



Tertiary Education Report: Converting the Western Institute of Technology at Taranaki's Crown loan to equity

Date:	16 August 2021	TEC priority:	High
Security level:	In Confidence	Report no:	B-21-00512
		Minister's office No:	

ACTION SOUGHT

	Action sought	Deadline
Hon Grant Robertson Minister of Finance	agree to convert to equity in Te Pūkenga the remaining balance of the Western Institute of Technology at Taranaki Limited's Crown loan of \$4.157 million.	At your earliest convenience
Hon Chris Hipkins Minister of Education	agree to convert to equity in Te Pūkenga the remaining balance of the Western Institute of Technology at Taranaki Limited's Crown loan of \$4.157 million.	At your earliest convenience
Enclosure: Yes	Round Robin: Yes	

CONTACT FOR TELEPHONE DISCUSSION (IF REQUIRED)

Name	Position	Telephone	1st contact
9(2)(a)	Principal Advisor	9(2)(a)	✓
Gillian Dudgeon	DCE, Delivery	9(2)(a)	

THE FOLLOWING DEPARTMENTS/AGENCIES HAVE SEEN THIS REPORT

- DPMC MPI ENZ ERO MBIE MoE MFAT
 MPP MSD NZQA NZTE TEC TPK Treasury

- Minister's Office to Complete:**
- | | |
|---|--|
| <input type="checkbox"/> Approved | <input type="checkbox"/> Declined |
| <input type="checkbox"/> Noted | <input type="checkbox"/> Needs change |
| <input type="checkbox"/> Seen | <input type="checkbox"/> Overtaken by Events |
| <input type="checkbox"/> See Minister's Notes | <input type="checkbox"/> Withdrawn |

Comments:

Recommendations

Hon Grant Robertson, Minister of Finance, **Hon Chris Hipkins**, Minister of Education

It is recommended that you:

- note** that, in 2009, Cabinet agreed the Western Institute of Technology at Taranaki (WITT) would retain a non-interest bearing Crown loan of \$5.196 million repayable in equal annual instalments over five years between 2020 and 2024 [CAB Min (09) 30/12 refers];
- note** that WITT made its first payment of \$1.039 million on 31 December 2020, with an outstanding balance to the Crown of \$4.157 million;
- note** that WITT and Te Pūkenga have sought for the remaining \$4.157 million be converted to equity to support WITT's ongoing financial sustainability and enable progress towards addressing significant deferred maintenance liabilities;
- agree** to convert to equity in Te Pūkenga the remaining balance of WITT's Crown loan of \$4.157 million;

Minister of Finance

AGREE / DISAGREE

Minister of Education

AGREE / DISAGREE

- approve** the following appropriation changes to give effect to the decision in recommendation 4 above, with no impact on the operating balance or net core Crown debt:

Vote Tertiary Education Minister of Education	\$ million increase/(decrease)				
	2021/22	2022/23	2023/24	2024/25	2025/26 & outyears
Non-Departmental Capital Expenditure: Support for a Single National Vocational Education Institution	4.157	-	-	-	-

- agree** that the proposed change to appropriations for 2021/22 above be included in the 2021/22 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply;
- note** there will be no fiscal implications to the operating balance or net core Crown debt given the original decision to issue the loan was charged against the capital allowance at the time [SDC Min (08) 11/3 and CAB Min (09) 30/12 refer];
- subject to the agreement of the Minister of Finance, **send** the attached letter to the Chair of Te Pūkenga informing him of the decision to convert WITT's Crown loan to equity;
- note** that we recommend you take an oral item to Cabinet on converting WITT's loan to equity; and

10. **agree** that the Tertiary Education Commission proactively release this briefing once decisions have been made.

Minister of Education

AGREE DISAGREE



Gillian Dudgeon

Deputy Chief Executive, Delivery
Tertiary Education Commission

16 August 2021



Hon Chris Hipkins

Minister of Education

28 / 09 / 2021



Hon Grant Robertson

Minister of Finance

27 / 09 / 21

Purpose

1. This briefing seeks Joint Ministers' agreement to convert to equity the remainder of Western Institute of Technology at Taranaki Limited's (WITT's) historical Crown loan, which totals \$4.157 million.

Background

2. On 18 December 2020, the Chief Executive of Te Pūkenga wrote to the Tertiary Education Commission (TEC) formally requesting that the Crown loan balance owing by WITT be converted to equity or forgiven to support the ongoing financial viability/sustainability of the subsidiary and enable progress towards addressing significant deferred maintenance liabilities.
3. We recently provided advice to the Minister of Education on WITT's Crown loan, who agreed to convert the loan to equity (B-21-00385 refers).

Background to WITT's Crown loan

WITT's loan was the result of financial difficulties in the mid-2000s...

4. A number of years of financial difficulties at WITT resulted in the Crown providing loans totalling \$17.618 million as well as the replacement of its Council with a Crown Commissioner in December 2006. In July 2008, the Government agreed to a "repair and rebuild" strategy for WITT that included converting the balance of the Crown loans to equity over the following five years, subject to performance targets being met [SDC Min (08) 11/3 refers].
5. In August 2009, the new National Government reviewed this decision and considered that retaining some debt, repayable at a future date, would strengthen incentives on WITT to achieve its recovery strategy whilst constraining its ability to incur further debt. As such, Cabinet agreed [CAB Min (09) 30/12 refers] that:
 - WITT would retain a non-interest bearing Crown loan of \$5.196 million repayable in equal annual instalments over five years between 2020 and 2024; and
 - The balance of the outstanding Crown loan (\$12.422 million) would be established as a suspensory loan, convertible to equity on the achievement of agreed performance measures over five years from December 2009.
6. Throughout the following five year period, WITT met the key performance measures that had been set for the annual conversion of the suspensory loan. Consequently, by 31 December 2013, the full amount of the \$12.422 million loan had been converted to equity.

...and the first instalment of the \$5.196 million loan was repaid at the end of 2020...

7. The Crown loan agreement with WITT requires \$1.039 million be paid at the end of each calendar year between 2020 and 2024. The first payment of \$1.039 million was made by WITT to the Ministry of Education (MoE) on 31 December 2020. Consequently, a total of \$4.157 of the Crown loan remains.

...but the WITT subsidiary has limited ability to repay the debt to the Crown going forward...

8. WITT has historically had ongoing financial viability and sustainability issues, largely due to its small scale. Prior to the establishment of Te Pūkenga, the TEC assessed WITT as 'high risk'. WITT has not achieved an underlying surplus since 2015.
9. At the end of 2020, WITT had \$2.5 million in cash reserves. With another deficit forecast in 2021 and a scheduled further Crown loan repayment of \$1.039 million at the end of the year, ^{9(2)(b)(ii)} ██████████ Based on these forecasts,

WITT may be able to make its 2021 payment, however it is likely that its 2022 position will become difficult to manage. It will have trouble managing any liquidity risks itself and be unable to undertake any significant capital expenditure.

...therefore the Te Pūkenga parent would need to provide support

10. If WITT had remained an independent tertiary education institution, it is unlikely that it would have had the ability to repay the Crown loan without some level of Crown support and there would have been a significant risk of it running out of cash. 9(2)(g)(i) However, the establishment of Te Pūkenga in April 2020 means that WITT is now part of a wider group.
11. Te Pūkenga has established a group treasury strategy which allows it to move cash (excluding ring-fenced cash reserves) around the network to where it is needed. As such, if WITT is unable to make any repayments on the Crown loan, it has the ability to seek support from the Te Pūkenga group. We consider it is likely that WITT would need to begin doing this from 2022, if not from late 2021 if financial performance is worse than expected.
12. While Te Pūkenga has the ability to fund WITT's repayment of the Crown loan, given its financial position and the need to fund its transformation programme over coming years, it is seeking that WITT's loan is converted to equity. In essence, Te Pūkenga would prefer to use those funds over the medium-term to drive its transformation programme and implement its new operating model rather than support WITT's cash position.

Ability to convert the Crown loan to equity and fiscal implications

13. There is a historical Crown loan agreement with WITT that was signed by the then Minister of Finance and Minister for Tertiary Education. The agreement allows the Minister of Finance to alter any of the terms and conditions of the Crown loan agreement. We consider that agreement by Joint Ministers to convert the loan to equity would fit within the terms of the Crown loan agreement and that a paper would not need to be taken to Cabinet. However, we would recommend that you still take an oral item to Cabinet on the issue.
14. The Treasury has advised that to convert the remainder of WITT's loan, MoE would need to remove the current receivable of \$4.157 million and increase its investment into Te Pūkenga by the same amount. The increase to its investment into Te Pūkenga would need to be appropriated. There would be no fiscal implications to the operating balance or net core Crown debt given the original decision to issue the loan was charged against the capital allowance at the time.
15. MoE has been consulted on this briefing and support the loan conversion and corresponding appropriation change to occur.

Impact if the Crown loan is not converted to equity

16. If a decision is made not to convert the loan to equity, WITT will be unable to address deferred maintenance issues which are significant given WITT's historical financial performance. WITT will also not be able to respond as well as it could to the recent increase in student enrolments. Finally, it will result in Te Pūkenga having to provide cash support to WITT to ensure its solvency. Te Pūkenga will need to cover all remaining loan repayments over the next four years as well as provide support to cover any potential shortfalls in operating expenditure.
17. We do not consider that there are any wider risks to students or the network if a decision is made not to convert the loan to equity. While WITT has capital expenditure and deferred maintenance needs, so do many other subsidiaries, and these can be highlighted and addressed through Te Pūkenga's capital asset strategy work stream. Te Pūkenga expect to identify a list of high-priority projects in coming months and it has indicated it will be seeking funding from Budget 2022 to help fund these projects and its wider capital asset strategy.

18. In the lead-up to the formal establishment of Te Pūkenga, officials had proposed writing off WITT and UCOL's historic Crown loans as part of a broader fiscal strategy for funding Te Pūkenga and other components of the Reform of Vocational Education [METIS 1218370]. However, the emergence of COVID-19 led to a two-stage approach to funding Te Pūkenga that did not include writing off WITT's loan. Following Te Pūkenga's letter to the TEC in late 2020 regarding converting WITT's loan to equity, we have engaged with Te Pūkenga on this issue a number of times. Both WITT and Te Pūkenga are seeking a decision from Ministers on this issue in the near future to assist it with future planning.

The Treasury's view

19. The Treasury does not support the Crown loan being converted to equity. This is due to the lack of value that would be obtained from gaining equity in Te Pūkenga and that the Crown would forgo \$4.157 million in expected repayments. 9(2)(g)(i)

Appendix 1: Draft letter to Murray Strong

Murray Strong
Chair
Te Pūkenga
PO Box 19400
Hamilton 3244

By email: murray.strong@tepukenga.ac.nz

Dear Murray

Conversion of the Western Institute of Technology at Taranaki's Crown loan to equity

The Minister of Finance and I have agreed to convert to equity in Te Pūkenga the remaining balance of the Crown loan to the Western Institute of Technology at Taranaki Limited (WITT), which totals \$4.157 million.

As per Te Pūkenga's correspondence to the Tertiary Education Commission at the end of 2020, I expect that converting the loan to equity will support WITT's ongoing financial viability and enable WITT and Te Pūkenga to begin to address the significant deferred maintenance liabilities that have arisen at WITT. More generally, I expect this decision to help support Te Pūkenga to effectively manage its network and deliver a sustainable network of vocational education and training as part of its transformation.

Thank you for your work to date. I look forward to receiving an update on Te Pūkenga's progress in the near future.

Yours sincerely



Chris Hipkins
Minister of Education

cc Tim Fowler, Chief Executive, Tertiary Education Commission
Stephen Town, Chief Executive, Te Pūkenga
Robin Brockie, Chair, Western Institute of Technology at Taranaki Limited