



LWBLA Briefing Note: Responding to Richard Review Consultation on Apprenticeship Funding

1. Introduction

The purpose of this briefing note is to summarise the key points contained in the LWBLA response to the Richard Review consultation on Apprenticeship Funding.

The Richard Review heralds the biggest shake up of apprenticeship policy in 20 years and has the potential to be a 'game changer' for the sector in England.

This specific review of funding consultation is part of the wider process covering all aspects of Apprenticeship policy in England. There are broadly three separate review processes in play: (i) the structure of qualifications and curriculum content, (ii) funding, and (iii) system wide issues. They come together in late 2013 with the publication of the Governments Implementation Plan - a policy process designed to affect change from 2016 onwards.

Everyone responsible for the delivery of apprenticeship training recognises that funding is the key issue that drives all aspects of behaviour and outcomes– the Government, customers and suppliers.

In summary this briefing note highlights the issues, risks, and potential consequences facing policy makers if a switch is made from an expenditure-based system to tax credits.

The LWBLA has undertaken a wide ranging consultation exercise with its members, involved stakeholders, and conducted a survey of London based employers to look at the key issues covered in the Government's consultation review. Over 200 businesses responded which exceeded our expectations; this has directly informed the detail of our response.

The main points of analysis from the business survey and on-going discussion with providers and stakeholders in London are:

- Businesses like the idea of being paid directly by Government but reject the principle of 'co-investment'.
- If Businesses had to pay up to 50% or more for the cost of training they would recruit significantly fewer apprentices.
- Businesses considered all of the options in the consultation document but by an overwhelming majority would prefer to retain the existing funding system.
- London employers have a wide variety of choice in the labour market when



filling vacancies. This includes different Government backed education and skills programmes as well as traditional recruitment processes in the labour market. This puts the Apprenticeship offer at a significant disadvantage as the employer under 'co-investment' carries the burden of managing both the cost and performance risk of training the individual.

- Providers fear a switch in funding with variable pricing will trigger a 'race to the bottom'. Many high quality social enterprises/charities, and owner managers, fear they would exit the market.
- The introduction of VAT potentially further disadvantages the independent provider compared to the College of Further Education (where VAT does not apply) in a supply chain delivery model.
- Local Authorities express the fear that direct funding of employers will make delivery 'invisible', and restrict local solutions particularly in those Boroughs with high NEET figures and or under performing schools.
- Any reduction in the full funding of apprenticeships for 16-18 year olds would significantly reduce employer commitment and volume thereby restricting the choices open to the learner under the RPA legislation.
- Apprentices fear that direct funding of employers is more likely to lead to a worsening of working conditions with narrow definitions of training restricted to the job role and not offering definable or 'expansive' career pathways.
- The collapse in volume for Apprentice loans for the Over 24's demonstrates widespread market failure compared to other models of learning and the current market place for qualifications.
- The experience in Holland where tax credits have been withdrawn as 'unmanageable' within 2 years should be carefully considered before the UK Government makes any final decisions.

The LWBLA is developing a three-year strategy for influencing the Governments 'direction of travel'. The next step will be to publish a policy prospectus for Apprenticeships in London setting out what works, why and where we believe improvements need to be made.

2. Richard Review: The case for change

To recap 3 Options are set out in the Government consultation document, but in the main there is a clear choice between introducing a new system of tax breaks through the employer payroll system – PAYE, or retaining in a modified form allocating public expenditure to providers and employers.

Three options are presented in the funding review consultation:

- Direct payments to employers
- Tax credits to employers



- Provider contracting

The Government introduces the concept of 'co-investment' for all three options and assumes that employers will make cash contributions to a set % for all apprentices.

Advocates such as the CBI believe that empowering the employer will drive up the overall volumes, increase the range of apprenticeships on offer, improve quality, and drive down the price and costs of training delivery. The case for 'co-investment' of human capital can be summed up as: 'the only way to value your investment is to contribute to it?'

There appear to be three recurring criticisms of the current system and specifically the role of providers within it:

- Qualifications that offer little learning or real skill acquisition,
- Employers that are taken 'hostage' by the provider, and
- Insufficient competition in the marketplace.

The LWBLA view is that these issues need to be tackled and not ignored if the key successes and achievements of the provider base are not to be ignored. The Government will use Providers as a justification for change as a 'problem that need fixing'. The provider view is that the Government confuses the means (money) with the ends (more and better quality apprenticeships).

Employers would become the customer purchasing what they want, when they want, at the price they decide upon. It sounds a compelling perspective – but is it deliverable?

What are the issues, risks, and consequences for pursuing such a radical shift in thinking?

On balance what should the Government consider when deciding upon the 'direction of travel' – if the devil is in the detail - so what's the detail?

The overall picture from the businesses and stakeholders we canvassed considering the three options in the Governments consultation can be summarised as the following:

Option 1

Making direct payments to employers appears to have relatively few supporters as this may require the Government to design and operate a new administrative system and employers will have to manage the paperwork –or get the provider to do it for them? How much would a new system cost, and why would employers want a mark two version of the administrative burden currently managed by providers under contract to Government?

The one advantage of this approach is that it could allow the Government to flexibly allocate on the basis of location and type of study programme similar in concept to the current provider funding rates / ILR system. The 'hidden hand' of the Government



will be its guiding feature and for that reason alone is likely to be rejected by business interests as potentially interfering and bureaucratic.

Option 2

Government assumes that if you give employers a tax credit on PAYE then this is a simple and easily understood way for employers to co-invest in the recruitment and training of apprentices. This is the preferred choice of the UKES and CBI. The simplicity of this option is the belief that all you need to do is enter numeric data on generic payroll software such as SAGE line 50 and the rest takes care of itself. This option is yet to be validated publicly by payroll and tax experts. The position of HMRC will be interesting to hear in due course.

In parallel with this debate is the requirement (from advocates such as the FSB) that all forms of 'red tape' are abolished or effectively irrelevant to the everyday operational requirements of the employer. The issue of 'red tape' and what regulatory framework accompanies the tax credit is fundamental to knowing how this will work in practise.

What are the consequences for providers if either options 1 & 2 are agreed?

Providers have assumed that in future they will deliver services under contract to an employer and cease to have a direct funding relationship with Government. The employer uses price sensitive information to contract with a provider in a competitive market. Services are defined and priced, and subject to VAT in accordance with the employer's requirements. The focus is on delivering training and qualifications – what else would the employer need to pay for?

What is not set out in the consultation document is whether the total cash value of the apprenticeship framework is retained before the employer co-invests? A central issue is whether the same funding formula pricing that currently exists transferred into the tax credit. What happens to the current arrangements for full funding of 16-18 year olds? Does the government want to reduce the overall level of public expenditure or reduce the average value of investment per apprentice as it seeks to drive volume upwards?

Providers assume that with options 1 & 2 the system over time will become invisible to the public. The only time you are likely to see an apprenticeship is when a vacancy is advertised. How do you then define, manage and make transparent the performance risks are a critical set of questions in determining whether the tax credit policy can be effective or not.

A key issue is the extent to which the operation of the price mechanism will act as a driver to squeeze down on the overall cost of training – which it is assumed to do, and the fear that this will consequently become a 'race to the bottom' as the price mechanism drives the delivery process and defines the quality of outcome.

Speculatively one scenario for the Government is to retain all compliance on the provider even though the provider has no direct relationship to the Government. In



the consultation document reference is made to 'approved' providers – but this is not specified in any detail. The fact that the Adult Skills budget is assumed to remain enables the Government through its Funding Agencies to retain significant influence on the supply side. Many Providers have commented that they regard this as the worst of both worlds – hidden regulation that they are accountable to couple with a loss of scalable volume and an uncertain cash flow.

Option 3

This is seen as a modified arrangement of the current system whereby provider contracts are retained but funding can only be drawn down upon evidencing of the employers cash contribution. Critics of the current system are vigorously opposed to this option as a 'cop out'. The risk is of course that in common with Options 1 & 2 the provider has to secure the employer cash contribution before it can draw down the public funds. The employer has committed to paying the cash so will have the incentive to behave as a customer would. The Government continues to measure and quantify the scale and total amount of co-investment that the new arrangements generate.

This option retains the possibility that the Government continues to fully fund the 16-18 year olds so not to disadvantage this education progression route when compared to all other choices that the young person can consider. In effect this provides an activist state with the capacity to influence locally and sectorally the type, range and outcomes the Government of the day wants to buy.

The key issues for Government lie in defining what level of accountability, transparency and performance risk should be shared between the employer and provider? Would a threshold of success rates be retained that justifies the policy as at present? This may provide difficult to sustain in future as SME's account for over 70% of all apprenticeship volume in London and are the least likely to both 'co-invest' and manage performance risk.

Critically for London will the high cost of delivery that is reflected in the area uplifts and social disadvantage be retained when setting the tax payment/credit, or if there is a national averaging would it put London at a relative disadvantage to the rest of the country.

Does it matter if apprentices are funded more generously in ne part of the country or another? Well yes in that over half of all new jobs in the UK are being created in London's economy. London is increasingly the driver of national prosperity.

As Vic Farlie the Executive Chair of the LWBLA stated:

"The rationale for co-investment on the scale that the consultation document implies is flawed. The combination of competing government programmes, affordability to the business, and choice in the labour market here in London means that the apprenticeship programme will always be severely disadvantaged."



I have some sympathy with the Government 's position but you need to see what will happen on the ground and not lose sight of what works."

To many of the LWBLA's members Option 3 looks like the 'least worst option'.

In summary none of the options carried sufficient detail within the consultation document from Government's rationale to be able to be evaluated detail.

3. What are views of businesses that responded to the LWBLA survey in London?

Over 200 businesses many of which are SME's across London completed a short questionnaire focused on the key issues of principle issues contained in the Government's Consultation document. In the main these were businesses that either employ apprentices or understand the role of a training provider. The LWBLA wanted to get a sense of where employer attitudes could be defined and what the individual feedback and comments were to each question. The survey carries both the statistical responses and the textual answers.

The key responses can be summed up as the following:

- A clear majority - 60% of businesses liked the idea of a tax credit or a direct payment towards employing an apprentice. They like the idea that this is a contribution from the Government towards the cost of hiring, the on-going salary and/or the cost of training. Large multi site employers with staff in Wales and Scotland wanted clarification as to which system would operate. Corporate HR departments want a single integrated model.
- A clear majority - 65% said they would be less likely to recruit if they had to pay up to 50% of the costs. The principle of co-investment on the scale that the Government assumed in the consultation document is evenly divided. The range of comments highlighted that lack of consensus as to what was the right % contribution from employers.
- However when tested an overwhelming majority - 73% said if they were required to co-invest to pay for training under any of the options then they would recruit fewer apprentices.

Examples of comments from London based employers were:

"A high calibre graduate intern is generally free, has a high commitment level and requires less on-going training commitment",

"There are a wide variety of highly subsidised college courses/graduates with free work experience providing a high level of technical knowledge and practical support at a nominal cost", and

"Now we have traineeships with no employment guarantee why should we pay for an apprenticeship?"



The key point to emerge for these responses is that whilst businesses like the idea of a tax credit or direct payment they do not accept the Government's principle of co-investment in return for increased control of the training and would recruit fewer apprentices.

Moving on to the management of training providers and the accountability for public funds employers expressed the following responses:

- 42% said costs would rise, 18% said they would fall and 40% were unsure. Different employers want different things. London was seen as a high cost area with different industries and sectors adopting different approaches. Businesses with the in-house expertise were more likely to want to manage the training but could see that there are currently services that are not charged where in future this may be a cost. An almost equal number were unsure. One business owner who did not wish to be named stated:

"I've won contracts on the golf course because I know the business owner and he knows me. That's the way of the world."

- 58% said they did have the team to oversee manage the training.
- 78% said that they agreed that the government would have to have rules and red tape to govern the tax credit/payment. This was also viewed as a 'deal breaker' for SME's who employ close to 70% of all apprentices in London. Of all the issues that businesses sought clarity on was how the system would work if there a change opt direct tax credits/payment
- 67% said they would not pay any money back if the apprentice did not complete the training.
- 55% would accept the findings an Ofsted report.

The key point is that business would accept rules on how public money is spent, but do not accept being accountable for performance - they would not pay any money back to the Government.

"Why should businesses pay twice - once through corporation tax system -when these kids were at school, and again when we have to employ them as an apprentice and pay for their basic education?"

In conclusion when all things were considered; the opportunity to receive a direct payment, the principle of co-investment, the desire to oversee the training, the necessity for red tape, the conclusion was decisive:

84% of all businesses that responded to the survey would prefer the system to stay as it is.

4. What are the views of London based training providers?

Whilst some providers see deregulation and service contracts with employers as a



progressive move, the majority believe that the evolution of the current arrangements is a more stable and sustainable long-term perspective. From the LWBLA's consultation the recurring comments are:

- 'The system isn't broken'; it requires simplification of funding and investment in the curriculum.
- The Government is confusing the means (money) with the ends (more & better apprenticeships).
- Employers already drive the recruitment and appoint a provider without being accountable for performance risks.
- London has a highly competitive market place of providers and they have to be proactive in sourcing both young people and employers.
- The very low take up of adult learning loans for apprenticeships since April 2013 is evidence of wider market failure.

From a provider perspective uncertain income forecasts will require 'deeper pockets' of cash flow to sustain the organisation. This in turn becomes a higher risk commercial proposition than has historically been the case. High performing providers with great reputations and industry leading quality assurance systems – as we have here in London could be swept away as providers run out of money. The risk in London is that many of the social enterprises, charities and owner managers do not have the resource, scale and 'cash in the bank' to survive this.

For providers such as Colleges of Further Education here in London who deliver very few apprentices they are most likely to focus on classroom based vocational education as this provides a steady cash flow with managed performance risk in a more certain operating environment.

5. What are the potential risks for Government?

The LWBLA discussed with its membership and stakeholders the issues that Government should take into account when considering these options. One of the central questions that were consistently raised by training providers is whether there is a trade off exists between the overall volume of apprenticeships and the aggregate level of co-investment. The lack of any technical evaluation, modeling or statistical analysis of the three options (in the consultation document) makes it almost impossible to be able to project what is likely to work and in what circumstances.

The following issues emerged as part of the consultation exercise, which we would welcome the opportunity of discussing directly with Government in relation to the three options:

- The economic cycle: what is the modelling/projection of aggregate demand & volume of future job creation - scale, impact and consequences particularly in a recession?



- Are there any 'moral hazards' attached to using PAYE tax breaks i.e.; will it be available to companies that pay no taxes in the UK?
- How complex could the payroll system become for Government, if errors and fraud take hold as in Holland or the tight regulatory environment in Canada?
- How realistic is it to secure business sentiment on a sufficient scale over the long term where radical variations of economic performance exist at the local / regional level?
- How can/do employers objectively compare government employment and skills offers when some are free, highly subsidised or give the employer higher qualified labour to start with compared to an apprentice?
- How much re-badging, displacement and deadweight of training is acceptable?
- How do you convince the public that this is the right policy re: safeguarding the interests of young people when compared to staying on at school or going to college?

The LWBLA is concerned that by changing one Post -16 option but not looking strategically at all other publicly funded qualifications and pathways this places the apprenticeship offer at a significant disadvantage in London.

6. What are the consequences for Government and the Apprentice?

There was a general concern that looking at funding in isolation from the rest of the education and skills landscape across all of Post-16 education raises the following policy questions:

- Does a relatively 'visible' system of accountability and compliance through training providers become relatively 'invisible' with employers?
- Are all localised solutions marginalised or rendered redundant?
- Can you objectively measure the quality of training in the workplace without Ofsted?
- Will SME's have the desire or expertise to manage performance risk?
- Will apprentice's aged 16-18 remain fully funded?
- Will Apprentice rights in the workplace be safeguarded?
- Does the switch from expenditure to tax credits reduce the scope for future Governments to respond to changing priorities affecting Post-16 education?
- Does it matter if some of the best providers exit the market and the sector is deregulated?
- Would applying VAT lead to a net reduction in the amount spent on publicly support training?



7. What the current system offers & delivers

Businesses and Training providers responded to the issue of how the current system operates and the case for change.

What employers currently like and value under the current arrangements is that they have influence without being accountable for any of the delivery risks, in particular:

- Employers control the recruitment of the apprentice.
- Can see that there are transparent funding rates for training.
- Carry no performance risk as they typically contract with a training provider to deliver the learning, and
- Have minimal accountability to Government.

The following points summarise why there is a consensus on what the current system offers:

- Certainty – of volume, pricing and administration.
- Direction - public policy can be used to set priorities in the market place.
- Transparency - Government knows who delivers apprentices, where the money is spent and by whom.
- Compliance – regulation ensures standardisation of product and outcomes evaluated by Ofsted.
- Accountability – expenditure is recouped/saved and recycled.

Where issues of non-compliance, fraud or abuse have occurred the current system is most likely to expose and resolve this in the public interest.

8. The International perspective

The LWBLA conducted an online literature search to look at how Governments currently organise and fund apprenticeships. The OECD, ILO and G20 Governments have spent the past two to three years looking at how to tackle youth unemployment & strengthen progression into employment. Published reports have highlighted the important contribution apprenticeship systems can make - all recognise the importance of employers to create jobs – but no country is proposing to go down the route of the UK switching from public expenditure to tax credits.

There are only two examples we can find of tax credits being applied; Canada and Holland. Canada appears to have a highly regulated system with fixed prices. However Holland is now after only two years abandoning this type of policy. See below:

“The Dutch Finance Ministry has recently announced plans to end the tax break currently accorded to companies in the Netherlands who offer apprenticeships. The Government aims to abolish the so-called “education” tax break, compensating



businesses that take on apprentices, and to replace the provision with targeted subsidies. The Government intends to do so without, however, changing the purpose of the provision, namely to provide a financial incentive to firms willing to offer apprenticeship places.

Defending the decision, the Finance Ministry highlights the fact that the existing system of granting corporate tax relief is simply proving “unmanageable.” Over the last five years expenditure has doubled from around EUR200m (USD259m) to approximately EUR400m, primarily due to the “improper use” of the provision, the Finance Ministry argues, emphasizing that targeted subsidies are intended to address the issue.

According to the Dutch Finance Ministry, a budget of EUR200m in subsidies is to be made available in future and to be distributed among applicants. Some schemes will no longer be eligible for the financial support, as money will be allocated on a basis of greatest need. Plans to replace the tax break with financial subsidies were provided for within the framework of the Government’s coalition agreement.”

The presumption is that any system change in funding would lead to a demonstrable improvement in overall volume, quality of learning, and job outcomes - otherwise why would the Government want to pursue this policy?

9. Apprenticeships: Regionalism & Localism

It is important to understand the scale & context of apprenticeships as part of the Post -16 education offer in London.

The apprenticeship offer for 16-18 year olds are broadly targeted at two distinct groups:

- Individuals who did relatively badly at school and need a way into work - typically through a Level 2 framework; and
- Those individuals who have a choice about going on to do A levels or University but wanted a specific career path – typically a level 3 framework.

In 2011-12 approximately 65% of all apprentices were Level 2 and the balance were Level 3. The number of higher level apprenticeships totaled less than 300 in total or less than 2% of volume in London. Figures provided by the Data Service for 2012-13 contract year to the end of April (Q3) indicate that the trend rate is down across all three age groups and apprenticeship levels.

Apprenticeships are marketed as an inclusive not an exclusive brand with the Mayor seeking huge increases in numbers. Sales and marketing campaigns drive take up, and employers have real choices over whom they wish to recruit. For London this means that:

- There are only 10,000 16-18 year old apprenticeships compared to 140,000 School 6th Form and FE College students. The ‘silent issues’ are how many



job outcomes do Colleges deliver here in London, and is the avalanche of unemployment for 19-24 year olds a consequence of limited work based training opportunity at 16?

- Level 3 + (equivalent to 2 A Levels +) Apprenticeships are most in demand as an alternative to going to Sixth Form or University. This is the key gap in the market with PLC's now creating new apprenticeship opportunities under the current funding methodology. The total volume of new employer led apprentices are not known.
- Apprenticeships are often seen as a targeted solution to educational under achievement or the 'at risk of NEET' cohort by Local Authorities, and are a key source of supply for the Level 2 apprenticeship offer.
- Local and regional policy targets for apprenticeships – see the London LEP require Independent providers to deliver stretching targets with no practical support.

Since 2010 there has been sustained progress despite a difficult recession which can be summed up as the following:

- Apprenticeship volumes have doubled over the past three years.
- Between 75-80% of all publicly funded apprenticeships are now delivered by the independent sector.
- 70% achieve a framework - comparable with school performance for 5 A-C's at GCSE.
- 91% progress into employment, self-employment and/or further education.
- Ofsted confirm that 78% of all apprentices (in London) are now trained by providers who are 'good' or 'outstanding'.
- Approx. 75% of apprentices are employed in an SME.
- An active market of suppliers with over 100 providers in a well organised in a trade association.

A central question for policy makers in London has been assessing the future projection and scale of new entry level employment & overall job generation in the capital. Debate has focused on the range and type of and the skills required. The orthodox view of London's labour market is that it is assumed to have a 'shrinking middle' of technical employment. Jobs are either being up-skilled to graduate and post graduate levels, or deskilled requiring little on the job skill acquisition masked by the overall net growth and size of employment opportunity. The apprenticeship offer had to be marketed and delivered within this prism of employer demand and job creation.

If for example apprenticeships were to be limited to level 3 qualifications only, London would have a significant market gap for level 2 work based learning and could experience a squeezing out of young under achieving adults from the labour market.



10. National Questions to ask as the Government moves into the next phase of the implementing the Richard Review.

- Volume Projections - How effectively could the policy work in a recession?
- Choice – why should an employer co-invest when other programmes are free?
- Moral hazard debate - Can an employer who pays no corporation tax benefit from the same tax break on PAYE when other employers do pay corporation tax?
- Deadweight – Wouldn't large employers have done this anyway by re-badging what already goes on?
- Costs – what are the hidden costs of using payroll and the systems the Government will need to administer?
- Complexity - How will the policy work outside of England for multisite employers?
- Performance- If an apprentice does not complete the qualification does the business have to rebate the credit?
- Fraud - What is an acceptable error rate or level of fraud for HMRC?
- Safeguarding- Will it apply to 16-18 year old apprentices?
- Red tape - Will all employers be subject to an Ofsted inspection?
- Will the introduction of VAT inexorably lead to a decline in the amount spent on the apprentice?

All the main political parties will want to be seen as 'business friendly. No one will want to give any hostages to fortune as the general election approaches. If the policy does run into the sand then it will only come from the technical evaluation and risks attached to the uncertainty of system implementation.

The key issue going forward will be the regulation or 'red tape' that accompanies the new system. Trade Unions will use this opportunity to strengthen workplace rights. Business will argue that red tape is a 'deal breaker' and that the move to a price sensitive market based on choice means the 'lightest touch' or no enforceable provisions. Hints from HMRC suggest they are not convinced that tax credits can work.

11. Forward strategy & Timetable

Our forward strategy assumes that Government will choose to implement one of the three options in the consultation document. The combination of ideological instinct and the desire to be seen to be 'doing something' appears irresistible. The reason that the options 1 and 2 may not be brought forward is the technical complexity of implementation. In particular if HMRC are not convinced.

Our forward strategy assumes on ensuring business is the customer – and if the government goes with either option 1 or 2 then businesses should inherit the regulatory framework.



The key area for providers to engage with is the curriculum and end state qualification approval. Delivery of the product must remain our responsibility, whilst businesses resolve how 'bespoke' or 'off the peg' they want to go we go about showing what we deliver. Showcasing our success, highlighting the customer and new marketing strategies will be at the heart of the next phase.

The Government may be vulnerable to interventions when legislation is going through the House of Commons. The Finance Bill in 2014 may be the set piece event and how we showcase ourselves as pragmatic and high performing will be important. The outcome of the General election will be a point of reflection and allow a new administration to press on or slow things down. To recap:

The Government's timetable assumes that BIS will publish an implementation plan in the autumn of 2013, with decisions and legislative matters to be contained in the 2014 Budget, and the new system going live in August 2016. This timetable drives our forward strategy, which is geared towards the following activity:

- Information
- Engagement
- Policy Development
- Promotion

The LWBLA will be updating and publishing its Policy prospectus for Apprenticeships in London later in the autumn of 2013. This will set out our strategic position and where we believe progress can and should be made. We welcome comments and views from as wide a range of organisations with an interest in apprenticeships in London. We recognise that an open dialogue has enabled the LWBLA to engage in a much broader understanding of policy and our guiding principle is to showcase and explain what works well and why.

Victor Farlie

Executive Chair LWBLA

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