for new applicants and existing RTOs. By 2014, Victoria funded ten per cent fewer RTOs (499) and rejected 19 per cent of new applicants (109).

Victoria also introduced extra safeguards for areas at high risk of poor practice and over-servicing. It only allows a short-list of pre-approved RTOs with documented controls to deliver foundation training and recognition of prior learning.

The Department has developed high-level frameworks for quality and customer services, which are discussed in Section 3.3. However, the Department has a no clear plan for using contestability to drive efficiencies and expand VET activity to meet the State's long-term objectives.

2.3 TAFE viability

The Department will ensure it maintains TAFE as the major provider of training across the State in 2015, by allocating an unspecified share of contestable training places. It will also exclude private RTOs from contesting:

- entitlement funding for foundation courses
- CSO funding
- TAFE's funding for Certificate IV, Diploma and Advanced Diploma courses.

In addition, the government will provide separate non-contestable funding to TAFE for the additional costs arising from its public ownership.

The government continues to provide TAFE with direct non-contestable funding. The budget for this direct funding is not subject to clear purchaser oversight, nor is it clear how long it will continue or what TAFE will deliver for it. In addition, the benefits of the VET reforms depend on achieving the efficiency outcomes of the TAFE reforms. This is discussed in Section 3.2.

2.4 Access to VET

The Department plans to meet the objective of ensuring access to training for regions and disadvantaged groups through:

- allocating RTO caps on a regional basis
- paying a subsidy loading to RTOs that train regional and disadvantaged students
- paying the gap to RTOs that train students eligible for fee concessions and exemptions
- providing additional CSO funding to provide VET that would otherwise not be available.

In determining allocations, the Department ranked RTOs on their capacity to provide quality training by qualification and region. It used Australian Bureau of Statistics (ABS) classifications to define markets in a way that balances regional access with contestability.

The Department has allocated provider caps for rural and remote regions in a way that ensures ongoing access to reliable and quality RTOs that can meet the needs of regional students and employers. The outcome of the Smart and Skilled procurement process is fewer RTOs competing in markets with lower student demand and vice versa. The Department nominated 15 regions for training delivery and is treating Greater Sydney as one region. This could facilitate the rationalisation of metropolitan TAFE as Institutes contest allocations between themselves as well as with private RTOs.

The Department will address thin markets once the initial allocation round identifies them. A thin market is one in which no quality RTO is ready to provide VET at the Skill List price. The Department has developed criteria for deciding which qualifications will classify for CSO thin market funding. In 2015, the government will only provide CSO funding for thin markets to TAFE and ACE Colleges.

Exhibit 8 summarises the approach of other States in ensuring access to subsidised VET.

Exhibit 8: State approaches to ensure access to subsidised VET

State	Regional loading	Disadvantaged loading to RTO	Concessions and fee exemptions for student
Victoria	10% regional	30% low SES background 50% ATSI	20% ATSI above Certificate IV Exemption for young people transitioning from care the justice system
South Australia	10% regional 20 to 40% remote		Free Certificate I and II for welfare recipients and inmates
Queensland	15% regional 75% remote	Cape York and Torres Strait 150%	
Western Australia	10% regional 30 to 155% remote		50% concession for welfare recipients and inmates up to Certificate IV
New South Wales	10% regional 20% remote	ATSI 15% Disability 15% Long term unemployed 10%	Concessions for welfare recipients Exemption for ATSI and disabled students

Source: Audit Office research 2010/4.

The Department's allocation of training places by region should ensure training is available across the State, if RTOs are willing to provide it at the Skills List price. The regional and disadvantaged loadings will ensure disadvantaged groups can get access to VET. However, the government's approach to fee setting has constrained access for non-disadvantaged groups. As the student fee component has been set at a lower rate than IPART recommended, less funds are available for training places.

2.5 The entitlement and student choice

In 2015, the Department will increase the proportion of VET funding which is contestable and follows student choice. This is not a fully demand-driven entitlement because the Department will restrict the number of subsidised places each RTO can offer to limit government expenditure.

From 1 January 2015, the Department will introduce an entitlement for people 15 years and over who have left school, do not have a higher qualification and live or work in New South Wales. The entitlement allows them to choose subsidised training for approved qualifications up to and including Certificate level III from an approved RTO. The Department will set the RTO's price consisting of the subsidy and the student fee (see Exhibit 12) and pay RTOs according to the number of students they enrol and train.

The Department will continue to subsidise other training, particularly higher training through the Targeted Priorities Program as part of the Smart and Skilled reform. It will use a single framework for both the entitlement and the Targeted Priority Program to identify which skills to subsidise, set prices, choose RTOs, monitor performance and make payments. The Targeted Priorities Program supports training in priority areas outside of the entitlement. This includes full qualifications at Certificate IV to Advanced Diploma as well as pre-vocational and part qualifications as identified on the 2015 NSW Skills List.

Exhibit 9 shows the qualifications covered by the two programs and which RTOs can deliver them.

Exhibit 9: Smart and Skilled programs

Entitlement Program		Targeted Priorities Program	
Qualifications	Eligible RTOs	Qualifications	Eligible RTOs
Certificate levels II and III	All RTOs, except enterprise based RTOs	Certificate level IV and above	Private RTOs and ACE except enterprise based RTOs and TAFE*
Foundation Courses – Certificate levels I and II	TAFE and ACE	Prevocational and part qualifications	All RTOs except enterprise based RTOs
Apprenticeships and Traineeships	All RTOs	Note: *TAFE receives direct funding to provide subsidised Certificate level IV, Diploma and Advanced Diploma training.	

Source: The Department of Education and Communities 2014.

In October 2014, the Department allocated the subsidised training places to approved RTOs by region to ensure access to training across the State. An RTO can use its entitlement allocation to enrol students in any course it has Department approval to provide in the region. This allows RTOs some flexibility in providing training that gives them the best return. An RTO must fill Targeted Priority Program allocations by enrolling students for the targeted qualifications.

Exhibit 10 shows that several States have capped their 'entitlement' to control VET expenditure.

Exhibit 10: Approaches to controlling VET expenditure

State	Entitlement Caps	Other budget control mechanisms
Victoria	Uncapped entitlement	Reduce subsidies for courses that can be provided on a full fee basis or that are of marginal value to the State
South Australia	Qualification caps – RTOs advised not to enrol new students once enrolment limits reached	Reduce subsidies and uses Skills list
Queensland	Uncapped entitlement of one Certificate III per person; Other training places capped	No subsidies for most qualifications above Certificate IV
Western Australia	Qualification caps – RTOs advised not to enrol new students once enrolments exceed workforce requirements	
New South Wales	Provider funding caps – the Department has set funding caps for each contracted provider. They have the flexibility to manage student enrolment numbers within their allocated funding caps.	NSW Skills List

Source: Audit Office research 2014.

Victoria is the only State with a fully uncapped entitlement. This increased training levels as RTOs met latent, and stimulated new, demand. VET activity increased by 72 per cent and government spending by 65 per cent. By 2012, Victoria recognised that some training was providing little value for money and it is reducing the subsidy for qualifications of marginal value to the State. For example, Victoria reduced the subsidy for personal fitness coaches to \$1.00 per training hour after it had funded a 3,000 per cent increase in the number of people with this Diploma.

The other States cap the number of subsidised students who can enrol in a qualification. This encourages RTOs to enrol as many students as quickly as possible. When the caps are over-subscribed, they tell RTOs not to enrol new students. For example, South Australia stopped new enrolments for 19 qualifications and cut the subsidies of many more by up to half within six weeks of introducing the entitlement.

The decision to cap the allocation of subsidised training places that each RTO can offer should meet the objective of no added cost. However, this means that not every student who is entitled to a subsidised training place will be able to access one at a particular point in time.

2.6 VET activity against State needs

The Department will only subsidise training that is valuable to the State's economy and wants to avoid funding training that students are prepared to pay for on a commercial basis. This is consistent with the approach of most other jurisdictions. Victoria and South Australia have found that ongoing market monitoring is required to address distortions and gaming in the VET sector.

Since 2012, the Department has conducted labour market analysis and industry consultations to determine which of the 1,623 nationally recognised qualifications to subsidise within the scope of the Smart and Skilled reform. These qualifications form the NSW Skill List which currently contains 743 qualifications, including all apprenticeships. The Department's criteria for prioritising qualifications include industry demand, skill shortages, job prospects and NSW Government priorities. The List excludes 880 qualifications that are of lesser value to the State or adequately provided without government assistance. Employer RTOs are only eligible for subsidies for apprenticeships and selected traineeships.

Most States use a similar list to restrict the qualifications that attract subsidies. Queensland is the most tightly targeted with around 300 qualifications while South Australia has nearly 900.

Exhibit 11: The number of subsidised skills in different jurisdictions

Jurisdiction	Number of subsidised skills	Other mechanisms
Victoria	3,088	Adjust subsidy to reflect value to State
South Australia	864	
Queensland	c.300	Adjust subsidy to reflect value to State
Western Australia	> 600	Adjust subsidy to reflect value to State
New South Wales	743	Annual review of Skills List

Source: Audit Office research 2014.

Victoria is more market-oriented and subsidises the training chosen by employers and students, including part-qualifications and units of competency. This contributed to the large increase in VET expenditure as RTOs attracted subsidies for training that had previously been full fee or provided by employers.

Since 2012, Victoria has sought to address cost-shifting and gaming by RTOs through pricing signals rather than restricting which skills it will subsidise.

New South Wales does not weight the subsidy for training to reflect relative public value of different qualifications, which may result in VET activity that does not meet State needs.

2.7 Pricing

The Department based the 2015 training price on what it cost TAFE and private providers to deliver training. This appears appropriate to address the objectives of quality and TAFE viability in the first year of reform, given the disruption experienced by other States. However, we have concerns about the Department's readiness to adjust price where providers in the market do not respond to price settings and allocations in a way that meets NSW training priorities. The Department plans to review the basis of pricing and the deregulation of fees during 2016.

The Department publishes prices for each qualification on the Skills List, based on 2013 IPART advice about the efficient cost of delivering training. The price reflects current modes of TAFE training, not alternative modes of delivery. It considers the duration of training, the level of qualification and the resources and hours required according to the national training standards. For example, it costs less to teach theory to a class than to teach practical skills in a workshop, where each student needs to operate industrial equipment safely.

IPART based the efficient price on 2012 costs of TAFE and private RTOs (from the Strategic Skills Program tender process) and did not include the additional TAFE salary, infrastructure and reporting costs associated with being publicly owned.

In 2015, NSW prices will range from \$1,520 for a prevocational Certificate level I to \$28,200 for a Diploma of Mechanical Aeroskills. Unlike other States, the price is for the qualification as a whole, rather than an hour of training, a subject or a unit of competency. This provides more certainty for students who will know their total fees when they enrol. RTOs must have a policy on the number of times a student can attempt to complete a unit of competency for their student fee.

The Department has divided the price paid to the RTO into two components, the government subsidy and the student fee.

Exhibit 12: Qualification price



Source: NSW Skills Board 2014.

The government received advice from IPART that the fee component should reflect the respective benefits that students and the State derive from training. The government partially adopted this advice with a lower fee component than recommended by IPART. The fee component is larger for higher qualifications and subsequent qualifications. The Department plans that the increased fees will fund 46,000 more enrolments and enable it to exceed the National Partnership Agreement target of 16,000 extra completions a year.

The price and fee structure for Smart and Skilled will be the same for all providers and replace the previous system where there were different models of pricing for TAFE, private RTOs and apprenticeships and traineeships. In order to provide RTOs with the flexibility to compete and innovate, IPART recommended that the fees should be defined as a maximum and allow RTOs to charge up to 50 per cent less. This was not supported by the government.

Exhibit 13 shows how the various States price training. Like New South Wales, Western Australia fixes fees to avoid the potentially negative effect of price competition on quality, efficiency and TAFE enrolments. In contrast, Victoria, South Australia and Queensland allow RTOs to set fees and compete for student enrolments on price. This increased contestability has caused volatility in their training markets and Victoria and South Australia adjust their subsidies frequently.

Exhibit 13: Jurisdictional approaches to VET pricing

State	Basis	Student fee	Review	Extra TAFE support
Victoria	Hourly rate based on market forces and value to State	Set by RTO	Active market monitoring can change subsidy at short notice	Higher hourly rate for TAFE until 2012
South Australia	Hourly cost adjusted for budget constraints	Set by RTO*	Active budget monitoring – eight subsidy changes in two years	Higher hourly rate for TAFE
Queensland	Cost of delivering course adjusted for value to State	Set by RTO* **	Annual	
Western Australia	Hourly cost adjusted for State need	Fixed	Annual	Higher hourly rate for TAFE
New South Wales	Efficient course cost	Fixed	Annual	Same hourly rate but separate direct funding for OBF and CSOs

Source: Audit Office of NSW research 2014.

Notes: *some priority courses and students fee free

**except for apprenticeships and traineeships.

New South Wales is the only State to base its subsidy on the cost of training alone. The others now all factor in the value of the training to industry and the State. Victoria has gone the furthest in targeting funding to maximise value to the State, industry and students.

Victoria changed its pricing from a cost to value basis in 2012. As Exhibit 14 shows, it pays RTOs more to deliver courses that address skill shortages or that help people enter the workforce and less for courses where there is already an adequate supply of training. The two right-hand columns show that these clearer price signals resulted in a shift from Bands D and E (least value) to A and B (greater public value), which jumped from 49 per cent to 69 per cent in 2013.

Exhibit 14: Victoria's public value pricing

Band (examples)	Subsidy per hour of training	Number of courses	Pre-band enrolments 2012	Post-band enrolments 2013
A – (apprenticeships)	>\$10	193	8%	12%
B – (foundation skills, Cert III aged care)	\$7.50 to \$10	345	41%	57%
C – (Diploma of Children Services)	\$5 to \$7	334	20%	22%
D – (Diploma of Events)	\$2 to \$4.50	154	10%	5%
E – (Diploma of Fitness)	< \$2	30	21%	4%

Source: Victorian Department of Education and Early Childhood Development 2014.

Exhibit 15 shows that in New South Wales the price (fee plus subsidy) and the proportion borne by the student rises as the level of qualification rises. In contrast, Victoria varies the subsidy according to a balance between public and private value.

Exhibit 15: Examples of pricing in NSW and Victoria

Qualification	Occupation	Duration (F/T)	NSW student fee	NSW subsidy	Victorian subsidy
Cert I – General Education for Adults	Foundation (not occupation specific)	Up to 1 yr	\$220	\$2,740	\$3,360
Cert II Music	Sound technician	Up to 1 yr	\$870	\$1,880	\$2,568
Cert III Sport and Recreation	Recreation assistant	Up to 2 yrs	\$1,440	\$3,320	\$872
Cert IV Screen and Media	Camera operator	Up to 2 yrs	\$1,960	\$5,230	\$8,652
Diploma of Accounting	Senior accountant	Up to 2 yrs	\$2,510	\$4,060	\$2,610
Advanced Diploma of Management	Regional manager	Up to 2 yrs	\$2,560	\$4,200	\$1,140

Source: NSW and Victoria Skills List 2014. New South Wales Audit Office analysis 2014.

Note: The NSW subsidies are based on the student undertaking a first post-school qualification. Victoria does not regulate the student fee; we calculated the Victorian subsidy by multiplying their hourly rate by the maximum hours for the qualification.

Given the concerns about poor training quality and TAFE viability associated with the introduction of price competition in other States, it is appropriate that the Department fixes fees in 2015 while it establishes systems to monitor training quality and performance. In 2016, the Department intends to review the approach to pricing and the deregulation of fees. This review should consider whether the price should reflect public value and needs to be informed by better cost data collected throughout 2015 to assess the impact of competition in the VET market.

Recommendation

To inform the 2016 review of VET pricing, during 2015 the Department of Education and Communities should:

- collect robust data on the cost of training delivery
- assess whether qualification pricing should be weighted to reflect public value
- assess the impact of the partial implementation of the 2013 IPART recommendations on pricing for VET in relation to the efficient price for student fees and the decision not to define the fee as a maximum and allow RTOs to charge up to 50 per cent less.

3. The roles and responsibilities of funder, purchaser and providers

Finding: The government has not yet fully defined the roles and responsibilities of funder, purchaser and provider.

Parliament has established the NSW Skills Board to support the funder, the Minister for Education, with advice and oversight of government-funded training. It is unclear whether the NSW Skills Board has adequate resources to meet its statutory responsibilities.

The separation of the purchaser (the Department) and the provider (TAFE) is incomplete. State Training Services (STS) is the Department's unit responsible for VET. Its role in planning for TAFE's non-contestable direct funding is ambiguous. This funding includes most of the State's support for higher-level training as well as TAFE's additional costs as public provider. TAFE's separation from the Department on 1 July 2014 created the current ambiguity over accountability for TAFE's direct funding.

Because the national regulator, the Australian Skills Quality Authority (ASQA), cannot ensure training quality by itself, the Department will need strong controls to ensure RTO performance and training quality. The Department has developed high-level frameworks for quality and customer service. It has also proposed a new organisational structure for its head office. These initiatives have the potential to support its expanded responsibilities: strategic planning; labour market analysis; monitoring of the training market; contract management; reviewing, supporting and funding RTO performance; and informing the choice and protecting the interests of students.

The Department advised that it had developed the required capabilities to take up all of these new roles, and these were in place for the 1 January 2015 commencement of Smart and Skilled.

3.1 Oversight of the sector and VET reform

The Minister for Education is the funder of VET. Together with Cabinet, he made the key decisions for Smart and Skilled, including the design of the reform and policy objectives, the budget, funding arrangements and pricing models.

During the initial policy development, the Skills Reform Reference Group advised Cabinet on options, funding models and coordination with the national VET reform framework. This inter-agency group comprised representatives of the Department, NSW Treasury and the Department of Premier and Cabinet. It has also been involved in subsequent work on VET policy design and review.

In late 2013, legislation was enacted to establish the NSW Skills Board to provide the Minister for Education with independent strategic advice on VET reform and funding. Its Act requires the NSW Skills Board to:

- oversee the reform and its implementation, including quality assurance and the maintenance of TAFE as the major provider of VET accessible across the State
- monitor and advise the Minister for Education on the performance of the VET system, including the level of training activity, financial performance and sustainability, achievement of State priorities and allocation of funding
- analyse skills shortages and coordinate the development of strategic skills plans for the State
- ensure the appropriate consumer protection and the availability of accurate consumer information.

The NSW Skills Board relies on the Department for regular reports on key reform policy and implementation, its secretariat and advice. It has reviewed and advised the Minister for Education on the Skills List, the pricing of qualifications and the Department's methodology

for allocating subsidised training places. The Board is commissioning a high-level plan to identify training priorities for 2015–17. It anticipates developing its broader oversight role for VET reform as a whole, as envisaged in its mandate, over the coming years. At this stage, the Minister for Education has not asked or resourced the Board to oversight TAFE's non-contestable funding.

Other States have similar Boards. Those that have been implementing the reforms for longer, are reviewing the extent to which they have sufficient independence, resourcing and advice to fulfil their oversight responsibilities. We suggest that the Department do the same in New South Wales.

Recommendation

By July 2015, the Department of Education and Communities should ensure that the NSW Skills Board has adequate resources to meet its statutory responsibility to provide oversight of the reform and independent strategic advice to the Minister for Education.

3.2 The separation of purchaser and provider

The NSW Government's goal is to introduce a transparent, flexible and competitively neutral VET system. To achieve this, it separated the roles of purchaser and provider.

The government removed TAFE from the Department's Executive in 2013 and established TAFE as a distinct financial entity in July 2014.

As the public provider, TAFE is responsible for delivering training that meets the State's skill priorities and delivers better outcomes for students. The government expects TAFE to continue to be the major provider of training in New South Wales by becoming more responsive, flexible and autonomous. From 2015, TAFE will have to compete for a share of the subsidised VET market.

As purchaser, the Department, through STS, is responsible for developing, designing and managing the market, achieving value for money and meeting State targets. Smart and Skilled is a new model for VET funding as a whole, not simply the entitlement program.

However, the separation of purchaser and provider is not complete. In 2014–15, the government will pay a significant portion of the \$2,310 million VET budget directly to TAFE for:

- operational base funding (OBF) for the additional costs arising from TAFE's public ownership such as salary and working arrangements, reporting requirements and heritage assets. The Minister for Education will adjust the OBF as circumstances change
- community service obligations (CSO) funding to deliver support services for Aboriginal and disabled students and outreach services. The Minister for Education has announced that CSOs may become contestable over time
- directly purchased pre-vocational training, skill sets and full qualifications above Certificate III, school based training, school-equivalent education and specific training programs to respond to community emergencies and industry restructuring. This funding will be reviewed in 2016.

The Minister for Education expects the Department and TAFE to negotiate what this non-contestable funding will achieve and for TAFE to regularly report on specific deliverables to the Department. The agencies had not resolved the negotiations or agreed to a memorandum of understanding at November 2014. A cause of the delay appears to be that the agencies and Treasury had not finalised the allocation of the 2014–15 budget or future estimates for VET.

The direct funding of TAFE creates ambiguity around the capacity and authority of the Department to plan and manage the VET sector as a whole. For example, TAFE will be directly funded to provide around 85 per cent of subsidised Certificate level IV and Diploma training. Since TAFE's separation from the Department on 1 July 2014, the Department is yet to determine the accountability arrangements for TAFE's direct funding.

Recommendation

By April 2015, the Department of Education and Communities should finalise accountability arrangements for TAFE's non-contestable funding and specify what it expects each TAFE Institute to provide and report on for its direct funding.

3.3 Purchaser's role

The Department is responsible for policy development, market design, purchasing, quality assurance, performance monitoring, funding and budget management. This is a major change for the responsible unit within the Department, State Training Services (STS).

Until 2014, the Department managed the State's \$248 million training market focused on regulating apprenticeships and traineeships, and purchasing priority qualifications. From 2015, the Department will have a significantly expanded budget and responsibilities. For the first time it will monitor the performance and quality of training delivery by TAFE Institutes as well as private RTOs. The Department has put in place the systems, tools, processes and trained team ready to implement the reform.

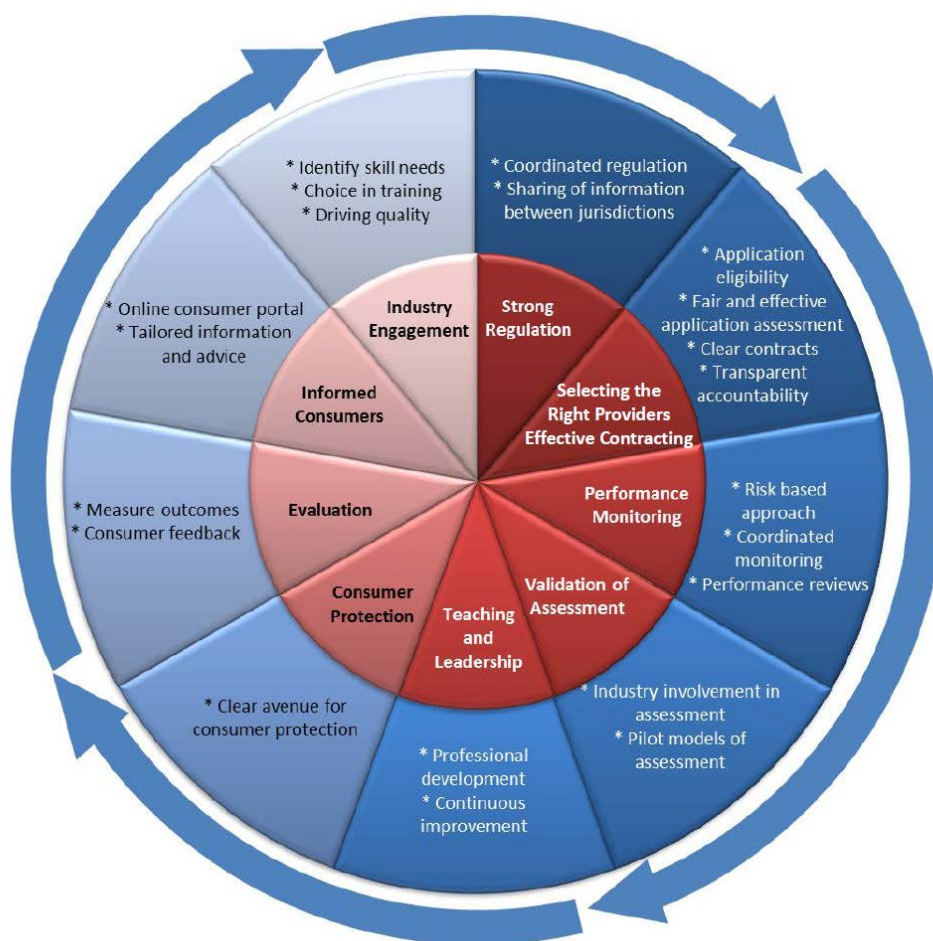
The Department has designed high-level quality and customer service frameworks to support its new roles. These frameworks have considered the experience of other States and the limited assurance of the national regulator. The Victorian and South Australian experience shows the need for strong oversight, contract management and quality assurance systems to ensure quality when introducing contestability.

Since 2012, Victoria has built up its contract compliance program. In 2013–14, it conducted 71 audits of RTOs focused on areas of high risk. At 30 June 2014, it was withholding \$25 million in payments, investigating 15 complaints and actively case-managing 20 RTOs to address inappropriate behaviours. In October 2014, it withheld a further \$20 million from one of the larger RTOs that was providing sub-standard training through sub-contracted providers. At the same time, Victoria reduced red tape for high quality providers by offering three-year contracts to RTOs with a strong record of contract performance and financial health. This provides quality RTOs with greater certainty and avoids the cost of annual contracting.

The national regulator, ASQA, has only 204 staff, including five investigators, to monitor the compliance of around 5,000 RTOs with national standards. Four out of five RTOs reviewed by ASQA in 2013–14 had misleading marketing, offered courses with unrealistically short duration or did not comply with standards around student assessment.

Exhibit 16 shows the NSW Quality Framework.

Exhibit 16: NSW Quality Framework



Source: The Department of Education and Communities 2014.

The Department has established protocols and regularly exchanges information with ASQA to ensure they provide **coordinated regulation** supporting each other in their respective roles of regulator and purchaser.

It has established controls to **select**, and **contract with the right providers** which are chosen on the basis of capacity, capability, past performance and ability to deliver specific qualifications. RTOs are able to sub-contract training to third parties, subject to approval. The contracts have clear requirements, performance standards and sanctions.

The Department is developing policies and implementation plans for the other seven principles of the NSW Quality Framework. At November 2014, the Department had issued policies on **consumer protection** and **teaching and leadership**. It conducted three pilots that used independent validation to improve RTO **assessment** of students. The results were mixed, especially in highly competitive training sectors where there was a lack of trust between RTOs and a reluctance to share assessment resources.

The major priority is to develop effective **monitoring**, oversight and **evaluation** systems to manage the increased contestability. Contestability is intended to harness the profit motive to produce innovation, improved service delivery, efficiency and public benefit. RTOs will seek to maximise revenues by meeting and stimulating demand. Fixed prices set by government will skew VET provision if they cease to reflect public value. RTOs will also bias provision to those areas which are most profitable. Where prices are fixed and allocation is done by queues, this can lead to significant distortions, particularly for providers with expensive cost structures. Even private RTOs with a history of profitable delivery have been hard hit by the disruptive impact of changes to government subsidies.

The Victorian Department of Education and Early Childhood Development told the Department to be ready to respond to sudden shifts in the contestable market. Victoria established a new unit in 2012, assisted by independent advisors, to monitor training trends to inform price adjustments, further reform and specific interventions. Exhibit 17 provides two examples of where Victoria intervened to protect the value of public investment in training.

Exhibit 17: Examples of ensuring public value

Recognition of Prior Learning (RPL)

A student who has acquired skills through prior training or work can have these assessed and counted towards a qualification. This is cost-effective, efficient and consistent with national skills reform and the State's goal of more people with post-school qualifications. Governments pay the RTO assessing the student's competency a proportion of the subsidy for the qualification. This can be profitable as the RTO doesn't incur the cost of training. It can also be exploited.

Victoria experienced a large rise in low quality RPL. It responded by tightening up RPL. Only one in seven of its providers can offer subsidised RPL. They must be pre-approved after demonstrating they provide quality assessment. Victoria has also reduced the RPL subsidy to 25 per cent of the course subsidy.

In New South Wales any RTO that is a Smart and Skilled provider can offer subsidised RPL and earns 50 per cent of the course subsidy.

Over-servicing

In an ideal market, well-informed consumers drive demand through their choice of providers. Practice shows that providers can drive demand too. In 2013, Victoria experienced a large increase in foundation training. Monitoring indicated that RTOs, including TAFE, were bundling foundation training with other qualifications to maximise their subsidies. Victoria responded by restricting foundation training to RTOs that assessed the individual's need for such training before enrolment.

Source: Audit Office research 2014.

The Department is developing systems with the potential to avoid the issues with training quality and value experienced by Victoria. It is developing monthly reporting of VET activity to keep it informed of trends and anomalies in the delivery of training.

As seen above, it has taken other States several years to build the capacity to provide oversight. The Department advised that it had developed the required capabilities to assume all of the new roles, and these were to be in place at the 1 January 2015 commencement of Smart and Skilled. However, the Department has not yet reviewed the structure of its regions that have over 300 staff who will be responsible for contract and performance management.

A key role of the purchaser should be to facilitate the development of the supply market. However, this is not in the list of functions for STS. We think this should be a focus for the Department going forward.

Recommendation

By April 2015, the Department of Education and Communities should expedite State Training Services' training and reorganisation to ensure its people have the capabilities to monitor and regulate training, protect students and ensure value for money.

4. The Department's systems to capture and communicate information to manage and regulate VET in 2015

Finding: The Department is progressing well in developing systems and information needed to manage and regulate the training market in 2015. To achieve the 1 January 2015 launch of Smart and Skilled, the Department prioritised critical tasks to allocate training places, take enrolments; and report on, and pay for, training activity. It has deferred other tasks until later in 2015.

This prioritisation was necessary for the Department to manage the high level of uncertainty around some parts of the design of the policy reform and the allocation of the budget between TAFE and the Department.

At November 2014, the Department appears on track to deliver the essential systems needed by 1 January 2015. It allocated training places to RTOs that met assessment criteria while maintaining TAFE as the major provider. Students are currently searching the Smart and Skilled website and enrolling with RTOs of their choice, but have limited information about the providers' comparative quality. The Department plans to publish information on provider performance by mid-2015.

The Department will require RTOs to report on their training activity every month. The Department will use this data to generate payments and monitor performance. Over time, it will include information about relative RTO performance on its website to inform student choice. This will include completion rates and student and employer satisfaction.

As part of the Smart and Skilled reform tender process, the Department gave RTOs useful information on the new market scope and eligibility categories for the Smart and Skilled programs. The Department advised that RTOs were also informed of the government's priorities and fully briefed on the tender assessment methodology on how allocations would be made across programs, qualifications and regions. However, RTOs were not informed about how much funding was available or how the Department would distribute it across qualifications and regions. Providing this information would improve transparency and is more likely to maximise public value, which is consistent with effective commissioning practice.

The Department's plan to publicly report on the State of VET every six months is encouraging. The Department should include reporting on: the realisation of benefits from the reform; trend data on training activity by provider and region to identify gaps in delivery; progress against NSW 2021 goals; the cost of providing training; and TAFE's performance in respect of its non-contestable funding.

4.1 Critical training information and systems

The Department is progressing well in developing the systems and information it needs to manage and regulate the training market in 2015. The main areas of concern relate to the lack of information about:

- performance indicators or a plan for benefits realisation to drive more efficient use of government funding
- the cost of training to inform pricing decisions
- RTO quality to inform student choice
- the allocation of funding to inform RTO planning and innovation
- efficiency and non-contestable funding to inform public accountability.

The Smart and Skilled reform changes the way the government funds training and RTOs compete for funding. All of these require information and systems to plan, manage and inform the new market. Exhibit 18 lists what is required to support the reform and its status: in place (Y), in development (D) and confidential (C). To assess the adequacy of the information and systems, this chapter then examines whether the Department:

- has the information and systems it needs to manage and regulate training
- communicates the information that students and RTOs need to effectively participate in the market and stakeholders need to assess the progress of the reform.

Exhibit 18: Status of critical information and systems to support the reform

The Department's proposed systems	Status	Comment
Planning		
Consultation and industry engagement	Y	None
Smart and Skilled strategy	Y	
Business case – costs, benefits	–	
Funding and budget model to support purchaser-provider model	Y and C	
Identify skill needs – Skills List and Prices	Y	
Market and entitlement design	Y	
Implementation plan – systems development and change management	Y	
Risk management	Y	To be developed – see 5.4
State Training Plan	–	
Budgets for qualifications and regions	Y and C	
Allocation of training places		
On-line tendering and allocation	Y and C	RTOs applied without information about funding
Contracts	Y	Due in 2015
Thin markets	D	
Enrolments		
Students search for provider and course	Y	Students enrol without detailed comparative information about RTO quality, such as graduate employment outcomes and student feedback
Calculate eligibility, subsidy and fee	Y	
Enrol against RTO allocation	Y	
Management		
Adjusting allocations and budgets	D	Due in June 2015
e-reporting VET activity and e-payments	D	Due in February 2015
Quality and performance monitoring	D	Due in 2015
Consumer protection	D	Due in 2015
Public reporting	D	Due in July 2015
Evaluation		
Public accountability and evaluation	D	Due in 2015
Continuous improvement	D	Due in 2015

Source: Audit Office research 2014.

4.2 Information and systems for managing and regulating training

Planning

The Department consulted industry and the community extensively and undertook training and labour market analysis to design the entitlement and reform strategy. As discussed above, the funding and budget model relied on information about the cost of training delivery provided to IPART for its VET pricing review.

While addressing the immediate government objectives associated with implementing NPASR at no extra cost and maintaining TAFE as the major training provider, the government has put less focus on increased contestability and student choice. Overall, it is the latter which are more likely to maximise the public value for the government's investment in VET.

The Department has used suitable management controls to ensure that the Smart and Skilled reform commenced on its revised 1 January 2015 launch date. Unlike other jurisdictions, New South Wales requires gateway reviews only for capital works, not for services such as the Smart and Skilled reform. The Department needs to develop a benefit realisation plan including baseline measures to monitor and report on achievements.

The Department has risk management systems to identify threats to the reform project. These have been significant throughout the project. Reviewers raised concerns between July 2013 and September 2014 that the Department had not integrated the systems and technology required to support the reform. They were more complex than conceived and the Department had not fully defined what the various systems were to achieve from end to end. This situation arose partly because policy settings and design requirements kept changing. Most significantly, the government adopted a new funding model in October 2013 that required TAFE to contest entitlement funding. This greatly expanded the scope and scale of the reform. The Department had to redesign its systems for selecting, managing and funding RTOs to include TAFE.

Subsequent ministerial decisions determined how the Department would allocate training places to balance the objectives of increased contestability while maintaining TAFE as the major provider. Negotiations between the Department and TAFE about their separation affected the design of systems for TAFE applications, activity reporting and payment. Uncertainty around budget allocations and reporting arrangements was unresolved at November 2014. The Department advised that it had to keep much of the detail confidential because it reflected unannounced decisions. The unreleased details include the size and shape of the contestable market and the budgets for TAFE and regional training.

The fluidity of the design requirements resulted in the Department designing, building and testing the systems concurrently on a 'just in time' basis. The Department is working to very tight timeframes, prioritising critical tasks and deferring others to achieve the 1 January 2015 launch of the entitlement.

Recommendation

By July 2015, the Department of Education and Communities should publish a benefits realisation plan so it can monitor and review its progress in reforming the VET sector.

Implementation status at early November 2014

The Department finalised an end-to-end project plan to manage the information systems needed for a January 2015 launch of the reform in September 2014. An independent review by the Office of Finance and Services at that time found Smart and Skilled should be ready for the January 2015 launch.

At November 2014, the Department had assessed applications from 747 RTOs and offered contracts to 346 that met its assessment criteria while maintaining TAFE as the major provider. The Department engaged an independent probity adviser to provide assurance about the fairness of the process.

Three hundred and thirty eight of the 346 RTOs that were offered allocations accepted contracts to provide subsidised training in 2015. Students are currently searching the Smart and Skilled website for courses and enrolling with the provider of their choice. Each enrolment makes a commitment against the RTO's allocation of financial caps.

The Department will develop strategies to manage thin markets identified through the letting of contracts. It defines a thin market as one in which no RTO wants to train in the region at the Skills List price.

The Department is building systems for reporting and payment. It will require RTOs to report their VET activity by student each month. It will pay RTOs for student progress in three to seven instalments depending on the length of the course.

The Department is currently designing systems for performance monitoring, contract management, complaints handling, consumer protection and evaluation. It will reallocate training places that students have not taken up to other RTOs.

The Department clarified how it will handle student churn and attrition through the Smart and Skilled Fee Policy. RTOs can enrol both subsidised and full-fee students. The Smart and Skilled contract terms and conditions prevent RTOs from filling a vacated subsidised place with a full-fee student enrolment.

4.3 Training information for students, RTOs and stakeholders

Information for students

Students need good information to choose the training that is right for them. The Smart and Skilled website currently gives them information about the entitlement, their eligibility and consumer protection. It also has information on each subsidised qualification including:

- description of the qualification
- student fees (including concessions and exemptions) and the availability of student loans
- which RTOs deliver that qualification and details about how, when and where they do so.

The Department plans to add information about RTO quality in 2016 by publishing their completion and satisfaction rates derived from VET activity reports and student and employer surveys respectively. At present, the website gives students no information that would allow them to differentiate RTO quality, even though it was the key criteria that the Department used to allocate training places.

Unlike its Victorian equivalent, the Smart and Skilled website does not give students searching for courses accessible information about job prospects and the demand for particular qualifications.

Recommendation

By April 2015, the Department of Education and Communities should add information about the demand for qualifications on the Smart and Skilled website for students looking for courses.

Information for RTOs

RTOs were informed of the government priorities and fully briefed on the tender assessment methodology on how allocations would be made across programs, qualifications and regions. However, RTOs were not informed about how much funding was available or how the Department would distribute it across qualifications and regions. The Department advised RTOs it would allocate places on the basis of demonstrated training quality and capacity, but did not explain how it would determine the size of the allocations. Successful and unsuccessful RTOs could request and receive detailed feedback on their applications. The Department has made a commitment to increase the information made to RTOs in future allocation rounds.

The lack of information around the available budget restricts RTO's ability to offer more effective and innovative training delivery. Providing this information would improve transparency and is more likely to maximise public value, which is consistent with effective commissioning practice. Other States give RTOs more information about their plans for future VET expenditure. This is discussed in Section 5.4.

Public reporting

The Department has developed a template for six-monthly public reporting of VET in 2015, which draws on the experience and reports of Victorian and South Australian Education authorities. This is a good start. Exhibit 19 summarises the main elements of the proposed report with our suggestions for improvement.

Exhibit 19: The Department's template for six-monthly public reporting on VET reform

Theme	Proposed information	Audit suggestions
Introduction	Overview of Smart and Skilled reform	
Highlights	Key achievements in period	Develop and report against benefits realisation plan
Increase participation in training	Commencements and enrolments by qualification level and provider type (TAFE, ACE, private RTOs)	Set targets and report trend information
Improve access for disadvantaged learners	Commencements and enrolments by qualification level by equity groups (Aboriginal, disabled, and long-term unemployed students)	Report by provider type
Improve access for regions	Commencements and enrolments by qualification level and type of region, that is metropolitan and non-metropolitan	Report by region and provider type to identify gaps in access to training
Meeting industry needs	Commencements and enrolments by qualification level by industry Commencements and enrolments by occupation in critical skills shortage area Top ten qualifications/areas in commencements and enrolments Commencements and enrolments for domestic full fee TAFE training Qualification attainment by AQF level by equity group, by region and skills shortage occupation	Include private full fee training from National Total VET Activity reporting Report against NSW 2021 targets
Community Service Obligations (CSOs)	Commencements and enrolments supported by CSO funding for thin markets by provider type CSO expenditure for thin markets CSO expenditure on disadvantaged students (loadings to subsidies and fee concessions and exemptions)	Report by qualification level and region and equity group Report by region and equity group

Theme	Proposed information	Audit suggestions
Quality Training	Number of RTO applications that are approved, refused and withdrawn. Number of complaints and referrals	Number of RTOs audited and investigated and the names of those suspended by the Department Number and names of RTOs that the Department is actively performance managing Value of VET expenditure withheld and recovered by the Department Graduate employment outcomes Student and employer feedback

Source: The Department of Education and Communities 2014.

The Department has indicated that it will include initial trend data by July 2015 on training activity. The rationale of the report is to tell the public how the reform is affecting training in New South Wales and should provide trend data where possible.

Where possible the Department should report training activity and outcomes:

- by provider type and region to identify gaps and changes in VET provision
- including private full fee training (as full VET activity reporting is implemented) to identify where government subsidies are not needed and could be better targeted
- against NSW 2021 targets.

The proposed report does not include references to efficiency gains or analysis of VET cost structures. Purchasers need good information about the cost of delivery to get value for money. The Department needs to get better cost information before it reviews the pricing framework in 2016. A possible solution would be to introduce 'open-book' approach to costs in its future rounds of Smart and Skilled applications. This approach is described by the UK National Audit Office report *Deciding prices in public services markets: principles for value for money*.

Exhibit 20: An open book approach to costs

A UK authority purchasing aged care commissioned a third party to act as 'honest broker' and formed a provider representative group including large and small care operators. The honest broker did not identify individual providers or only disclosed anonymised cost data. The third party used weighted averages and excluded statistical outliers to estimate the true costs of provision. This helped providers to improve their efficiency and delivered savings to the authority.

Source: UK National Audit Office 2014.

Recommendation

By July 2015, the Department of Education and Communities should establish six-monthly public reporting metrics and publish initial data and information on:

- trends in training activity by provider type, industry, equity group and region to identify gaps and changes in VET delivery
- progress against NSW 2021 targets
- RTO quality indicators, such as graduate employment outcomes and student and employer feedback
- trends in efficiency gains and the cost of delivery
- what TAFE provided for its non-contestable funding.

5. The Department's plans to contribute to the government's long-term training outcomes

Finding: The Department is on track to meet its obligations under the National Partnership Agreement on Skills Reform. However, it is most unlikely to achieve the NSW 2021 targets of 83.7 per cent of working aged people having post-school qualifications at Certificate level III and above, and 90 per cent of school leavers participating in further education and training or working, by 2020.

New South Wales has achieved encouraging increases in the number of courses completed by female, Aboriginal and regional students and the number of Diplomas, apprenticeships and traineeships earned. It has reached most of its goals in these areas already and needs to reset them.

The Department plans to develop a State Training Plan in 2015. This should describe the training that the Department will prioritise and fund and the long-term role of TAFE. It needs to explain how the Department will develop the VET sector to address latent demand for training and build a sustainable system to train future cohorts so that the State goal of a skilled population can be achieved.

While the cautious nature of the initial reforms in 2015 should limit disruption to TAFE, the Department needs to proceed with its planned evaluation framework to better define what happens next and how it will achieve the efficiencies, innovation, student choice and flexibility needed to support the government's long-term objectives for training.

5.1 The need for a longer-term implementation plan

In Chapter 2, we examined the frameworks the Department has in place for the launch of Smart and Skilled in 2015. This chapter examines whether these frameworks address the government's longer-term objectives, particularly the State Plan target for 83.7 per cent of the population to have post-school qualifications at Certificate level III and above by 2020. Achieving this in the next six years will require substantial efficiency improvements or more funding. In either case, the Department needs to provide clear signals to RTOs about its plans for the sector and how and where growth will occur.

5.2 National Partnership Agreement on Skills Reform commitments

The Department is on track to meet its obligations under NPASR by its expiry on 30 June 2017. As described in Exhibit 21, it will introduce the entitlement in 2015 and review it in 2016 together with pricing, the regulation of fees, the NSW Quality Framework and the VET budget and funding model.

Exhibit 21: NSW progress against NPASR commitments

Obligation	Progress	Audit comment
Create an entitlement	<p>The Department will launch the entitlement in 2015 (six months late). The Department has committed to review it after one year and may extend it to higher qualifications.</p> <p>The Department reviews the Skills List and indexes the price each year.</p> <p>In 2016, the Department plans to review pricing, concessions, exemptions and whether to deregulate fees.</p>	<p>While the NPASR commits States and Territories to entitlement for all, it allows them to manage:</p> <ul style="list-style-type: none"> • RTO and student eligibility • the uptake of the entitlement to balance supply, demand and budget constraints. <p>There is no requirement to create a system that meets unmet demand.</p>
Increase student access to income contingent loans (ICL)	<p>The Department has met its commitment to pilot ICL for Certificate IV.</p> <p>There is no plan to roll these out.</p>	<p>Certificate IV enrolments may fall as Smart and Skilled attracts students to qualifications with lower fees (up to Certificate III) or loans (Diplomas and above).</p>
Improve transparency by reporting comprehensive information	<p>The Department is on track to meet its 2015 commitment to improve inter-governmental reporting on total VET activity using the Unique Student Identifier. The Department is developing systems to use this data to inform students about available courses, the quality of providers, completion rates, price, government support and job prospects.</p>	<p>The NPASR calls for transparency in regards to inter-governmental and consumer information.</p> <p>There is no explicit commitment to improve information for RTOs. The Department has not advised the market about its long-term expectations, making investment and planning difficult.</p>
Strengthen VET quality	<p>The Department has met its commitment to:</p> <ul style="list-style-type: none"> • develop a Quality Framework • facilitate three pilots to independently validate RTO assessment of student's skill levels. <p>These met with mixed success. The one involving the most competitive market did not proceed because of a lack of trust between RTOs.</p> <p>The Department has committed to review its Quality Framework in 2016.</p>	<p>Inadequate assessment of students by RTOs is an Australia-wide problem. Neither the Commonwealth nor New South Wales has plans to advance independent validation.</p>
Improve public RTO efficiency in a competitive environment	<p>NSW has met its commitment by separating TAFE from the Department, and issued a Statement of Owner Expectations for TAFE.</p> <p>It has committed to reviewing the VET budget and funding model in 2016.</p>	<p>The Department and TAFE have yet to make the non-contestable component of the VET budget transparent to drive the efficiency required by the Minister for Education.</p>
Increase training outcomes	<p>NSW exceeded its 2016 targets in 2013 as shown in Exhibit 22.</p>	<p>NSW achieved the agreed outcomes before the entitlement was introduced.</p>

Source: Commonwealth Department of Industry 2012, the Department of Education and Communities 2013 and 2014, and Audit Office research 2014.

The 2012 NPASR based the agreed training outcomes on increases in graduations and completions above 2008 and 2009 levels. New South Wales achieved these by 2013 mainly through full fee training and subsidised training funded through increased fee revenues.

Exhibit 22: NSW targets under the National Partnership Agreement for Skills Reform

Target	2013 target	2016 target	2013 outcomes
All qualification completions	127,675	138,136	141,366
All commencements in higher level qualifications Certificate level III and above	196,957	210,815	231,771
All qualification completions by indigenous students	4,062	4,603	5,805
All commencements by regional and remote students	127,691	136,322	139,605
All commencements in value-add services courses*	53,769	58,335	81,889

Source: Department of Education and Communities 2014.

Note: *a value-add services course commencements are in the following occupation (ANZSCO) groups that the Department, in consultation with industry, identified as priorities: community and health services, technician and trade workers, and information communication and technology

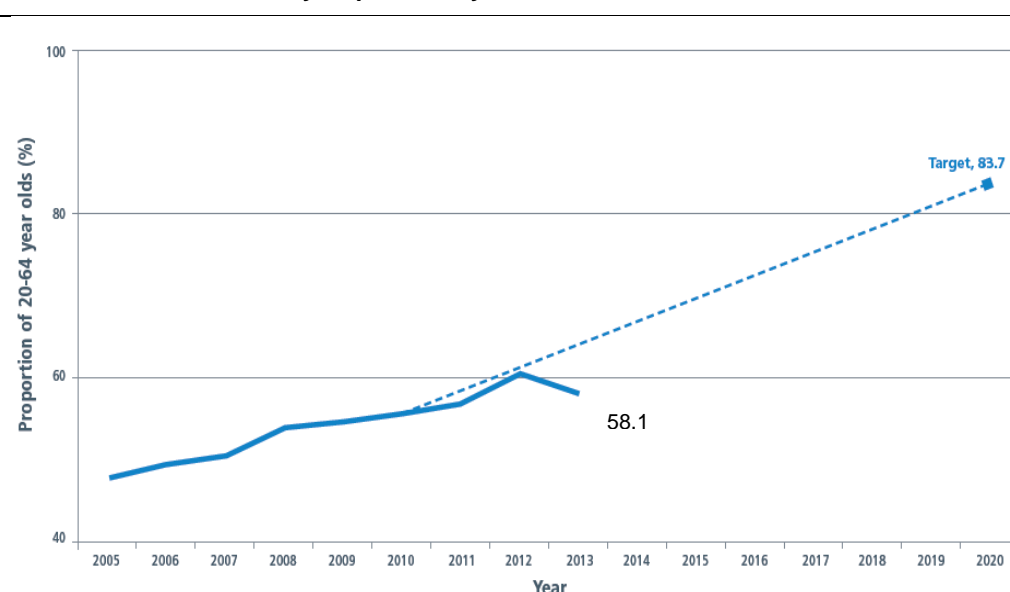
5.3 NSW State Plan commitments

In 2012, the government set additional goals for VET in the NSW 2021 State Plan. It reports progress against these goals in the NSW Budget Papers. Two of the goals are ambitious, most are not.

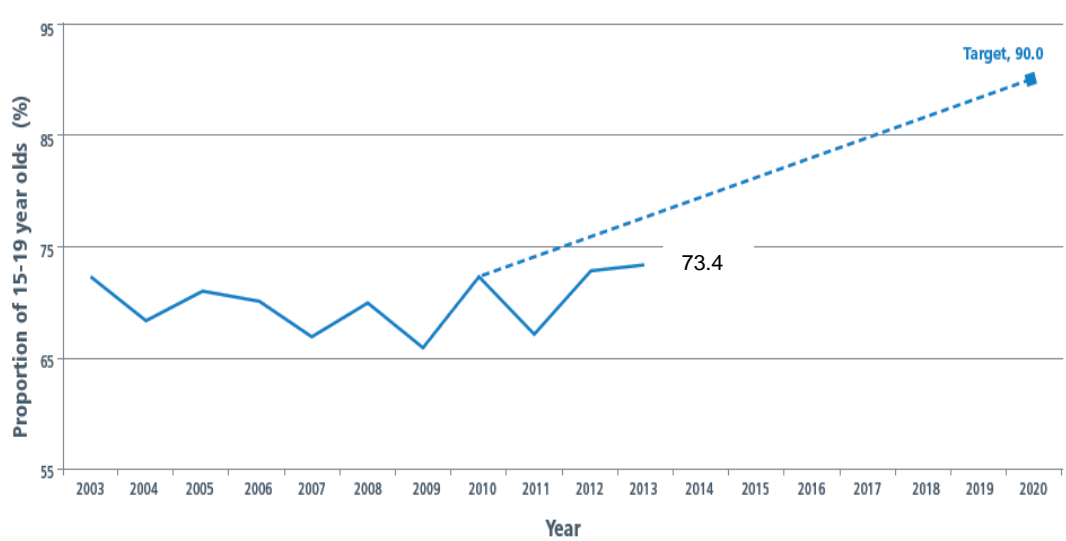
On current trends, New South Wales is unlikely to achieve the targeted increases in the proportion of the working age population with qualifications at Certificate level III and above, and the proportion of school leavers fully engaged in further education and training or work.

Exhibit 23: State Plan targets at risk

Increase the proportion of people aged between 20 and 64 with qualifications at AQF Certificate III and above by 50 per cent by 2020



Ninety per cent of young people who have left school participate in further education and training or employment by 2020



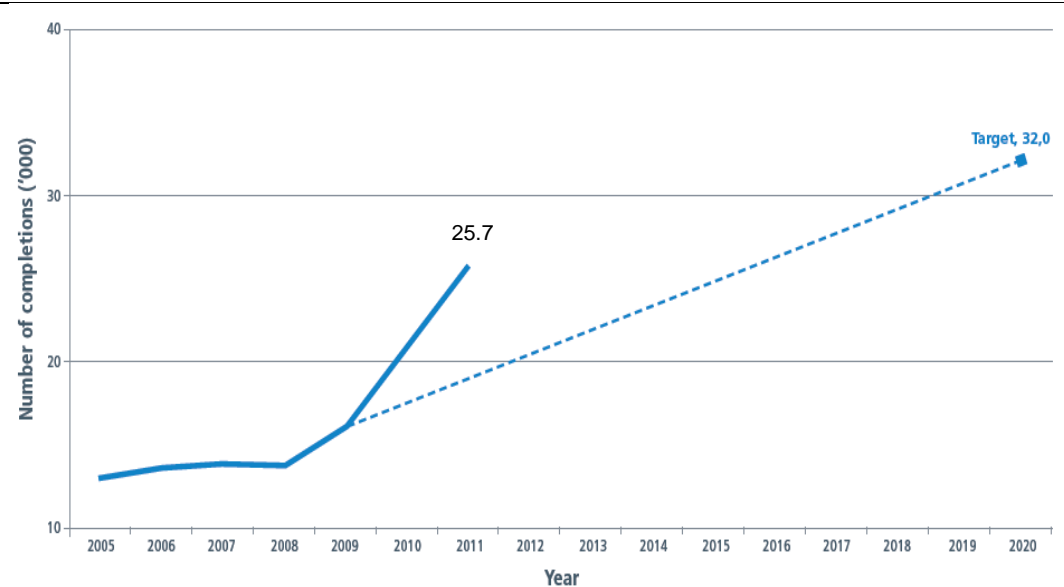
Source: NSW Government 2012.

Notes: The base year is the year the target line starts.

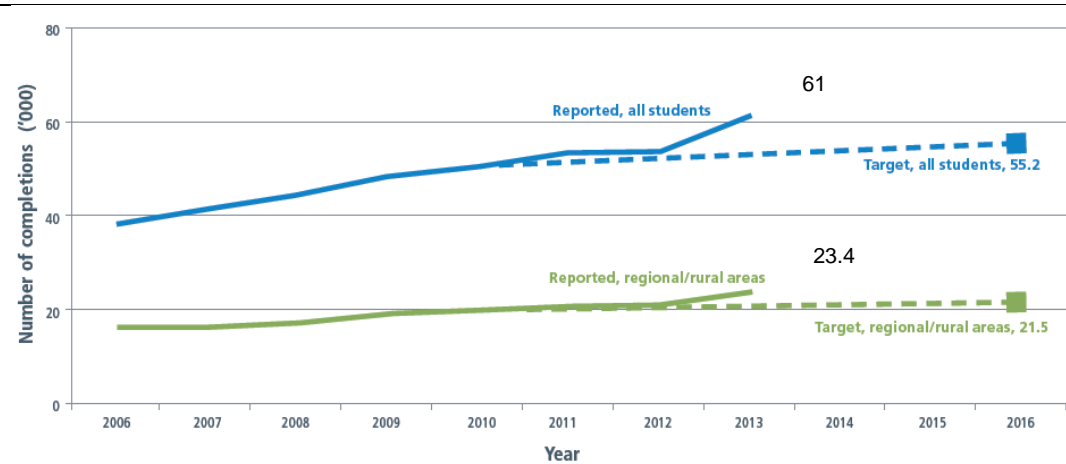
Other State Plan goals were less ambitious. New South Wales largely achieved the targets for increased numbers of Diploma, apprenticeship, traineeship, regional, female and Aboriginal students between the base year (2010) and 2011. In the case of women and Aboriginal students, it achieved the goals for 2020 before it published them in 2012.

Exhibit 24: State Plan targets 'on track'

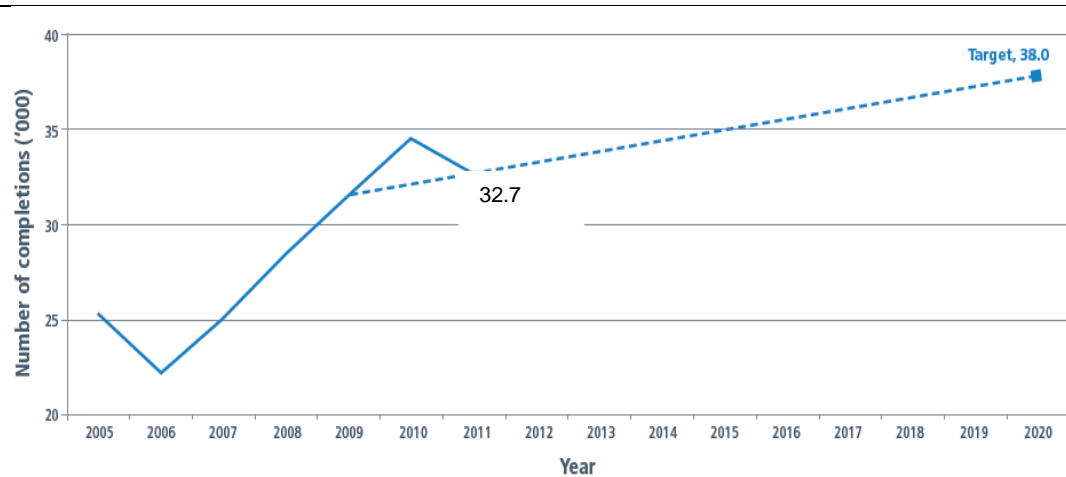
Double the number of Diploma and Advanced Diploma completions by 2020



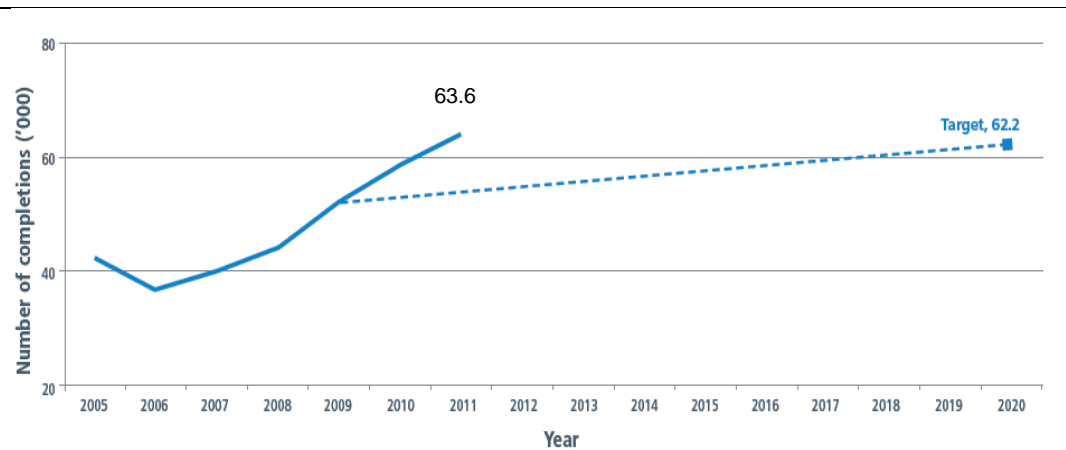
Increase by 10 per cent the number of apprenticeship and traineeship completions by 2016, including in rural and regional NSW



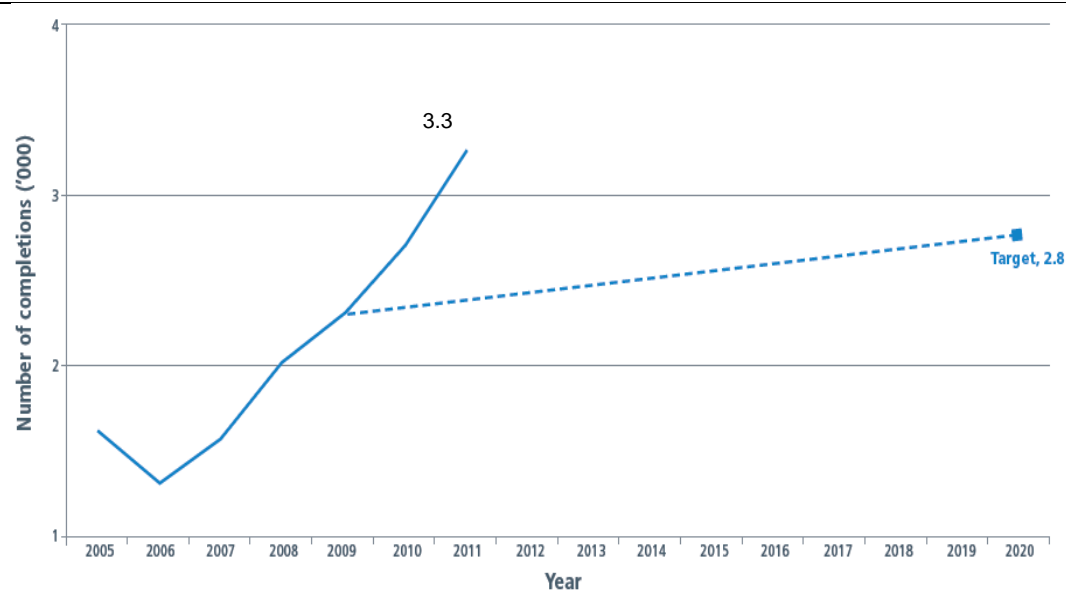
Increase by 20 per cent the number of completions at Certificate III and above by students in regional and rural New South Wales by 2020



Increase by 20 per cent the number of completions at Certificate III and above by women by 2020



Increase by 20 per cent the number of completions at Certificate III and above by Aboriginal students by 2020



Source: NSW Government 2012.

Notes: The base year is the year the target line starts; with the exceptions of apprenticeship and traineeship completions the most recent data is 2011.

The climbing rates of completions for Diploma level qualifications, apprenticeships, traineeships women and Aboriginal students, as last reported in 2013, are encouraging. In many cases current goals have already been achieved and should be reviewed to provide direction for the next six years.

The Department needs to translate its overarching objective of increasing the proportion of the population with post-school qualifications into interim targets with specific action plans. For example, to achieve 83.7 per cent of the working-age population with Certificate level III and above qualifications by 2020, the Department needs to know and plan for:

- how many students need to graduate each year to reach these goals
- how many students need to enrol to get the desired number of graduates based on current and expected attrition rates; and how will it reduce attrition
- how and where it can focus its VET spending to maximise the State's skills growth.

5.4 State Training Plans

The improved reporting that the Department will introduce in 2015 (see 4.4) should inform the development of a NSW State Training Plan that describes what training the Department will prioritise and fund. The plan should describe how the Department will address unmet demand for training and build a sustainable VET system to train future cohorts. Other States have three to five-year training plans that prioritise training needs and funding. Some States, including Queensland, developed these plans to guide their implementation of VET reform. Most plans seek to ensure that State funding of training provides value for money. States that monitor VET activity effectively can adjust price to reflect not only the cost but also the public value of training. Victoria, in particular, uses price as a lever to target spending on areas of market failure while reducing subsidies for training that can be provided on a full fee basis.

Exhibit 25 provides an overview of State Training Plans.

Exhibit 25: Comparison of State Training Plans

Theme	NSW <i>proposed</i>	Victoria	Western Australia	Queensland	South Australia
Duration (years)	<i>Two years</i>	Ongoing – updated in six-monthly Training Market reports	Three years updated each year by Skills Board	Five-year plan to manage reform and annual investment plans	Four years
Funding priorities to increase skills		Yes	Yes	Yes	Yes
Market monitoring	Yes	Yes		Yes	Yes
Value for money		Yes	Yes	Yes	Yes
Access for regions and equity groups	Yes	Yes	Yes	Yes	Yes
Work with industry	Yes	Yes	Yes	Yes	Yes
Quality	Yes	Yes	Yes	Yes	Yes
TAFE adjustment		Yes		Yes	Yes
Educational pathways		Yes		Yes	Yes

Source: Audit Office research 2014.

The NSW Skills Board has approved the development of a State Training Plan for 2015 to 2017.

State Training Plans in other States provide information about the government's future priorities and address value for money and efficiency.

The experience of other States also indicates the need to plan for TAFE's adjustment to a more competitive environment and ensure the plan is capable of supporting the State's ambitious goals for VET over the next six years. While the cautious nature of the initial NSW reforms should limit the disruption to TAFE in 2015, the Department needs to better define what happens next and how it will achieve efficiency and value for money to support the government's 2020 goals.

All jurisdictions need to improve educational pathways and reduce barriers between the school, VET and university sectors. This requires cooperation across the levels of government.

Recommendation

By July 2015, the Department of Education and Communities should publish a State Training Plan for the next four years that:

- identifies the actions it will take to capture efficiencies and build a sustainable VET system capable of supporting the NSW goal of a more highly skilled population
- sets targets for the number of VET enrolments and completions each year needed to support this goal
- identifies the State's investment priorities and planned funding for VET.

Appendices

Appendix 1: About the audit

Audit objective

This audit assessed the effectiveness of the Department of Education and Communities' (the Department's) framework for the Smart and Skilled vocational education and training (VET) reform.

Audit scope and focus

Line of Inquiry	Criteria
Does the Smart and Skilled framework have the potential to achieve the outcomes sought by government? that is: <ul style="list-style-type: none">strengthen the NSW skills baseremain budget neutral while ensuring that: <ul style="list-style-type: none">training is provided in regions and other thin marketstraining is provided to disadvantaged groupsensuring the viability of TAFE in a competitive market.	1.1 The Department's framework contains key design features to support government outcomes. These features address: funds following students to their choice of provider, budget neutrality, which skills are to be subsidised, contestability, quality control, price and allocation of funding to training providers.
	1.2 The framework clearly defines the roles and responsibilities of funder, purchaser and providers.
	1.3 The Department has systems to capture and communicate information about courses, students and providers to manage and regulate the VET market for 2015, and beyond.
	1.4 The Department has a long-term implementation plan that provides a feasible pathway for delivering its contribution to government outcomes.

Audit exclusions

The audit did not examine:

- Public and private training providers' preparedness for the Smart and Skilled reform, although we did talk to them as stakeholders
- VET that is provided outside of the Smart and Skilled reform (for example, VET in schools)
- The Department's decisions around the allocation of the Smart and Skilled reform contracts to individual training organisations
- The Department's decisions around the allocation of Community Service Obligation (CSO) funding to support training in thin markets.

However, we have commented on these where they affected our findings or to provide context.

Audit approach

We collected evidence by:

- interviewing agency personnel responsible for:
 - a) designing and implementing the Smart and Skilled reform, including the Office of Education, Corporate Finance, State Training Services, IT Development, Procurement Services and business change management group, regional and disadvantaged programs, and regional STS managers
 - b) Smart and Skilled policy and implementation working groups developing the provider application, prices, fees and subsidies, budget and funding, strategic reporting and finance, strategic communications, and Smart and Skilled IT Business Systems Development and Integration and Transition and Alignment working groups.

- gathering information from other stakeholders as appropriate
- examining:
 - c) the Smart and Skilled and VET reform plans, policies, procedures and reviews relating to:
 - modelling of various options for VET reform
 - NSW Skills List and ITAB advice
 - the NSW Quality Framework
 - the Smart and Skilled reform Pricing review
 - the Smart and Skilled reform entitlement, including loadings and concessions for disadvantaged learners
 - the Smart and Skilled reform RTO tender documents and contracts
 - RTO eligibility and allocation of VET funding, including supplementary funding (CSO's) to support thin markets
 - risk management plan and register
 - d) VET budgets and projections of training to be undertaken and qualifications to be completed under the Smart and Skilled reform
 - e) experience of other jurisdictions to provide equitable training in a contestable market
 - f) government decisions relating to the VET and TAFE reforms
 - g) management reporting, data and trend analysis in relation to:
 - student numbers
 - private and public registered training organisations
 - NSW State skill requirements and gaps
 - usage of VET by region and demographic
 - cost of delivering VET compared to other jurisdictions.

Audit selection

We use a strategic approach to selecting performance audits which balances our performance audit program to reflect issues of interest to parliament and the community. Details of our approach to selecting topics and our forward program are available on our website.

Audit methodology

Our performance audit methodology is designed to satisfy Australian Audit Standards ASAE 3500 on performance auditing. The Standard requires the audit team to comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance and draw a conclusion on the audit objective. Our processes have also been designed to comply with the auditing requirements specified in the *Public Finance and Audit Act 1983*.

Acknowledgements

We gratefully acknowledge the co-operation and assistance provided by the Department of Education and Communities. In particular, we wish to thank our liaison officers and staff of the State Training Services who participated in interviews and provided material relevant to the audit.

Audit team

Michael Johnston conducted the performance audit, assisted by Suzanne Mousallem and Jason Li. Rob Mathie and Giulia Vitetta provided direction and quality assurance.

Audit cost

Including staff costs, printing costs and overheads, the estimated cost of the audit is \$345,000.

Appendix 2: Chronology of NSW VET reform

Date	Details
2011	<p>The Department and the central agencies produced various models and costings to deliver the NSW target of halving the working-age population without post school qualifications by 2020. The Department conducted a State wide public consultation on VET reforms.</p> <p>The Victorian reforms indicated that NSW needed to invest an additional \$800 million. Alternatively the Department could increase revenues by raising fees by up to 60 per cent and gain efficiencies by allocating 40 per cent of TAFE's budget to private RTOs.</p>
April 2012	New South Wales signed the National Partnership Agreement on Skills Reform.
October 2012	<p>The Minister for Education announced that the Smart and Skilled reform would be launched in 2014 and would initially provide a demand-based entitlement to subsidised training up to a Certificate III. The Department would implement reform at no additional cost by capping the available subsidy, restricting the eligible qualifications, regulating prices and increasing fees.</p> <p>The other major policy objectives were to:</p> <ul style="list-style-type: none"> • introduce more consumer driven contestability • set a bar for quality and only approve the best providers to deliver training • ensure VET is available across the State and to disadvantaged groups • ensure TAFE remains a strong and viable public provider of VET by becoming more competitive. <p>Separate, transparent budget arrangements would fund TAFE for its:</p> <ul style="list-style-type: none"> • higher cost structure (operational base funding) • delivery of VET to thin markets • share of the entitlement funding • its share of other directly purchased VET funding (for example Certificate IV and above).
2013	<p>Treasury commissioned a consultant to develop a funding model for VET, that amongst other things, quantified the additional cost incurred by TAFE's infrastructure and pay structure.</p> <p>Government commissioned the Independent Pricing and Regulatory Tribunal for advice on price and fee arrangements for Smart and Skilled based on the cost of efficient training delivery and the benefit provided to students. The Treasury consultancy informed this advice.</p> <p>State Training Services (STS), which is responsible for coordinating and managing the reforms:</p> <ul style="list-style-type: none"> • began to develop systems to fund and manage the market for contestable government subsidies. STS assumed that it would only manage the private RTOs and that TAFE would continue to be separately funded • consulted with industry to produce a Skills List of qualifications that would be subsidised.
October 2013	<p>Government approved a new funding model for VET and decided that the Department should:</p> <ul style="list-style-type: none"> • defer the launch of the entitlement to 1 January 2015 • distribute TAFE's share of entitlement funding on a contestable basis. This required STS to redesign its systems for funding and managing VET.
November 2013	<p>The <i>Skills Board Act 2013</i> created the NSW Skills Board to oversee the reform of the VET system and to provide independent advice to the Minister for Education. STS supports the NSW Skills Board and provides its secretariat.</p>

Date	Details
December 2013	<p>The government approved:</p> <ul style="list-style-type: none"> a methodology to set fees prices and subsidies based on the advice of IPART moderated by the Skills Board the Skills List on the advice of the Skills Board.
27 February 2014	<p>The NSW Skills Board approved a methodology for allocating funding designed to balance government objectives. The Skills Board clarified that earlier government decisions meant that:</p> <ul style="list-style-type: none"> STS will manage the VET budget for contestable entitlement training and targeted subsidies for higher level training in priority area. STS is to increase the diversity of RTOs while ensuring that TAFE remains viable TAFE will manage its budget for operational base funding, community service obligations and non-entitlement training.
05 May 2014	<p>The Department released information on the Smart and Skilled website:</p> <ul style="list-style-type: none"> Schedules of 2015 prices and loadings to providers A Guide for Training Providers Details of student fees and concessions 2015 NSW Skills List Fact sheets.
June 2014	Applications opened for Smart and Skilled contracts.
1 July 2014	TAFE separated from the Department.
August 2014	Applications closed for Smart and Skilled contracts.
October 2014	Smart and Skilled contracts offered to successful RTOs.
November 2014	Students enrol.
1 January 2015	RTOs can start providing entitlement training.
February 2015	The Department starts paying RTOs for entitlement training.

Source: Audit Office research 2014.

Performance auditing

What are performance audits?

Performance audits determine whether an agency is carrying out its activities effectively, and doing so economically and efficiently and in compliance with all relevant laws.

The activities examined by a performance audit may include a government program, all or part of a government agency or consider particular issues which affect the whole public sector. They cannot question the merits of government policy objectives.

The Auditor-General's mandate to undertake performance audits is set out in the *Public Finance and Audit Act 1983*.

Why do we conduct performance audits?

Performance audits provide independent assurance to parliament and the public.

Through their recommendations, performance audits seek to improve the efficiency and effectiveness of government agencies so that the community receives value for money from government services.

Performance audits also focus on assisting accountability processes by holding managers to account for agency performance.

Performance audits are selected at the discretion of the Auditor-General who seeks input from parliamentarians, the public, agencies and Audit Office research.

What happens during the phases of a performance audit?

Performance audits have three key phases: planning, fieldwork and report writing. They can take up to nine months to complete, depending on the audit's scope.

During the planning phase the audit team develops an understanding of agency activities and defines the objective and scope of the audit.

The planning phase also identifies the audit criteria. These are standards of performance against which the agency or program activities are assessed. Criteria may be based on best practice, government targets, benchmarks or published guidelines.

At the completion of fieldwork the audit team meets with agency management to discuss all significant matters arising out of the audit. Following this, a draft performance audit report is prepared.

The audit team then meets with agency management to check that facts presented in the draft report are accurate and that recommendations are practical and appropriate.

A final report is then provided to the CEO for comment. The relevant minister and the Treasurer are also provided with a copy of the final report. The report tabled in parliament includes a response from the CEO on the report's conclusion and recommendations. In multiple agency performance audits there may be responses from more than one agency or from a nominated coordinating agency.

Do we check to see if recommendations have been implemented?

Following the tabling of the report in parliament, agencies are requested to advise the Audit Office on action taken, or proposed, against each of the report's recommendations. It is usual for agency audit committees to monitor progress with the implementation of recommendations.

In addition, it is the practice of Parliament's Public Accounts Committee (PAC) to conduct reviews or hold inquiries into matters raised in performance audit reports. The reviews and inquiries are usually held 12 months after the report is tabled. These reports are available on the parliamentary website.

Who audits the auditors?

Our performance audits are subject to internal and external quality reviews against relevant Australian and international standards.

Internal quality control review of each audit ensures compliance with Australian assurance standards. Periodic review by other Audit Offices tests our activities against best practice.

The PAC is also responsible for overseeing the performance of the Audit Office and conducts a review of our operations every four years. The review's report is tabled in parliament and available on its website.

Who pays for performance audits?

No fee is charged for performance audits. Our performance audit services are funded by the NSW Parliament.

Further information and copies of reports

For further information, including copies of performance audit reports and a list of audits currently in-progress, please see our website www.audit.nsw.gov.au or contact us on 9275 7100

Performance audit reports

No	Agency or issues examined	Title of performance audit report or publication	Date tabled in parliament or published
249	Department of Education and Communities	<i>Vocational Education and Training reform</i>	29 January 2015
248	Transport for NSW Roads and Maritime Services Sydney Water Corporation	<i>Security of critical IT infrastructure</i>	21 January 2015
247	Roads and Maritime Services WestConnex Delivery Authority Infrastructure NSW Transport for NSW NSW Treasury Department of Premier and Cabinet	<i>WestConnex: Assurance to the Government</i>	18 December 2014
246	Department of Education and Communities	<i>The Learning Management and Business Reform Program</i>	17 December 2014
245	Environment Protection Authority Department of Trade and Investment, Regional Infrastructure and Services	<i>Managing contaminated sites</i>	10 July 2014
244	Office of Finance and Services Department of Education and Communities Forestry Corporation of NSW Fire and Rescue NSW NSW Businesslink Pty Ltd Essential Energy Sydney Trains	<i>Making the most of Government purchasing power – Telecommunications</i>	26 June 2014
243	NSW Treasury	<i>Use of purchasing cards and electronic payment methods</i>	5 June 2014
242	NSW Police Force	<i>Effectiveness of the new Death and Disability Scheme</i>	22 May 2014
241	Road and Maritime Services	<i>Regional Road funding – Block Grant and REPAIR programs</i>	8 May 2014
240	NSW State Emergency Service	<i>Management of volunteers</i>	15 April 2014
239	Fire and Rescue NSW NSW Rural Fire Service	<i>Fitness of firefighters</i>	1 April 2014
238	Transport for NSW Department of Attorney General and Justice Department of Finance and Service Roads and Maritime Services NSW Police Force Department of Education and Communities	<i>Improving legal and safe driving among Aboriginal people</i>	19 December 2013
237	Department of Education and Communities	<i>Management of casual teachers</i>	3 October 2013
236	Department of Premier and Cabinet Ministry of Health – Cancer Institute NSW Transport for NSW – Rail Corporation NSW	<i>Government Advertising 2012-13</i>	23 September 2013
235	NSW Treasury NSW Police Force NSW Ministry of Health Department of Premier and Cabinet Department of Attorney General and Justice	<i>Cost of alcohol abuse to the NSW Government</i>	6 August 2013
234	Housing NSW NSW Land and Housing Corporation	<i>Making the best use of public housing</i>	30 July 2013

No	Agency or issues examined	Title of performance audit report or publication	Date tabled in parliament or published
233	Ambulance Service of NSW NSW Ministry of Health	<i>Reducing ambulance turnaround time at hospitals</i>	24 July 2013
232	NSW Health	<i>Managing operating theatre efficiency for elective surgery</i>	17 July 2013
231	Ministry of Health NSW Treasury NSW Office of Environment and Heritage	<i>Building energy use in NSW public hospitals</i>	4 June 2013
230	Office of Environment and Heritage - National Parks and Wildlife Service	<i>Management of historic heritage in national parks and reserves</i>	29 May 2013
229	Department of Trade and Investment, Regional Infrastructure and Services – Office of Liquor, Gaming and Racing Independent Liquor and Gaming Authority	<i>Management of the ClubGRANTS scheme</i>	2 May 2013
228	Department of Planning and Infrastructure Environment Protection Authority Transport for NSW WorkCover Authority	<i>Managing gifts and benefits</i>	27 March 2013
227	NSW Police Force	<i>Managing drug exhibits and other high profile goods</i>	28 February 2013
226	Department of Education and Communities	<i>Impact of the raised school leaving age</i>	1 November 2012
225	Department of Premier and Cabinet Division of Local Government	<i>Monitoring Local Government</i>	26 September 2012
224	Department of Education and Communities	<i>Improving the literacy of Aboriginal students in NSW public schools</i>	8 August 2012
223	Rail Corporation NSW Roads and Maritime Services	<i>Managing overtime</i>	20 June 2012
222	Department of Education and Communities	<i>Physical activity in government primary schools</i>	13 June 2012
221	Community Relations Commission For a multicultural NSW Department of Premier and Cabinet	<i>Settling humanitarian entrants in NSW: services to permanent residents who come to NSW through the humanitarian migration stream</i>	23 May 2012
220	Department of Finance and Services NSW Ministry of Health NSW Police Force	<i>Managing IT Services Contracts</i>	1 February 2012

Performance audits on our website

A list of performance audits tabled or published since March 1997, as well as those currently in progress, can be found on our website www.audit.nsw.gov.au.

Our vision

To make the people of New South Wales proud of the work we do.

Our mission

To perform high quality independent audits of government in New South Wales.

Our values

Purpose – we have an impact, are accountable, and work as a team.

People – we trust and respect others and have a balanced approach to work.

Professionalism – we are recognised for our independence and integrity and the value we deliver.

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