National School Resourcing Board

Review of the Schooling Resource Standard (SRS) Indexation Arrangements

Issues Paper

February 2024

Contents

Background

The Review of the Student Resourcing Standard (SRS) Indexation Arrangements (the Review) is a commitment arising from the National School Reform Agreement (NSRA). In the extension of the NSRA, Ministers committed to completing the Review in 2024, and several jurisdictions requested it be completed in early 2024 to inform negotiations for the next NSRA.

In accordance with Section 128 (8) of the *Australian Education Act 2013*, in developing the Terms of Reference (Appendix A) for this Review, this Minister consulted with the Education Ministers Meeting, Independent Schools Australian and the National Catholic Education Commission. Following this consultation, on 1 February 2024, the Australian Government Minister for Education, the Hon. Jason Clare MP, commissioned the National School Resourcing Board (the Board) to undertake this Review and deliver its final report by 28 March 2024.

Deloitte Touche Tohmatsu (Deloitte) was engaged to support the Board to undertake this review, including to undertake an analysis of the indexation arrangements that are currently being applied to the SRS.

The SRS estimates how much total public funding a school needs to meet its students' educational needs. It is made up of a base amount and up to six needs-based loadings. The base amount and loadings are periodically reviewed to reflect changing educational needs.

Each year, the SRS base amount and loadings are indexed to reflect changes in prices which affect the cost of providing schooling. Indexation is a critical component of the SRS as it ensures that funding is responsive to changes in the prices of salary and non-salary inputs, allowing the real value of funding to be maintained over time.

Current SRS indexation arrangements have been in place since 2019 and are outlined in the *Australian Education Act 2013*. The final indexation rate is determined as either:

- A rate calculated as the higher of:
  - 3 per cent (the indexation 'floor'), or
  - A percentage derived from a composite index, comprising of 75 per cent of the change of the Wage Price Index (WPI) and 25 per cent of the Consumer Price Index (CPI); or
- A rate prescribed by the Minister for Education.

To date, the indexation factor has been prescribed (in 2019 and 2020), set to the indexation floor (in 2021), and set at the composite index (in 2022 and 2023).

This issues paper explores four aspects of the current indexation arrangements:

- The **appropriateness** of current SRS indexation arrangements, including whether the operation of the SRS indexation arrangements since 2019 has kept pace with schooling price-related cost increases
- The suitability of the current SRS indexation **floor of 3 per cent**
- The **structure and weighting** of the composite index for the SRS indexation factor
- The **timing** of SRS indexation rates, including the reference period for source WPI and CPI data and the date at which the indexation rate is confirmed for the school year.

The analysis has been based primarily on publicly available data. Data referred to in the review Terms of Reference has not been used in this analysis due to timeframes and availability.

1. Preliminary findings on the appropriateness of current indexation arrangements

Schooling inputs

- Since 2018, salaries have consistently represented 74 to 76 per cent of total recurrent school expenditure across Australian schools.
- Salaries of teaching staff account for between 48 and 58 per cent of total recurrent expenditure in schools.
- The percentage of recurrent expenditure allocated to salary-related expenses varies across jurisdictions, particularly in government schools.
    - In the 2019-20 financial year, salary-related expenditure ranged from 62 per cent (in the Northern Territory) to 79 per cent (in the Australian Capital Territory) of the total expenditure for government sector schools.
- Since 2017, there has been a steady rise in the proportion staff in schools which are non-teaching.
- There is very limited information publicly available on the components of non-salary related expenditure.

Schooling input prices

- On a weighted average basis[1], the annual salary increase for teaching staff in government schools from 2019 to 2024 fluctuated between 2 and 6 per cent.
- Information on non-government schools indicates that teaching staff salary increases tend to align closely, or slightly surpass, the increases stipulated in the government-sector Enterprise Bargaining Agreements (EBAs) for teaching staff in their respective states.
- For non-teaching staff, the annual salary increase across jurisdictions ranged from 2 to 5 per cent (on a weighted average basis) over the period.

Comparisons with SRS indexation

- The WPI has increased by an average of 2.5 per cent over the period 2019–2023. Throughout this timeframe, teacher and non-teacher salaries in the government sector have, on a weighted average basis, increased by 2.6 per cent and 2.4 per cent respectively. Consequently, the growth in the WPI appears to be relatively consistent with the growth in both teacher and non-teacher salaries across Australia, on average.
- Over the analysis period, growth in the CPI tended to outpace growth in CPI categories likely to be related to schooling (including Newspapers, books and stationary, Utilities, Audio, visual and computing equipment and services and Insurance and financial services).
- More detailed information on the nature and shares of non-labour schooling inputs would enable a more robust analysis.

Key drivers of CPI and WPI

- Movements in WPI and CPI are driven by a range of factors that are not all relevant to schooling inputs.

[1] Weights reflect the relative proportion of FTE teaching staff in government schools across jurisdictions.

- The key drivers of price growth between 2021 and 2023 stemmed from supply chain disruptions and rising demand after removing COVID-19 restrictions. Most key drivers of CPI growth over this period are not relevant to schools, except for Utilities and Automotive fuel.
- Similarly, wage growth in recent years has been strongest in sectors like Construction which have seen persistent shortages and COVID-19 disruptions. Education and training WPI growth has tracked lower than overall WPI in recent years due to EBA timing, but this may change as more EBAs are renegotiated.

Discussion questions:

- Are data sources available on the breakdown of non-salary operating expenses for schools?
- What are the most substantial non-salary operating inputs?

2. Preliminary findings on the suitability of current indexation floor

- The rationale for an indexation floor is to provide funding certainty and protecting the system against deflation. However, there is a trade-off between these objectives and funding accuracy.
- In periods of low inflation, a floor of 3 per cent would increase the purchasing power of funding.
- Protecting the system from deflation and a reduction in funding suggests that an indexation floor may be appropriate.
- Funding certainty might be more important in times of high inflation volatility. While difficult to predict, there are reasons to consider that the inflationary environment may be more variable in the future than was the case over recent decades prior to the COVID-19 pandemic.
- If the concept of a floor is a desirable feature of an indexation formula, the next consideration is what is an appropriate level. The level of the floor should directly reflect the rationale for the floor's adoption.
- One principle for setting the indexation floor in this context might be that it should not be engaged in a 'normal' inflationary environment.
- Based on this principle, the current indexation floor of 3 per cent may be appropriate.

Discussion questions:

- How are the trade-offs between funding certainty and funding accuracy perceived?
- Have perspectives about the rationale for an indexation floor changed over time?
- Is the current indexation floor of 3 per cent appropriate? Should it change?

3. Preliminary findings on the structure and weighting of composite index

- The current composite index is based on the CPI and WPI, which are broad-based measures of changes in prices and wages. As such, the composite index reflects changes in the price of goods, services and labour that are not all relevant to schooling inputs.
- Alternative measures were considered against four key principles:
  - Frequency and timing
  - Is it is education focussed?
  - Would it reflect costs faced by schools?
  - Is it policy independent?
- On balance, WPI and CPI are considered appropriate components for SRS indexation. Education-specific measures like the Education and Training WPI pose risks of circularity of funding policy and indexation (‘policy independence’), while other data sources like PPI and Average weekly earnings are often less timely and add minimal value.
- It is possible that a combination of some subcomponents of the CPI would better reflect schooling non-labour input prices than the overall CPI, while still maintaining policy independence. A more detailed understanding of these expenditure items would enable a more robust analysis of how well the CPI (or subcomponents of CPI) reflects the true price increases being faced by schools.
- Expenditure on salaries and wages has consistently represented around 74 to 76 per cent of total recurrent school expenditure, across both government and non-government sectors. This suggests that the current weighting remains relevant and appropriate in reflecting the composition of school expenditure.

Discussion questions:

- Are there any other data inputs that should be considered for the composite index?
- To what extent does the SRS indexation rate, or expectations regarding future rates of indexation, inform or influence government policy decisions regarding input prices? For example, are agreed wage increases negotiated through EBAs set with regard to the SRS indexation rate?

4. Preliminary findings on timing of SRS indexation rates

- Indexation rates are applied to Australian Government funding payments using data from the **June quarter** of the year in which the payments are made, which is generally known by September in that year.
- Payments to non-government schools are made in January and July using estimated indexation rates, with a final payment in October based on actual indexation (including revisions to prior payments based on the difference between estimated and actual indexation).
- Payments to government school systems are made on a monthly basis using estimated indexation rates, with a final funding revision made in December to reconcile the difference with actual indexation.
- Determining the most appropriate timing for the application of indexation to the allocation of funding requires balancing the trade-off between timeliness of funding to changes in input prices against the need to provide certainty to systems and schools when determining their budgets and allocating resources.
- Indexation rates utilising CPI and WPI data from earlier quarters may improve budget certainty and the ability for schools and systems to effectively plan.
- Data from up to 12 months prior to the current approach may be appropriate for the purposes of indexation, depending on the extent to which schools and systems require greater budget certainty to support their planning and effective use of funding.

Discussion questions:

- To what extent is it important that funding payments respond quickly to estimates of changes to input prices?
- How much lead time after final indexation is known do schools and systems feel is needed to support effective budget planning and resource allocation?
- For government school systems, how is budget planning affected in cases where final monthly payments in December account for large differences in projected vs. actual indexation?

Appendix A

Terms of reference
Review of Schooling Resource Standard Indexation Arrangements

Commonwealth funding for schools is needs-based and is calculated with reference to the Schooling Resource Standard (SRS). The SRS is an estimate of how much total public recurrent funding a school needs to meet its students' educational needs and is indexed each year by the SRS indexation factor to reflect changes in prices and wages and therefore costs faced by schools.

The purpose of this Review is to consider the appropriateness of the SRS indexation arrangements to ensure arrangements reflect changes in the costs associated with meeting the educational needs of students. It fulfills a joint commitment from the Australian Government and the State and Territory Governments to review the SRS indexation arrangements in 2024 ahead of the next National School Reform Agreement.

<u>Current SRS indexation arrangements</u>

Since 2019, SRS funding has been indexed annually by either:

- a rate calculated as the higher of:
  - 3 per cent, or
  - a percentage derived from 75 per cent of the change of the Wage Price Index (WPI) and 25 per cent of the change of the Consumer Price Index (CPI); or
- a rate prescribed by the Minister for Education.

This approach introduced a minimum increase in funding and certainty for schools. It is weighted towards changes in wage costs reflecting that teachers' and staff salaries are a significant driver of schools' costs.

Given the current economic climate, it is prudent to review the SRS indexation arrangements to ensure it remains current and appropriate to ensure the effective delivery of school education.

Scope

The Review will consider and provide advice on:

1. The **appropriateness of current SRS indexation arrangements,** including whether the operation of the SRS indexation arrangements has kept pace with average schooling cost increases since 2018.

2. The **suitability of the current SRS indexation floor** of 3 per cent.

3. The **appropriateness of the composite index**, including its structure, weighting and possible alternatives to the current composite index – currently set as 75 per cent Wage Price Index and 25 per cent Consumer Price Index.

4. The **timing of SRS indexation** rates, including;
   a) the reference period for source WPI and CPI data,
   b) the date at which the indexation rate is confirmed for the school year, and its impact on systems and schools' ability to effectively budget.

In providing this advice, the Board will engage closely with State and Territory Governments and their relevant departments as well as the non-government sector. This includes seeking financial data to support the Review as required.

Timing

The Board will provide its final report to the Australian Government Minister for Education by 28 March 2024. The Minister will share the report with Education Ministers and non-government peak bodies within 5 business days of receiving the report, and will invite the Chair of the Board to present the final report to the Education Ministers Meeting.