

## Submission on “Our Schooling Futures: Stronger Together (*Whiria Ngā Kura Tūātinītinī*)”: Report by the Tomorrow’s Schools Independent Taskforce

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### 1. Introduction

1. I am making this submission on behalf of myself as:
  - 1.1. A parent of three school-aged children; and
  - 1.2. A PhD-qualified consulting and academic economist, with over 25 years’ expertise and experience in industrial organisation and regulation, as well as institutional economics and organisational design.
2. As to my relevant expertise and experience, I have authored or co-authored a range of studies and other publications on organisational or sectoral design, such as:
  - 2.1. The ownership of tertiary education institutions;<sup>1</sup>
  - 2.2. The economics of social service delivery;<sup>2</sup>
  - 2.3. Governance, incentives and performance in Māori organisations;<sup>3</sup>
  - 2.4. The innovation, growth and performance impacts of ownership, industry structure and institutional arrangements in agriculture;<sup>4</sup>

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<sup>1</sup> *Ownership of Tertiary Education Institutions*, with B. Howell, research paper prepared for the New Zealand Productivity Commission, September 2016.

<sup>2</sup> *Economics of Social Services*, technical appendix prepared for the New Zealand Productivity Commission, providing a microeconomic framework for analysing how best to organise social service delivery, with an emphasis on the theories of incomplete and complete contracting, February 2015.

<sup>3</sup> *Comparing Apples and Kūmara: Well-Being and Profitability Implications of Māori using Land for Cultural Purposes as well as Commercial*, March 2019; and *An Economic Appraisal of Ngā Tipu Whakaritorito: A New Governance Model for Maori Collectives*, December 2004.

<sup>4</sup> *The Effect of Industry Structure and Institutional Arrangements on Growth and Innovation in the New Zealand Agriculture Sector*, with L. Evans, research report prepared for the New Zealand Ministry of Agriculture and Forestry, August 2007; and *The Role and Significance of Cooperatives in New Zealand Agriculture: A Comparative Institutional Analysis*, research report prepared for the New Zealand Ministry of Agriculture and Forestry, with L. Evans, December 2005.

- 2.5. How institutional arrangements in electricity sectors affect firm incentives, strategies and behaviours;<sup>5</sup> and
- 2.6. Optimal industry regulation, including in the light of disruptive new technologies, business models and players – in electricity, transport, and generally.<sup>6</sup>
3. I have not been commissioned or funded by any party to provide this submission – it represents my own personal and professional views, freely offered.
4. The report of the Tomorrow’s Schools Independent Taskforce (the Taskforce) – “Our Schooling Futures: Stronger Together (*Whiria Ngā Kura Tūātinini*)” (the Taskforce Report) – makes a very wide range of sometimes very detailed recommendations (the Recommendations):
  - 4.1. I do not propose to address all of what the Taskforce has recommended, but instead to:
    - 4.1.1. Make a number of high-level observations; and
    - 4.1.2. Provide more specific comments on a selection of issues arising from the Recommendations.
5. A comprehensive analysis of all of the Recommendations would represent a very substantial exercise, given the wide-ranging realignment they would cause in education sector governance arrangements and incentives, and hence likely performance:
  - 5.1. My specific comments on selected issues seek to address matters which are likely not to be the focus of many other submissions, given they are perhaps more subtle and technical in nature (albeit in fundamentally important ways).

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<sup>5</sup> *Strategic Forward Overbuying as a Counterstrategy against Raising Rivals’ Costs*, May 2014; and *The Effects of Vertical Integration, Forward Trading and Competition, on Investment and Welfare, in an Imperfectly Competitive Industry*, September 2011.

<sup>6</sup> *Preparing Electricity Regulation for Disruptive Technologies, Business Models and Players – In the Long-Term Interests of Consumers*, independent White Paper commissioned by the Electricity Retailers’ Association of New Zealand, August 2018; *Regulation 2025: The Future of Transport Regulation*, exploring how transport should be regulated in 2025, as Strategy Director for the Ministry of Transport, August 2015 to October 2016; *Should Regulation be Applied by Sector or by Activity?*, presentation to the New Zealand Ministry of Transport, Wellington, June 2016; and *Regulation 2025: Spectrum of Regulatory Responses*, with L. Evans, research report prepared for the New Zealand Ministry of Transport surveying regulatory approaches and rationales, July 2015.

## 2. High-Level Observations

6. The Taskforce Report concerns itself with something that most people would agree on – the need to ensure New Zealand’s education sector organisation is in some sense delivering the best possible “overall” outcomes for New Zealand students, and will continue to do so in light of expected future changes and challenges.
7. A major theme that permeates the Tasforce Report is the Taskforce’s view that current education sector arrangements are not delivering outcomes that are “fair”, and that significant changes are required to ensure that the sector provides outcomes that are.
8. Major deficiencies of the Taskforce Report are that:
  - 8.1. It does not precisely and clearly define what it means by “fair”; and
  - 8.2. It offers no credible or convincing analysis that the solutions it proposes will in any way achieve the Taskforce’s apparent or stated aims, or indeed lead to better outcomes (however measured) – setting aside the question of whether the Taskforce’s problem definition itself is even valid.
9. Without a precise and clear statement of what the Taskforce is seeking to achieve it is difficult:
  - 9.1. For any party to evaluate the Taskforce’s problem identification and its recommended solutions; and
  - 9.2. For the Taskforce itself to demonstrate that its proposed changes are either required or will be effective, or are superior to other possible approaches.
10. Without a competent assessment of either the problem or the proposed solution, there is a very real risk that the Recommendations will not only fail to achieve their apparent or stated aims, but could simply lead to worse outcomes than the status quo.

## 3. Specific Comments on Selected Issues

### 3.1 Overview

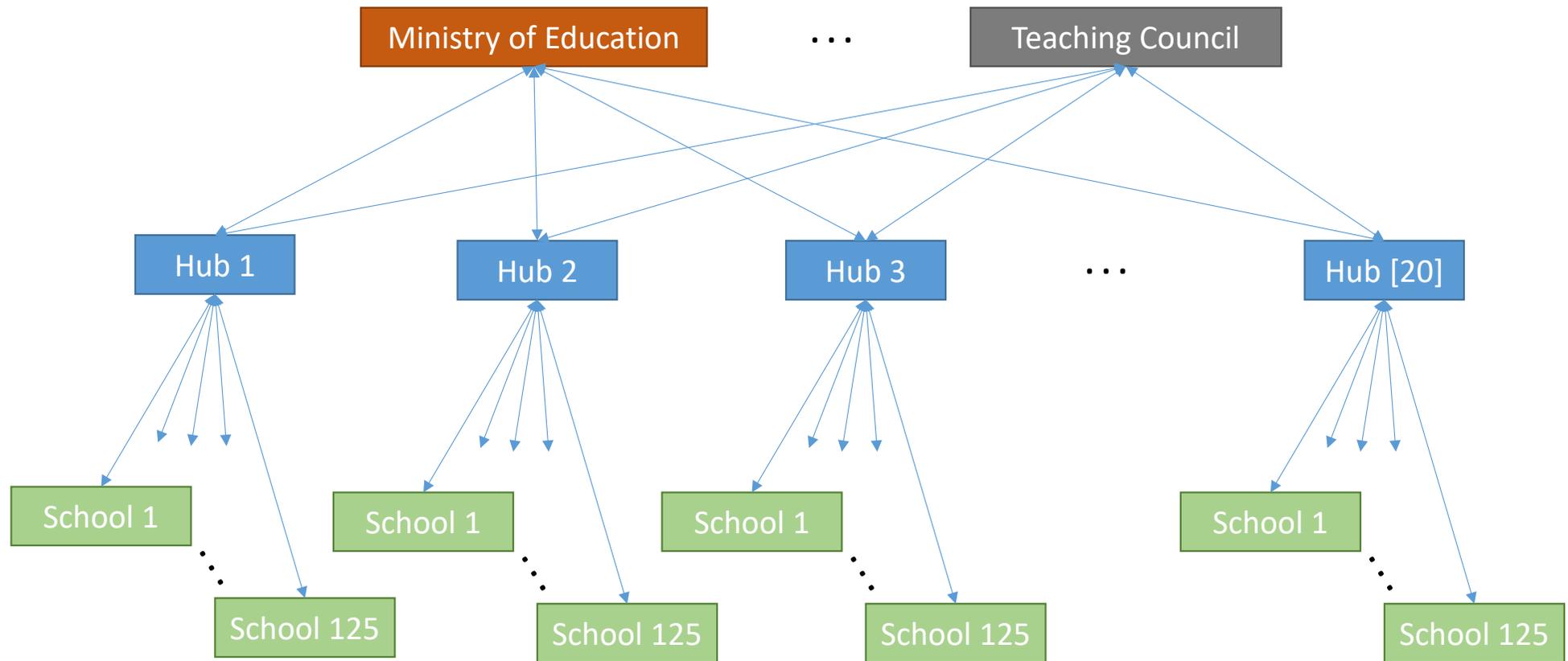
11. I wish to focus on just three important aspects of the Recommendations:
  - 11.1. How they infeasibly and impractically re-assign key governance rights within the sector, with important implications for incentives, risk and performance;

- 11.2. How proposed tenure limits for school principals are likely to defeat the Taskforce's intention to improve the diffusion of innovation across the sector; and
- 11.3. How proposed measures to reduce "unhealthy competition" between schools target the wrong issue, and fail to appreciate the inevitable competition any school faces in the markets for both staff and students.

### **3.2 Infeasible and Impractical Re-Assignment of Governance Rights**

- 12. Status quo arrangements in the New Zealand education sector provide a high level of autonomy to each school, with self-governance achieved through boards of trustees (Boards) that are accountable to local communities and responsible for key school functions:
  - 12.1. The Recommendations provide for many of the decision-making rights and areas of responsibility currently held by Boards being re-assigned, to varying degrees, between Boards and to-be-created "local" education hubs (Hubs).
- 13. Based on data provided in the Taskforce Report, it would seem:
  - 13.1. There would be roughly 20 Hubs nationwide, including one national hub for Kaupapa Māori education;
  - 13.2. Each Hub would be associated with an average of 125 schools, and would be in some unspecified form of "partnership", not only with the Ministry of Education, Teaching Council and other (also unspecified) education and social sector agencies, but also with each of the other Hubs;
  - 13.3. Directors of each Hub, which would be a Crown Entity of some unspecified form, would be appointed by one or more central government ministers, with at least half of those directors being practicing educators, complemented by local iwi representation.
- 14. Figure 1 illustrates the proposed Hub model of education sector governance, with arrows representing the likely bi-directional governance rights arising under the "partnership" envisages between Hubs and schools, and between Hubs and other sector bodies.
- 15. It should be clear from this figure that:
  - 15.1. The "span of control" of any one Hub, at 125 on average, is extremely wide; and
  - 15.2. The apparently anticipated network of partnerships will be very expansive.

Figure 1 – Proposed Hub Structure



Note: bi-directional arrows represent proposed, but not precisely-specified, “partnership” arrangements.

16. The former suggests any one Hub will face severe obstacles in effectively monitoring (or indeed, effectively interacting at any substantive level) with such a broad range of schools:

16.1. Unless, that is, it adopts “one-size-fits-all” approaches to managing its interactions with any given school.

17. The expansiveness of the apparently anticipated network of partnerships begs the question as to how material any one such partnership will be:

17.1. Partnerships in the conventional sense arise in only certain sectors, and are typically limited to two or only a small number of partners, with close mutual monitoring and specific, strong incentive mechanisms to ensure quality provision and good performance:<sup>7</sup>

17.1.1. None of these features are apparent in the Recommendations;

17.2. Having more than 20 partners in the case of each Hub, possibly thousands in the case of schools, suggests such “partnerships” will be empty, or worse, create unresolvable monitoring and incentive problems:

17.2.1. E.g. if performance at one school is contingent on conduct at a Hub or some other school, with the affected school having little or no visibility, let alone control, over that conduct.

18. The Recommendations state (p. 49):

“... Hubs would assume all the legal responsibilities and liabilities currently held by school Boards of Trustees. This would include responsibility for school quality and performance, principal and teacher employment, 5YA property funding and property development, financial management including final approval of a school’s annual budget, health and safety, and human resources services.”

19. Conversely, they also state (p. 48) that Boards will “retain final approval of” principal appointments, and schools’ strategic and annual plans:

19.1. This appears to create inherent conflicts on key decisions – is it the Hub or the Board which has final approval over a school’s principal appointment, and its strategic and annual plans?

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<sup>7</sup> Examples include legal partnerships. For a discussion of related issues see Howell, B. and R. Meade, 2016, *Ownership of Tertiary Education Institutions*, research paper prepared for the New Zealand Productivity Commission, September.

- 19.2. If Boards retain rights of final approval over these matters, how will Hubs be able to discharge their “legal responsibilities and liabilities” in cases where Hubs and Boards are at odds?
20. It is clear these proposals are not mutually consistent or feasible – rather they appear to be creating a very real risk of governance failure:
- 20.1. A compelling example is in relation to health and safety – most health and safety risks are localised in nature, and hinge on parties with local knowledge using it to mitigate those risks;
- 20.2. If Hubs have “legal responsibilities and liabilities” for health and safety matters – for an average of 125 schools each – then it seems clear that Hubs will be wholly reliant on schools, and their Boards (whose health and safety risks have been assumed by their Hub), to discharge their very extensive legal obligations:
- 20.2.1. This will expose Hubs to an unacceptable risk of legal liability with no capacity to manage that liability, meaning no able director or officer should wish to serve on Hubs for fear of assuming uncontrollable and severe personal liability;
- 20.2.2. Alternatively, it will require Hubs to be exempted from health and safety requirements, which would undermine the intent of the associated legislation, or those requirements will need to be retained by Boards (who themselves will not be able to manage those risks, unless status quo governance rights are preserved).
21. At their heart the Recommendations propose a wholesale (though convoluted) centralisation of powers currently exercised by Boards:
- 21.1. This means moving towards the centralised and bureaucratic (due to ministerial director appointments) governance of an impossibly-large number of schools per Hub, from the status quo model of highly decentralised accountabilities and decision-making held by Boards over individual schools:
- 21.1.1. In turn this is akin to moving from a “franchise” model of school governance, in which the local information advantages held by Boards are exploited to provide incentives for educational delivery, towards a centralised bureaucratic model of delivery in which the incentive benefits of any such local information advantages are lost.

22. Implicitly, the Taskforce seems to believe that Hubs will provide sufficient economies of scale (e.g. in non-strategic “back-office” functions), diffusion of innovations, and other (unspecified) network/partnership benefits to overcome any governance costs associated with extremely wide spans of control, reduced access to local information, misalignment of information and accountabilities, and outright conflicts in accountabilities and authority:

22.1. The Taskforce Report does not provide any evidence that this will be so, or even seems to appreciate the nature of these very real, and very significant, governance trade-offs.

23. The re-assignment of governance rights proposed in the Taskforce Report appears to create a range of important, unresolvable governance conflicts, without clearly and credibly setting out sufficiently offsetting benefits:

23.1. For this reason alone the Taskforce’s governance recommendations need to be revisited in their entirety, and developed by parties with requisite skills in designing governance arrangements in complex social service environments.

### **3.3 Undermining of Innovation Incentives**

24. Another important area in which the Recommendations contain inherently conflicting features is in relation to innovation:

24.1. A major aim of the Recommendations is to enhance the diffusion of innovations from innovating schools to those that are less innovative. One means which the Taskforce appears to believe will achieve this is through compulsory five year term limits for principals.

25. Superficially, such term limits ensure that innovative principals will rotate to other schools and thereby help to diffuse their innovations:

25.1. Of course the reverse is also likely to be true – non-innovating principals will possibly be relocated to schools which previously had an innovative principal, with no innovation gains.

26. However, such term limits – like the Taskforce’s desire to reduce “unhealthy competition” between schools (see Section 3.4 below for more):

26.1. Do nothing to address the factors known to be important for achieving diffusion of innovations; and

- 26.2. Undermine innovation incentives in the first place – even if they enhance diffusion, they enhance diffusion of less innovation.
27. As to the former, innovation is typically the product of:<sup>8</sup>
- 27.1. Coordination and cooperation among research-focused institutions – schools are not examples of these;
  - 27.2. “Creative destruction” in which innovating organisations displace non-innovating ones – schools are not an example of this either, except to the extent that inter-school competition is permitted to result in creative schools thriving and non-creative schools failing;
  - 27.3. A culture of risk-taking and experimentation, including thinking beyond established practices and rules – bureaucratic hubs that are accountable to ministerially-appointed directors are hardly likely to exhibit such a culture:
    - 27.3.1. They are far less likely to foster innovation than competing, “franchise”-like schools, since the latter at least benefit from their innovations in terms of being able to attract and retain good principals, staff and students;<sup>9</sup>
  - 27.4. An ability to capture the returns from innovation, such as through licencing or other intellectual property protections;
  - 27.5. Adopting innovations made by others, which in turn requires “absorptive capacity” – i.e. local skills and resources for recognising and being able to apply the innovations of others; and
  - 27.6. Freedom from “cultural inertia”, such as that often featuring in organisations with a strong sense of “mission orientation” – which will likely feature strongly in Hubs with directors who are predominantly practicing educationalists.
28. It is not at all clear that the proposed Hubs will feature any or all of these characteristics – indeed, the opposite would seem to be the case:

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<sup>8</sup> See Appendix F.5, and references therein, of Meade, R., 2015, *Economics of Social Services*, technical appendix prepared for the New Zealand Productivity Commission, February.

<sup>9</sup> For a related study, see Hart, O., Shleifer, A. and R. Vishny, 1997, “The Proper Scope of Government: Theory and an Application to Prisons”, *Quarterly Journal of Economics*, 112(4), 1127-1161.

- 28.1. Even if some form of competition will endure between schools themselves (see Section 3.4 below for more), it seems almost inconceivable that there will be any competition at all between hubs, which instead will be bureaucratic, risk-averse, policy- and procedure-based institutions, accountable to politically-exposed government ministers who will not be able to commit to allowing innovators to capture the benefits of their innovations;
  - 28.2. None of this is a formula for Hub-level innovation.
29. More importantly, the Taskforce's proposed five-year caps on principal tenure will seriously undermine school-level innovation incentives:
- 29.1. Schools must innovate in order to differentiate themselves when competing for students, principals and staff, particularly when they cannot use price-based mechanisms (e.g. performance-based salaries) instead; and
  - 29.2. Any school's innovation culture will be strongly determined by its Board's attitude towards risk-taking and experimentation, its principal's innovation capabilities and capacity, and the quality of the team of teaching staff that the Board and principal can retain and attract.
  - 29.3. Importantly, successful innovation can require time for failures to be translated into successes. Additionally, successful innovation often requires long-term investments, included among which are investments in recruiting and training innovative staff, and achieving cultural alignment between the principal and his or her teaching team:
    - 29.3.1. Five year tenure limits for principals are therefore highly misguided, since they eliminate both the ability and incentives of principals to make such long-term investments;<sup>10</sup>
    - 29.3.2. In turn, this means principals will find it harder to recruit and retain capable teaching staff, and obtain their buy-in to whatever culture the principal wishes to create, and innovations he or she wishes to pursue.

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<sup>10</sup> For evidence on the importance of executive tenure on innovation, in not-for-profit contexts which are more likely than profit-oriented contexts to characterise schools, see Musteen, M., Berker III, V. and V. Baeten, 2010, "The Influence of CEO Tenure and Attitude Toward Change on Organizational Approaches to Innovation", *The Journal of Applied Behavioural Science*, 46(3), 360-387.

30. In short, the Recommendations seem to envisage an “open source” innovation environment, in which innovations will be freely made available to all, despite bureaucratic and risk-averse Hubs, and in which principals have less than five years to achieve any school-level innovation in the first place, yet must still compete on non-price terms to attract and retain students and staff:
  - 30.1. Open source innovation works well in certain environments (e.g. in the tech sector), but those environments hold the promise of very considerable financial prizes to parties developing reputations for innovation:
    - 30.1.1. The education sector offers no comparable grand prizes, so if open source innovation is to work as proposed, there would have to be very strong compensatory mechanisms in lieu of such prizes – the Recommendations offer no guide as to what those mechanisms might comprise.
31. Relatedly, it is quite possible that any current innovation failures in the education sector are perpetuated by non-innovating principals who Boards find difficult to remove:
  - 31.1. This, of course, must be judged in light of the wider systemic incentives for principals to innovate in the first place, and the fact that there is not an unlimited pool of principal talent to draw upon, so naturally some principals will be more innovative than others;
  - 31.2. While imposing five year tenure limits on principals might crudely address this particular problem by creating “churn” for under-performing principals, it is a blunt instrument due to simultaneously churning performing principals as well, and undermines their incentives to perform:
    - 31.2.1. If the Taskforce is concerned about under-performing principals being entrenched, to the detriment of innovation, then perhaps it should look at mechanisms to make it easier for Boards to remove such principals, without destroying the incentives of performing principals to innovate.
32. Hence, the Taskforce Report seems to be proposing very blunt instruments to induce higher rates of innovation diffusion across schools, but simultaneously undermines those incentives in the first place, meaning there could be far less innovation to diffuse, even if it is diffused more widely:
  - 32.1. The Taskforce Report presents no evidence that this trade-off is positive, and does not appear to even appreciate that the trade-off exists in the first place.

### 3.4 Misguided Attribution of Failings to Competition

33. The Taskforce Report identifies “unhealthy competition” between schools as a cause of unfairness in educational outcomes:
  - 33.1. This seems to relate to things like schools “cherry-picking” good students from out of zone, with caps on out-of-zone enrolments being one proposed solution;
  - 33.2. It also indicates a desire that schools be more even in size, and that they cooperate and collaborate rather than compete.
34. To the extent that schools compete for enrolments in order to increase their size and achieve economies of scale and scope, any move by the Taskforce to limit the achievement of such economies would seem counterproductive:
  - 34.1. Certainly the Taskforce Report does not provide evidence that sacrificing such economies of scale and scope would be more than outweighed by credible gains in other areas;
  - 34.2. Ironically, this seems to be at odds with the Taskforce’s own apparent pursuit of scale economies at the Hubs level – the Hubs are apparently motivated by the expectation such scale economies will outweigh the governance costs from greater centralisation outlined in Section 3.2 above.
35. Moreover, if schools seek scale because this increases their funding, then this implies that they compete for students because they are responding to the incentives created by funding formulas:
  - 35.1. If that is indeed the case, then reducing competition through blunt means like out-of-zone enrolment caps is merely to address a symptom and not the cause;
  - 35.2. Perhaps the Taskforce should instead propose changes to funding formulas that better provide the sorts of incentives it wishes to create?
36. More fundamentally, and as eluded to in Section 3.3 above, it is naïve to imagine schools not being in competition with each other:
  - 36.1. Principals are charged with achieving quality educational outcomes for the communities they serve;

- 36.2. Their ability to do so depends on them being able to attract and retain quality teaching staff who share their vision for that particular community, and how best to achieve it.
37. In a world in which teaching talent is not unlimited, this necessarily requires competition in the (global) teacher labour market. In a world where labour market competition occurs only weakly in terms of price (e.g. because of pay-scales that poorly reflect differences in teacher quality), then principals must resort to non-price means of competing:
- 37.1. One means, as discussed in Section 3.3, is for principals to innovate – e.g. by providing attractive teaching environments that differentiate their school from others:
- 37.1.1. Further to my comments in Section 3.3, the Taskforce’s desire to more widely diffuse innovations across schools only further diminishes principals’ incentives to innovate, since if all schools adopt their innovations then they are less able to differentiate themselves to attract and retain good staff;
- 37.2. Another form of such non-price competition includes competing for student profiles that better align with the principal’s vision for that community, and which also align with the type of teaching team the principal seeks to achieve that vision.<sup>11</sup>
38. It is true that there are circumstances in which less competition can be better than more. As a PhD-qualified economist who routinely studies problems of imperfect competition across a range of sectors, I feel qualified to determine when this is, or is not, the case:
- 38.1. I hesitate to conclude that inter-school competition presents such an example, and certainly the Taskforce Report presents no compelling evidence or arguments that it does;
- 38.2. Much deeper analysis would be required before concluding less competition is desirable to more in the school sector.
39. Instead, in general terms, competition can be expected to be net beneficial, especially if innovation is a desired outcome:

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<sup>11</sup> Obvious examples include principals trying to achieve literal cultural (e.g. Māori or Pasifika) alignment between students and staff, as well as alignment in terms of (e.g.) sporting, musical or academic aspirations.

- 39.1. Collaboration and cooperation are superficially appealing alternatives to competition, but they arise as dominant methods of organisation only under very specific conditions;<sup>12</sup>
- 39.2. For the Taskforce to demonstrate that collaboration and cooperation are to be preferred over competition between schools, it would have to provide evidence that such specific conditions arise, and are best addressed by reducing competition.
40. Ultimately, of course, it is not possible for the Taskforce to eliminate competition in the education sector:
  - 40.1. Parents choose where to live at least in part based on the educational opportunities afforded by such locational decisions;
  - 40.2. Additionally, some parents have the resources to place their children in private education.
41. For each of these reasons, and in addition to the labour market competition issues raised above, there will always be competition both within the public education system, and between the private and public systems:
  - 41.1. The question which the Taskforce must address (and which it doesn't) is whether the Recommendations, taken in the round, achieve desirable or undesirable changes in all forms of competition – for students, principals and staff – in light of such competition being inevitable to some degree.
42. In conclusion, the Taskforce seems to have adopted an unrealistic view on the incidence, role and merits of inter-school competition, and proposes reductions in competition that may have both unintended and undesirable consequences (not least in terms of innovation, which the Taskforce seems to prioritise).

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<sup>12</sup> One example is so-called “cooperative” business ventures, as are common in many parts of agriculture, but also in banking/insurance, and professional service firms (e.g. lawyers). An important hallmark of such cooperatives is that they address some underlying market failure (e.g. buyer or seller market power, or informational asymmetries), and their costs of collective governance are not too severe (e.g. because the interests of cooperative members are strongly aligned). See Evans, L. and R. Meade, 2005, *The Role and Significance of Cooperatives in New Zealand Agriculture: A Comparative Institutional Analysis*, research report prepared for the New Zealand Ministry of Agriculture and Forestry, December; or Howell, B. and R. Meade, 2016, *Ownership of Tertiary Education Institutions*, research paper prepared for the New Zealand Productivity Commission, September.

## 4. Conclusions

43. It is timely to revisit institutional arrangements for the New Zealand education sector, given they were created three decades ago, in a world quite different to now. However, any changes to those arrangements, as a matter of good policy-making, should only arise if there are sufficiently strong grounds to incur the risks and costs of change:
- 43.1. Specifically, this requires that there are credible benefits of a magnitude sufficient to offset those risks and costs, and by a margin large enough to warrant not investing further in obtaining information and analysis.
44. Importantly, changes to New Zealand's schooling institutions – particularly radical ones of the sort recommended by the Taskforce – should not be made on basis of aspirations or sentiments, no matter how worthy or passionately-held:
- 44.1. Rather, what is needed is a level-headed analysis of the pros and cons of any specific recommended changes;
- 44.2. In turn, this requires a clear assessment of the pros and cons of any specific means being proposed to realise those changes.
45. The Recommendations do not lack aspiration or passion, but they regrettably lack any clear or credible analysis of whether the proposed changes will be net beneficial – on some precise and clear performance criterion – or even feasible.
46. As such, if the Recommendations are implemented:
- 46.1. It is very likely that they will need significant modification as and when practical difficulties arise, as they most likely will; and
- 46.2. Even if they could be implemented without such difficulties arising, it is not at all clear they will lead to a better education system, and indeed, there is a very real risk that they will make it worse.
47. Accordingly, before any of the Recommendations are agreed upon, let alone implemented, there is urgent need for some very level-headed organisational analysis of the sort outlined above to ensure they result in changes that are either necessary, desirable, or superior to possible alternatives.

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