eef The manufacturers' organisation

LIFTING THE LID ON THE LEVY

MAKING THE APPRENTICESHIP LEVY WORK FOR INDUSTRY

In partnership with:

LLOYDS BANK


11:31:27
Colchester

FOREWORD

David Atkinson
UK Head of Manufacturing, Commercial Banking, Lloyds Banking Group

What has always impressed me about the manufacturing industry, is its true commitment to invest in, and train, its people. Long before apprenticeships were the buzzword of the moment, manufacturers were offering high-quality training, and that is still the case today.

These are true apprenticeships – training that combines the right balance of practical and classroom based learning, and that leads to good quality jobs, with high pay.

This report is a valuable addition to the debate on apprenticeships. What really shines through in the findings is the continued commitment to training across the manufacturing sector. Almost half (46%) of manufacturers say they will increase engineering apprenticeship numbers in response to the Levy and a third (35%) plan to increase apprenticeships in other areas of their business.

It also shows that that over a quarter (26%) of manufacturers believe one of the benefits of the Levy will be that it will attract more young people into apprenticeships.

The EEF and Lloyds Banking Group share a common desire to train the next generation of engineers and we want to do all we can to encourage young people to consider apprenticeships as a route into the manufacturing sector.

The yawning skills gap in the manufacturing industry is well documented and needs to be tackled head on. We hope that through a continued focus on training, we can one day close that gap.

David Atkinson
UK Head of Manufacturing, Commercial Banking,
Lloyds Banking Group

EXECUTIVE SUMMARY

Manufacturers are striving to attract and retain the best people and to fill the well-documented skills gaps in our industry. As our Manufacturing Ambitions[1] report found, reducing the skills gap appears to be our sector's Everest. Delivering a more skilled and adaptable workforce is, however, a key pillar for a successful industrial strategy, and therefore needs to take centre stage and be addressed appropriately.

Apprenticeships have for a long time been ingrained within the manufacturing industry and are an effective means both to mitigate the skills gap and to prevent it from widening further. Manufacturers' reliance on apprenticeships to meet their current and future skills needs will undoubtedly increase as Brexit negotiations begin and the UK starts its journey towards exiting the European Union.

The ambitious timeline to implement the Apprenticeship Levy has always been a cause for concern, and with just a couple of months to go, time to prepare remains a key issue for manufacturers. This is against a backdrop of a policy that has been subject to much debate and some significant changes – some positive, some less so – and one that has arguably been taken in isolation.

A joined-up approach is what we need to see from Government policy in all areas, and all the more so when it comes to skills and education. Yet the Apprenticeship Levy has been introduced without fully addressing the wider issues around improving our education system to increase the number of good-quality candidates who can fill employers' vacancies, and the issues around driving up the quality of national training provision to meet the needs of manufacturers, who are continuously investing in new technologies, new processes and new innovations, and putting pressure on demand for higher-level, and often niche, skills.

Our report lifts the lid on the Levy and reveals that manufacturers are finding themselves in scope of the Levy because of complex tax rules, and are automatically disadvantaged because they operate across the UK. They also lose all their current public funding.

The perception that the Levy is nothing more than a tax has not been erased, and a worrying number of manufacturers still see no benefits from it. They lack confidence in their ability to spend their Levy funds, despite plans to increase apprenticeship numbers, both at entry level and within their business. There are also concerns around a lack of time to prepare, the inability to absorb this new cost within the business, and an uncertain future. This uncertainty comes not just from the mechanics and rules of the Levy itself, but also from the wider economic context, particularly in light of Brexit.

While there are many challenges, manufacturers are seeking to embrace the Levy. Our report finds that the Levy should, in the short to medium term at least, increase the number of engineering apprenticeships, encourage manufacturers to think about apprentices in other areas of their business, and use apprenticeships as a means to up-skill and re-skill their existing workforce.

Maintaining this over time, however, is the major worry. The Levy must be a policy that is reviewed and evolved over time to ensure it is fit for purpose and sustainable.

If the Levy is to have a chance of success, changes need to be made, not just to the mechanisms but also to the wider skills system. We have made specific recommendations to the Government to make the Apprenticeship Levy work for manufacturing.

[1] EEF Manufacturing Ambitions (2017)

KEY RECOMMENDATIONS

Recommendation 1: The rules around connected companies has resulted in the smallest of companies being in scope of the Levy. The Government should amend this so that each company (legal entity) receives an allowance.

Recommendation 2: The devolved administrations must give employers clarity on how they will spend their portion of funds that are collected from the Apprenticeship Levy. Manufacturers want to see funding spent on skills and training within their industry, and therefore the funds should be ring-fenced accordingly. Moreover, the devolved administrations must commit to transferable qualifications and equivalent funding to England.

Recommendation 3: Creating greater simplicity by allocating one allowance per company, and not per group, should be coupled with the ability to pool and share digital funds among groups of employers. This will help employers spend more of their digital funds and create more apprenticeships.

Recommendation 4: As demand for Higher and Degree Level Apprenticeships increases, the Government should review the current maximum funding bands. The cost of delivering a Degree Level Apprenticeship in advanced manufacturing and engineering is likely to exceed £27,000 – the current top band – and therefore funding bands should reflect this.

Recommendation 5: While we welcome the decision to allow employers to use digital funds for lower or equivalent level qualifications, the term "materially different" must be flexible and allow for re-skilling within a sector. The Government should empower the employer panels that form part of the Institute for Apprenticeships and Technical Education, which would be a suitable, independent body to decide on this.

Recommendation 6: SMEs need further support to get involved in the design of new standards. The new funding model incentivises employers to deliver apprenticeship standards, which in general attract more funding. However, SMEs are not as engaged in this process as larger firms, particularly those in niche sectors. All new employer panels should have a quota for the number of SMEs appointed to these panels.

Recommendation 7: The Government should increase to 50% the amount of unspent digital funds a Levy-payer can transfer. Only then will it be viewed as a worthwhile transaction from an employer's perspective. Moreover, the Government needs to immediately look to register non-Levy-paying employers on the new Digital Apprenticeship Service, otherwise they will not be eligible to receive the transferred funds.

Recommendation 8: The Government should commission an independent, employer-led review of the implementation and roll-out of the Apprenticeship Levy by the end of 2018. The review should then make recommendations to ensure that the Apprenticeship Levy is fit for purpose and sustainable in the long term.

Recommendation 9: The funding rules and rates only apply for the year 2017-18. This does not give employers the certainty they need. The Government should confirm that the funding rules and rates, including the rate at which the Levy is set and allowances are set, will not change over the course of the Parliament and will remain in place for the lifetime of each Apprenticeship. In addition, the funding bands should increase in line with inflation.

CHAPTER 1: WHAT DO MANUFACTURERS WANT FROM APPRENTICESHIPS?

Manufacturing – the gold-standard apprenticeship

When it comes to looking for gold-standard apprenticeships, look no further than the manufacturing industry. Engrained within our sector, seven in ten manufacturers are currently offering apprenticeships. Only 5% of manufacturers have never had apprentices. When the Government talks about increasing the number of high-quality apprenticeships, they are preaching to the converted.

Despite this, there are elements of apprenticeship policy where there is room for improvement. Recent EEF research found that the biggest barriers facing manufacturers to recruiting *more apprentices* included a lack of good-quality apprentice candidates (cited by 36% of manufacturers), jobs needing to be filled immediately (30%) and a lack of suitable training provision (25%). At the top of the list, however, and for the first time since running our skills survey, was monetary cost, cited by 38% of manufacturers.[2]

When it comes to apprenticeship funding, manufacturers are more than willing to put their hands into their pockets. 71% of companies say they use a combination of employer and public funding to deliver their apprenticeship training, and over (26%) fully fund the training themselves.

Relying solely on employer funding is often a consequence of manufacturers bringing their training in house, which can mean that employers lose access to public funding. This action is usually triggered because employers are unable to buy the training provision they need locally. On other occasions, employers may fund training themselves owing to the complexities involved in accessing public funding.

How apprenticeships are funded in England is going to dramatically change with the introduction of the Apprenticeship Levy (the Levy).

What do manufacturers want from the apprenticeship system?

Before moving on to the Levy, let us take a step back and look at what manufacturers want from apprenticeships, and what they want from the rather complex system that surrounds apprenticeships.

Apprenticeships fit within the wider skills system, which is notoriously difficult to navigate and subject to constant change. It is not uncommon for skills policy to do a complete 360-degree turn. What manufacturers want is a skills system that is as responsive to their needs as they are to their customers. The same rule applies for apprenticeships.

So manufacturers want simplicity and responsiveness. What else?

Good-quality (and a good quantity of) candidates applying for their vacancies. Despite the buzz around apprenticeships, manufacturers still raise concerns about their access to – or more accurately, lack of access to – good-quality apprenticeship candidates. It is the worst-kept secret that manufacturing has a poor image – and this has fuelled the problem of insufficient numbers of candidates applying to manufacturing and engineering apprenticeship vacancies. In particular, we fall down when recruiting female apprentices.

A further challenge is attracting a high calibre of candidates. It is startling that at EEF's Apprentice Training Centre, based in Aston, we received 8,500

[2] EEF Skills Survey 2015-16

applications for 350 posts yet could only fill 330 this year as many of the candidates did not meet the basic entry requirements.

Quality is also key when it comes to provision. For too long, manufacturers have told us that apprenticeship training provision remains “patchy” at best. There are some exemplar examples of FE colleges and providers serving employers’ needs, but this does not happen everywhere.

Employers want greater responsiveness from apprenticeship training providers and colleges. And, as we will explore in subsequent chapters, a silver lining from the Apprenticeship Levy may be that this will finally be achieved – or at least, in part.

But it is not just the role of the provider to drive responsiveness. Manufacturers want apprenticeship standards and frameworks that meet the needs of their business. As we move away from frameworks towards employer-led standards, there are greater opportunities for employers to be firmly in the driving seat, but they must themselves step up to the plate. There needs to be a careful balance of standards that can meet the needs of niche, specialist skills and which ensures transferability for the learner.

Finally, employers want value for money, and a return on investment. Manufacturers see the benefits of offering apprenticeships and consider them a benefit, not a cost. But that is not to say that offering apprenticeships does not come at a price. The ball-park cost of offering and delivering an engineering apprenticeship is around £80-90,000. It is unsurprising then that the top barrier to recruiting an apprentice is now monetary cost. So, manufacturers want simplicity, responsiveness, good-quality candidates, relevant provision and apprenticeship standards, value for money, a return on investment, and, in general, the creation of more good-quality apprenticeships.

The question is – will the Levy help or hinder these asks?

WHAT IS AN APPRENTICESHIP? THE CORE PRINCIPLES:

- Is a job in a skilled occupation
- Is a recognised ‘accreditation’
- Requires substantial and sustained training, lasting a minimum of 12 months and involving at least 20% off the job training (training which is outside of the normal day-to-day working environment)
- Develops transferable skills, and maths and English, to progress careers
- Leads to full competency and capability in an occupation, demonstrated by the achievement of an apprenticeship standard
- Trains the apprentice to the level required to apply for professional recognition where it exists
- Is designed by employers to meet their needs and the needs of their businesses
- Is assessed through a single end point assessment

CHAPTER 2: LEARNING ABOUT THE LEVY

The Apprenticeship Levy and its complexity

In Spring 2017, the way in which the Government funds apprenticeships in England is changing. A new Apprenticeship Levy will be introduced, which will replace all existing funding for apprenticeships in England.

Employers will be required to pay 0.5% of their pay bill towards the Levy, with a £15,000 allowance that they can deduct from their Levy liability. Employers will need to pay the Levy on a monthly basis alongside their PAYE and NI on their HMRC return.

Employers paying in to the Levy will in return receive digital funds which they can spend on apprenticeship training. The amount they receive will be the "English fraction". This is the proportion of their pay bill paid to employees with an English home postcode. They will also receive a 10% top-up from the Government on the amount that they pay into their digital accounts on a monthly basis.

Employers that train apprentices will be able to access digital funds that they can then spend on apprenticeship training and assessment. The amount they can spend is subject to a cap, dependent on the type of apprenticeship they are offering. When it comes to buying the training, Levy-paying employers will pay the provider from their digital accounts. Funds will be taken automatically on a monthly basis, with 20% of the cost held back until completion.

KEY FACTS:
New Apprenticeship Levy to be introduced from April 2017.
The Levy replaces all current funding for apprenticeships.
Single companies, or groups of companies, with a pay bill of more than £3m in scope of the Levy.
Levy-payers must pay 0.5% of their pay bill to HMRC monthly.
Levy-payers have a £15,000 allowance to deduct from their Levy liability annually.
In return, Levy-payers will receive digital funds to be spent on training.
The amount received will be the English "fraction" of your pay bill plus 10% top up from Government.
From 2018, Levy-payers can transfer up to 10% of their Levy funds to another account.
Non-levy-payers will be required to co-invest 10% towards apprenticeship training and assessment.

Any unspent funds will expire after 24 months. From 2018, a Levy-paying employer will be able to transfer up to 10% of their digital funds to another employer's digital account.

Employers not in scope of the Levy will be required to financially co-invest 10% of the cost towards apprenticeship training. The remaining 90% will be funded by the Government. Any apprenticeships started on or after 1st May 2017 will be funded under the new model.

How a Levy-payer will pay into the Levy and pay for training

1. A.Company Ltd has a paybill of £5m. 80% of their pay bill is paid to employees that live in England.
2. The company will receive £8,808 of levy credit each year. This has been calculated as follows: 0.5% of pay bill (£25k) less £15k allowance = £10,000 divided by 12 is £833. £833 x 80% (England fraction) + 10% top up = £734 a month.
3. A.Company wants to train 1 apprentice in Engineering Manufacture - Fabrication & Welding at Level 3.
4. For this apprenticeship they will be able to spend £5,000 over 18 months. 20% of this (£1,000) is held back until completion.
5. The cost is spread out monthly, therefore the cost of training for the first 17 months is £222. This is taken from the company's digital account.
6. On the final month (month 18) the payment will be £222 + 20% withheld (£1,000). Final payment = £1,222.

APPRENTICESHIP LEVY: THE FACTS

FROM APRIL 2017
EMPLOYERS WILL HAVE TO PAY **0.5%** OF THEIR PAY BILL TOWARDS A NEW APPRENTICESHIP LEVY

PAYBILL IS BASED ON TOTAL EMPLOYEE EARNINGS SUBJECT TO CLASS 1 SECONDARY NICs

NI

YOU WILL HAVE A LEVY ALLOWANCE OF **£15,000** PER YEAR

FIRST DECLARATION WILL BE MAY 2017 FOR THEIR APRIL PAY BILL

EMPLOYERS WILL THEN RECEIVE DIGITAL FUNDS, TO THE VALUE OF THEIR LEVY CONTRIBUTIONS

HOWEVER, EMPLOYERS WILL ONLY RECEIVE **VOUCHERS** FOR THE PROPORTION OF THEIR PAY BILL THAT EQUATES TO EMPLOYEE'S WITH AN ENGLISH HOME POSTCODE

THESE DIGITAL FUNDS CAN BE USED TO BUY **APPRENTICESHIP TRAINING**

LEVY PAYING EMPLOYERS **WILL RECEIVE A 10% TOP-UP** ON THEIR DIGITAL FUNDS

THE FUNDS CAN ONLY BE SPENT ON TRAINING FOR AN **ENGLISH** APPRENTICESHIP STANDARD

THE FUNDS CAN ONLY BE SPENT ON AN APPRENTICE WHOSE MAIN PLACE OF WORK IS IN **ENGLAND**

NEW FUNDING MODEL STARTS 1ST MAY **2017**

PRE-MAY 2017 APPRENTICESHIPS **WILL KEEP** CURRENT FUNDING

YOU CANNOT USE LEVY VOUCHERS ON APPRENTICESHIPS STARTED **BEFORE 1ST MAY 2017**

PAYMENTS FOR TRAINING **WILL LEAVE** DIGITAL ACCOUNTS **ON A MONTHLY BASIS**

NON-LEVY PAYERS WILL BE REQUIRED TO **CO-INVEST 10%** TOWARDS THE COST OF TRAINING

DIGITAL FUNDS CAN ONLY BE SPENT ON **POST-MAY APPRENTICESHIPS**

This information is correct as of November 2016

Are manufacturers in scope of the Apprenticeship Levy?

The complexity of the connected companies rule

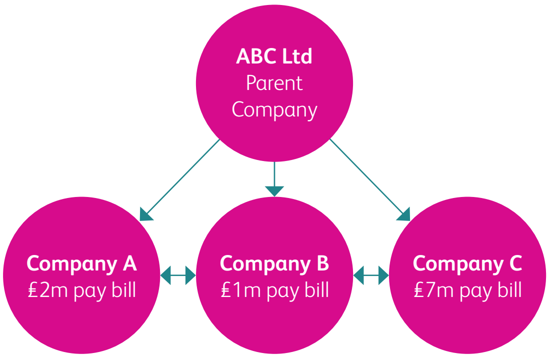
Our survey, targeted at companies who had shown a prior interest in the Apprenticeship Levy, revealed that 81 % of companies are in scope of the Levy, 16 % are not and 3 % do not know.[3]

The question then is, why are so many manufacturers saying they will be required to pay the Levy?

Much of the answer to this question lies around the "connected companies" rule. Under this rule, only one allowance of £15,000 is allocated to a group of connected companies. Companies within the group must decide how they will split the allowance, or whether they wish to nominate one company to receive all the allowance.

Ultimately, if a company is part of a group and that group in its entirety has a pay bill of more than £3m, then it will be in scope of the Levy. Here is what this looks like.

How the connected companies rule brings manufacturers in scope of the Levy



ABC Ltd, is the Parent Company of **Company A, Company B and Company C.** Collectively the group has a pay bill of **£10m.** ABC Ltd has decided that **Company C will receive all of the £15,000 allowance.** Therefore the three companies' levy liabilities would be as follows:

Company A: 0.5 % of £2m = £10,000 levy liability
Company B: 0.5 % of £1m = £5,000 levy liability
Company C: 0.5 % of £7m = (minus £15,000) = £20,000 levy liability

Definition of a connected company: The basic rule for determining whether two companies are "connected" with each other is if one of them has control of the other or if both are under the control of the same person or persons. The term "control" is given the same meaning as in sections 450 and 451 of the Corporation Tax Act 2010. This is where a person has or is entitled to acquire the greater part of the share capital or voting power in a company, or in the event of a distribution of the company's income the greater part of the amount distributed, or in the event of distribution of assets the greater part of the company's assets.

How can I check if my company is connected?

- Look at your last Companies House return.
- Look at your last annual report.
- Speak to your auditor.
- Find out your arrangements for paying corporation tax (although this may not be the same for paying into the Apprenticeship Levy.)

[3]EEF Apprenticeship Levy Survey 2016-17

The importance of the connected companies rule

The connected companies rule casts the Levy net far wider. While more than a third (35%) of companies that said they would be in scope of the Levy because they are a single entity with a pay bill of more than £3m, almost half (46%) said they would be paying the Apprenticeship Levy because they are a connected company (generally part of a group) and the group has a total pay bill of more than £3m.

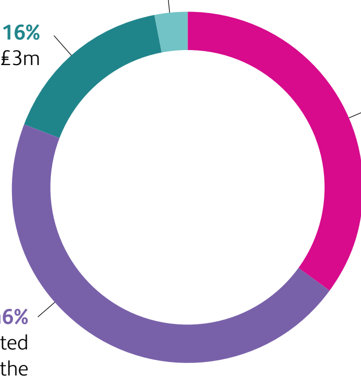
As more detail about the funding rules surrounding the Apprenticeship Levy were released, EEF saw a surge in queries and questions from manufacturers around the connected companies rule.

Because of the rules around connected companies, the Levy isn't just for "large firms". Our survey findings revealed that companies with fewer than 50 employees are in scope of the Levy, some because they themselves are a single company with a pay bill of more than £3m, and others because they are part of a wider group. For some manufacturers, finding themselves in scope of the Levy has come somewhat as a surprise, having initially ruled themselves out, as so much of the Government and wider stakeholders' collateral has focused on employers with a pay bill of more than £3m.

Recommendation 1: The rules around connected companies has resulted in the smallest of companies being in scope of the Levy. The Government should amend this so that each individual company receives an allowance.

Chart 1: Manufacturers find themselves in scope of the Levy

% companies citing whether they are in scope of the Levy



Source: EEF Apprenticeship Levy Survey 2016-17

Table 1: Which manufacturers are in scope of the Levy and why?

No. of employees in company	In scope of the Levy as a single company	In scope of the Levy because part of a group	Not in scope of the Levy	Don't know if in scope of the Levy
1-50	7.7%	7.7%	84.6%	0.0%
51-100	9.1%	18.2%	63.6%	9.1%
101-250	45.2%	48.4%	0.0%	6.5%
251+	40.7%	59.3%	0.0%	0.0%

Source: EEF Apprenticeship Levy Survey 2016-17

The implications of operating across the UK

Why the devolution of education and skills policy creates challenges

Following queries around the connected companies rule, the other area which has caused a great detail of confusion for employers is how the Levy will operate across the UK.

Skills is a devolved policy. However, the Apprenticeship Levy is a tax. What this means in practice is that the Levy applies to all UK companies and their respective UK pay bills. However, what they receive in terms of digital funds to then spend on training only equates to the "English fraction" of their pay bill. This is the proportion of their pay bill paid to employees with an English home postcode.

Manufacturers operate across the UK. They can often be multi-sited across regions and devolved nations. Almost all (98%) of respondents to our survey have their individual sites located in England, with 1% in Scotland and 2% in Wales. However, loss of funding occurs when manufacturers have employees who live in Scotland, Wales and Northern Ireland, and this is more acute. 12% of manufacturers said they have employees who live in Scotland, 16% in Wales and 5% in Northern Ireland. For all these companies, they will not get back from the Levy what they have to pay in, because they only get back the "English fraction".

Manufacturers want to see the Levy spent on skills and training across the UK

Employers that operate across the UK and have employees that live in the devolved nations struggle to understand why the Levy will operate in this way. It has been a subject that has caused great irritation. This has been exacerbated by the lack of information and guidance as to how the devolved administrations will act in response to the funding that they will receive from the Apprenticeship Levy.

A difficult pill for employers to swallow is that the funding the devolved administrations will receive does not have to be spent on apprenticeships. In fact, it does not have to be spent on skills and training. There is currently no ring-fencing in place. Manufacturers are, however, clear that they want this funding to be spent on skills and training within their industry.

Recommendation 2: The devolved administrations must give employers clarity on how they will spend their portion of funds that are collected from the Apprenticeship Levy. Manufacturers want to see funding spent on skills and training within their industry, and therefore the funds should be ring-fenced accordingly. Moreover, the devolved administrations must commit to transferable qualifications and equivalent funding to England.

AN ILLUSTRATIVE EXAMPLE OF HOW THIS WORKS:

ABC Manufacturing is a precision engineering firm based in the North East of England. It is a single company with 1000 directly employed employees. The company's UK pay bill is £35 million. Therefore, its Levy liability is going to be £160,000 (0.5% of £35m =£175,000 minus £15,000 allowance = £160,000). However, the company has employees that live in Scotland as well as England. 250 of their employees live in Scotland. These employees' wages account for 30% of the total pay bill. Therefore, ABC Manufacturing will only get 70% of their Levy liability back in digital vouchers. This amounts to £112,000. They will however receive a 10% top-up from Government. Therefore, receive £123,000 in Levy vouchers to spend on training each year.

SUMMARY:

- More manufacturers are in scope of the Levy because of the rules around connected companies.
- Manufacturers that operate across the UK are worse off because the levy is UK-wide, but what employers get back only relates to their English pay bill.

CHAPTER 3: READY, STEADY, LEVY

Since its initial announcement at the 2015 Budget, the policy has been somewhat of a roller coaster and a subject of much debate.

EEF made its position on the Apprenticeship Levy clear: manufacturers do not support the principle of a Levy. We had major concerns that the Levy could incentivise the wrong behaviour from employers and lead to a rebadging of low-level, low-quality training not akin to the high-quality, gold-standard apprenticeships seen in the manufacturing industry.

Since then a raft of announcements have been made. Some of these EEF have flagged as areas of concerns; others are more positive, and can be seen as wins for the manufacturing industry. We are almost at a point where the majority of information has been published, although much of this is short term and applicable to 2017-18 only.

How prepared are manufacturers?

Information read, but processes not updated

The Levy is a step change in not only the way the Government funds apprenticeships, but also how employers buy training. It will require preparation and planning from employers.

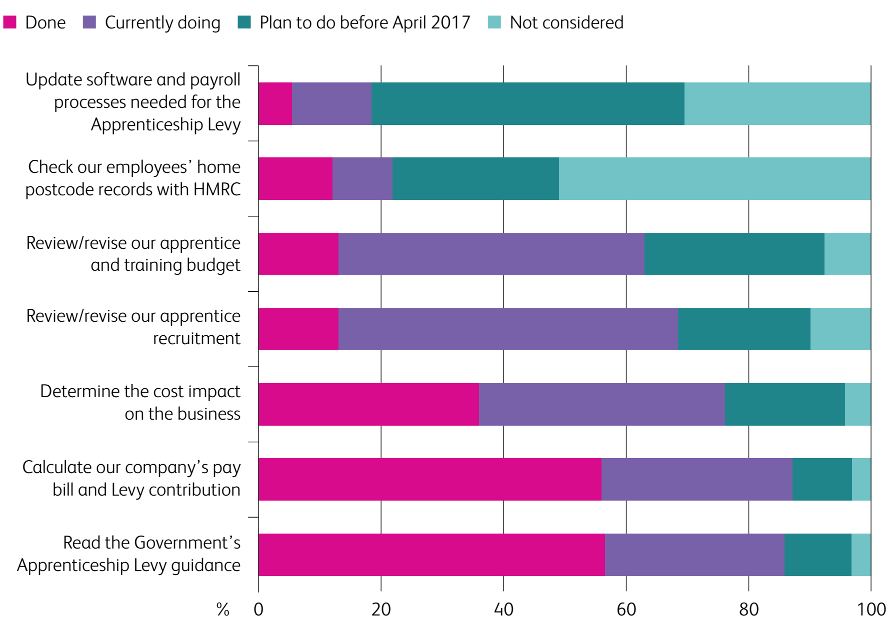
Manufacturers have begun to take the necessary action to prepare themselves for the Levy. However, the focus to date has been around paying into it. Almost six in ten manufacturers have read the Government's Apprenticeship Levy guidance and a further 30% were in the process of doing so.

While manufacturers have in general read the guidance, many do not think it adequately addresses their concerns or answers their questions. A post-webinar survey found that just 25% thought the guidance answered their questions.[4] This is a view shared by many.

More than half (56%) have already calculated their company's pay bill and Levy liability and a further 31% are in the process of doing so. The next step is determining the cost impact on the business. However, only around a third (36%) of companies say they have already done this, and 40% are currently doing so. This is concerning. Determining the cost implications on the business is an important discussion that businesses should be having. This policy change cannot be taken in isolation within a business. It requires input from a range of contacts within a business which may include HR, Payroll, Finance and MDs/CEOs.

Chart 2: Manufacturers have taken the basic steps

% companies citing what steps they have taken ahead of the Apprenticeship Levy



[4]EEF Apprenticeship Levy Webinar 2016

Source: EEF Apprenticeship Levy Survey 2016-17

Updating payroll and software process

The Levy will interact with payroll systems and will require employers to ensure that their records of employees' home postcodes are aligned with the records held currently with HMRC. Ensuring that both of these are up to date had not been considered by a number of manufacturers.

Indeed, more than half of companies had not considered checking their employee records with HMRC. This is particularly important for those companies that have employees who live in the devolved nations. Similarly, three in ten had not considered whether they would need to update their software and payroll processes to deal with the additional payment of the Levy.

Back to those tricky connected companies rules

Splitting and sharing allowances

As mentioned in the previous chapter of this report, connected companies are entitled to just one £15,000 allowance, and they must decide how this is to be split between them, whether by splitting the £15,000 into various parts or allocating it to one single company.

The decision on how to split the allowance will need to be made at the time of the first payment to HMRC. This cannot then be changed during that financial year. Of those companies who are in scope of the Levy, less than a third (32 %) had made a decision on how to split the allowance. More than half (53 %) said they had not and 15 % did not know.

Pooling digital funds

A further piece of the puzzle is the decision whether or not to "pool" digital funds as a group, or whether to spend digital funds on an individual basis. The new Digital Apprenticeship Service (DAS) will allow for additional PAYE references to be added to an account at a separate time.

It's not a case of one-size-fits-all here. Employers are looking for advice and guidance as to whether they should – as a group of companies – pool their digital funds. However, such decisions can only be made on a case-by-case basis.

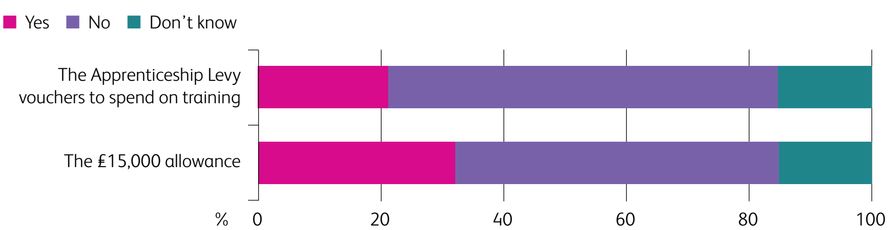
A company that, for example, has an R&D site that only recruits PhD level graduates may see little need for their respective Levy digital funds and may therefore decide to pool their digital funds together with another part of the business that is in a better position to utilise them.

Other companies will see a strong case for keeping their Digital Apprenticeship Service (DAS) accounts, and therefore digital funds, completely separate. They may, for example, be connected to a parent company, but have few or no dealings with the other subsidiaries within the group.

It is unsurprising, then, that few manufacturers have made a decision on whether they will spend their Levy digital funds as a group or single companies. Only one in five (21 %) has done so, with almost two-thirds (64 %) having not yet decided and 15 % not knowing whether this decision has been made.

Chart 3: Groups of companies have not yet made vital decisions

% companies citing whether they have decided on splitting their allowance and sharing their digital funds



Source: EEF Apprenticeship Levy Survey 2016-17

Recommendation 3: Creating greater simplicity by allocating one allowance per company, and not per group, should be coupled with the ability to pool and share digital funds among groups of employers. This will help employers spend more of their digital funds and create more apprenticeships.

Recruitment and budget decisions have yet to be made

Manufacturers have yet to determine the impact the Levy will have on apprenticeship recruitment and training budget decisions. Only a handful (13%) of companies have reviewed or revised their apprenticeship recruitment, and the same number again have reviewed or revised their apprenticeship and training budget. That said, a large number – almost half – have already begun this process, with the remainder generally planning to do so before April 2017.

Given that the final funding rules and funding caps were announced at the end of October 2016, it is likely that employers are only now fully considering their options and next steps for recruitment.

Important discussions are now being held. For example, our industry has traditionally recruited apprentices within the academic year. However, with an expiry date on digital funds which starts ticking as soon as funds enter an employer's digital account, employers are now considering the options for rolling apprenticeships (apprenticeships that start throughout the year). This is particularly attractive for employers that plan to use apprenticeships as a channel to up-skill or re-skill their existing workforces. Employers cannot do this alone, however, and colleges will themselves need to become more flexible and more responsive to employers' needs. And with the money now in employers' hands, colleges and providers that don't become more flexible will risk falling by the wayside.

Brexit: why recruitment and training plans are more important than ever

The discussions mentioned above are all the more important as Brexit negotiations take place and the UK prepares to leave the European Union. With the Government's Brexit White Paper stating that the Free Movement Directive will no longer apply and the migration of EU nationals will be subject to UK law, there is a great deal of uncertainty and concern among employers in their ability to fill their vacancies and meet their companies' skills needs.

It is vital therefore that manufacturers plan current and future recruitment within this context. Manufacturers must ensure that they have a pipeline of talent coming into the industry, taking into consideration the ageing demographic of the manufacturing workforce and the knowledge that Free Movement will soon end. In addition to this, manufacturers must also look at their skills and recruitment needs in the immediate and medium term, and where entry-level apprentices will not be able to fill these skills gaps. Manufacturers will need to look at whether apprenticeships could be effective in up-skilling and re-skilling their workforce. We will explore this in the next chapter, looking at what actions manufacturers will take in response to the Levy.

SUMMARY:

- Manufacturers have done their reading on the Levy and have started to crunch their numbers to understand their Levy liability.
- However, there is much more to be done. Only a handful have checked their own records with those of HMRC, which is important given the complexities of the devolution issue explained in the previous chapter.
- The difficulties of being connected companies raises its head again, with fewer than a third of companies having made decisions on how to split their allowance, and even fewer making decisions on whether or not to pool their digital funds.
- While some recruitment and training decisions have been made, this is not enough, and manufacturers need to be making these decisions in the context of Brexit, which may affect their plans further in the near future.

CHAPTER 4: LIFTING THE LEVY LOAD

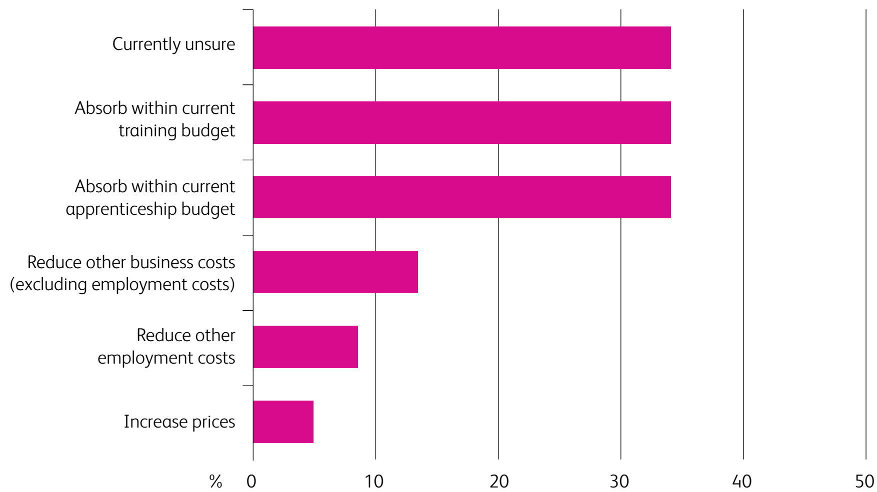
Lifting the Levy load

For many manufacturers, the Apprenticeship Levy will be a significant cost, one that will hit them at a time of great uncertainty following the UK's decision to leave the European Union. Despite some substantial sums being paid out by manufacturers, a third of companies (34%) are still unsure as to how they will cover the cost of the new Apprenticeship Levy.

For many, the Levy will come from their current apprenticeship (34%) or training (34%) budgets. Some 13% plan to reduce business costs (excluding employment costs), and just 9% plan to reduce employment costs – unsurprising given the level of costs that will hit businesses, as mentioned above.

Chart 4: Training budgets take the hit of the Levy

% companies citing how they will absorb costs of the Levy



Source: EEF Apprenticeship Levy Survey 2016-17

As with many other costs facing businesses – such as the National Living Wage – manufacturers do not see increasing prices as a way to absorb additional costs, as this was cited by just 5% of companies. Manufacturers must remain competitive, including on price, and increasing costs to customers is not seen as an option.

Making the Levy work

An up-tick in planned recruitment of engineering apprentices

The tide is turning on how manufacturers plan to act in response to the Apprenticeship Levy. When asked in early 2016 what action they would take, 41% of companies said no action. This has fallen to 8% of manufacturers, the majority of which will pay into the Levy. Whether manufacturers view the Levy as a tax or a talent generator, not many plan to simply write it off.

The number of manufacturers now saying they will increase manufacturing and engineering apprenticeships has also risen, with 46% saying they will do so in response to the Levy. This will be music to the Government's, and indeed our, ears. The Government wants to create three million apprenticeship starts over the course of the Parliament. Manufacturers want more quality apprenticeships created. A happy medium could be on the cards.

of manufacturers said that financial support for costs associated with recruiting apprentices would support them with the implementation of the Levy

The October funding announcement – which committed to additional funding for STEM (science, technology, engineering and maths) apprenticeships and significant increases in a number of engineering frameworks and standards among the funding bands – is likely to have played a part. A key principle of the Levy from EEF has been that it covers the true cost of training, and the October 2016 announcement gave a nod in this direction.

In line with trends from EEF's previous skills survey, manufacturers are increasingly seeing the value of placing apprentices in other parts of the business, with 35% saying they will increase recruitment of non-manufacturing and engineering apprentices, such as IT, sales and marketing.

The expanded use of apprenticeships does, however, call into question what impact the Levy will have on the recruitment of graduates. Until now, recruitment of engineering graduates has been on par with apprentices; however, the Levy may change this.

Recommendation 4: As demand for Higher and Degree Level Apprenticeships increases, the Government should review the current maximum funding bands. The cost of delivering a Degree Level Apprenticeship in advanced manufacturing and engineering is likely to exceed £27,000 – the current top band – and therefore funding bands should reflect this.

EEF'S APPRENTICESHIP LEVY WINS FOR MANUFACTURERS – AUTUMN 2016

- Increasing the expiry date of the digital funds Levy-payers will have to spend on training to 24 months, giving employers more time to spend their funds and adjust to the new system.
- EEF sitting on a new employer group to determine how the new system can allow Levy-paying digital funds to transfer/spend their unused funds on apprenticeship training in supply chains and the wider industry.
- Confirmation of the increase funding for STEM (science, technology, engineering and maths) apprenticeship frameworks – increased by 40% for Level 2 Apprenticeships and 80% for Level 3.
- A number of new standards including Machinist (Advanced Engineering) and Food and Drink Manufacture Engineer moving into higher bands, therefore attracting more funding.
- Key engineering apprenticeship frameworks including Engineering Manufacture in Aerospace, Electrical and Electronic Engineering and Automotive, all moving up into higher bands and again attracting more funding.
- Removing the restrictions requiring employers to choose one provider to deliver at least 50% of their apprenticeship training, therefore giving employers greater flexibility to choose training providers of their choice.
- Increased funding for 16- to 18-year-olds in a transition period, which will be of benefit to EEF members who are more likely to recruit younger apprentices.
- Confirmation that employers will be able to fund apprenticeships where learners have lower, equivalent and higher qualifications as long as the training is "materially different", therefore allowing our members to spend their levy funds on re-skilling and up-skilling.

Up-skilling and re-skilling remains the focus

The most common action taken by manufacturers will be to turn existing training into apprenticeships. This will not be without its challenges.

Apprenticeship Levy digital funds can only be used to re-skill and up-skill where there is a higher-level qualification to obtain, or where the qualification is equivalent or lower but the training is "materially different". The definition of "materially different" is likely to be a sticking point. While we may all be able to agree that a history graduate retraining as a Level 3 engineering technician is "materially different", there will undoubtedly be more debate when re-skilling within a sector.

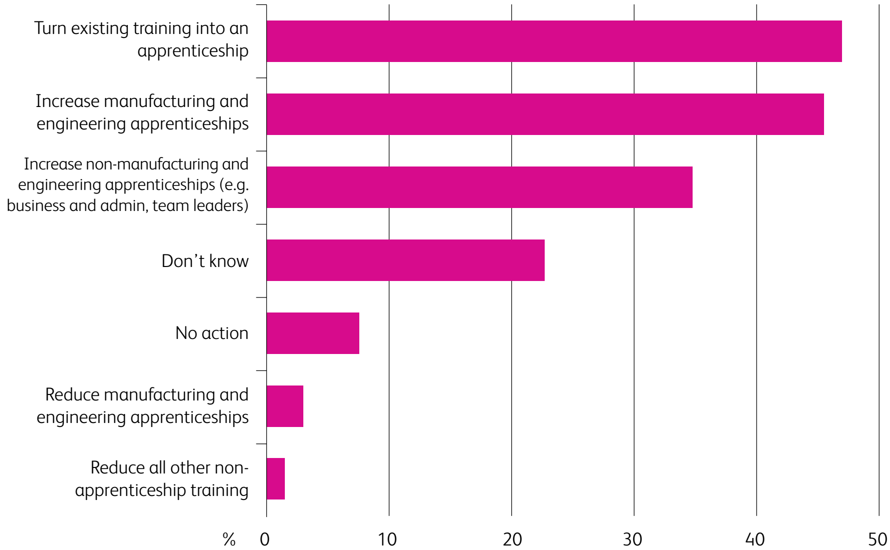
Manufacturers would view a move from electrical to mechatronics (engineering) as "materially different", and the Government must ensure that this flexibility is maintained. Determining what is "materially different" should be a role for the expanded Institute for Apprenticeships and Technical Education.

Recommendation 5: While we welcome the decision to allow employers to use digital funds for lower or equivalent level qualifications, the term "materially different" must be flexible and allow for re-skilling within a sector. The Government should empower the employer panels that form part of the Institute for Apprenticeships and Technical Education, which would be a suitable, independent body to decide on this.

[5] EEF Skills Survey 2015-16

Chart 5: Up-skilling and re-skilling will be the focus of the Levy

% companies citing action in response to the Apprenticeship Levy



Source: EEF Apprenticeship Levy Survey 2016-17

Our 2016 Skills Survey revealed that the skill-sets most in demand among manufacturers were leadership and management and people and line management.[5] We predict that we will see an increased uptake in demand for such apprenticeships, for example the new Team Leader and Supervisor Standards, some of which are at Level 5.

Niche skills needs do not easily fit into existing frameworks and standards

The other major difficulty facing employers is the lack of relevant apprenticeship frameworks and standards that meet their often niche and specialist skills needs. It is important that new standards are flexible enough to allow a learner to move from sector to sector, or from industry to industry. However, manufacturers investing in technologies and new processes often have niche, specialist needs. It can be difficult for such companies to find

of manufacturers want more support to turn current training into an approved apprenticeship framework or standard relevant standards, and then to find a provider willing and able to deliver this effectively.

Even if companies do come together and design standards, they need to feel confident that colleges and providers will deliver them. While larger organisations may have greater purchasing power as they can benefit from economies of scale, smaller companies, who are also in scope of the Levy, may not.

Recommendation 6: SMEs need further support to get involved in the design of new standards. The new funding model incentivises employers to deliver apprenticeship standards, which in general attract more funding. However, SMEs are not as engaged in this process as larger firms, particularly those in niche sectors. All new employer panels should have a quota for the number of SMEs appointed to these panels.

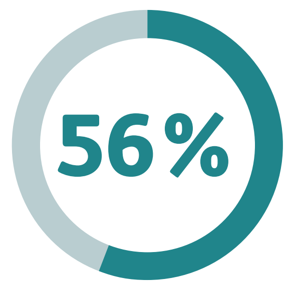
Providers must be sufficiently resourced to deliver an increased demand for new training

With new standards being developed, training providers and colleges will need to step up to the plate to deliver high-quality training that meets employers' needs. For manufacturers, continuous investment and improvements to new technologies, processes and innovations, coupled with their ambitions to take advantage of the fourth industrial revolution, will mean that demand for responsive provision will increase further. With the purchasing power now in employers' hands, there will be an expectation that providers are able to quickly and effectively meet their needs. However, some additional capital investment will be required. Therefore, any existing or new capital funding should be directed towards providers and colleges that can demonstrate genuine employer investment, an ability to deliver high-quality STEM training of wider economic value, and capability to deliver higher-level training, again reflective of the needs of industry. This includes the recently announced funding for new Institutes of Technology.

Transferring of digital funds

The Government has begun to recognise that employers are unlikely to spend all their Levy digital funds, and has made a commitment to allow employers to transfer up to 10% of their unspent Levy digital funds to another employer's digital account from 2018. EEF, together with other business groups, third sector and public sector representatives, currently sits on a Steering Group to determine how best to make that happen. This is not an easy task. Complex state aid rules and choosing the best method to allow for transferability creates challenges. At a level of 10% there is a major risk that the benefit gained from being able to transfer digital funds will not offset the bureaucracy of having to undertake the process under strict guidelines. Employers may be left wondering whether it is actually worth it.

of manufacturers want more information on available apprenticeship frameworks and standards



of manufacturers said that more information on finding and recruiting apprentices will help them with the implementation of the Apprenticeship Levy

Recommendation 7: The Government should increase to 50% the amount of unspent digital funds a Levy-payer can transfer. Only then will it be viewed as a worthwhile transaction from an employer's perspective. Moreover, the Government needs to immediately look to register non-Levy-paying employers on the new Digital Apprenticeship Service, otherwise they will not be eligible to receive the transferred funds.

Saturation point?

Clearly, manufacturers are going to act positively in response to the Apprenticeship Levy in the immediate term. The challenge will come when the Levy will have been in place for a number of years and employers reach a point of saturation, i.e. they cannot increase their Apprenticeship numbers, either through new recruits or their existing workforce. The former will be particularly challenging for those companies that must maintain strict headcounts.

Up-skilling and re-skilling of employees to a new and materially different apprenticeship standard will be easily achieved in the short term, but continuously doing so will become more challenging. Government must ensure that apprenticeship training continues to add value, otherwise there is a risk that we will end up asking the question, are apprenticeships still fit for purpose?

Manufacturers are likely to continue to recruit entry-level apprentices on an annual or a bi-annual basis, but by no means in the volumes they would need to reach in order to get back what they put into the Levy on an annual basis.

Recommendation 8: The Government should commission an independent, employer-led review of the implementation and roll-out of the Apprenticeship Levy by the end of 2018. The review should then make recommendations to ensure that the Apprenticeship Levy is fit for purpose and sustainable in the long term.

CHECKLIST

To use digital funds or co-investment the individual learner must:

- ✓ Start their apprenticeship after the last Friday in June of the academic year in which they have their 16th birthday
- ✓ Be able to complete the apprenticeship in the time they have available
- ✓ Not be enrolled on another apprenticeship at the same time as any new apprenticeship they start
- ✓ Not be asked to contribute financially to the direct cost of learning or assessment.
- ✓ Not use a student loan to pay for their apprenticeship
- ✓ Spend at least 50% of their working hours in England over the duration of the apprenticeship
- ✓ Have the right to work in England
- ✓ Be employed by you the employer or the connected company

SUMMARY:

- The Levy should, at least in the short to medium term, result in new apprenticeship enrolments and the up-skilling of existing employees where appropriate.
- For this to happen effectively, the Government support is needed to ensure that employers have access to relevant provision, both in terms of new standards and delivery partners (training providers and colleges).
- There is a concern that there will be a point at which employers cannot recruit more new apprentices, or utilise apprentices in their existing workforce. Therefore, the Government will need to take into consideration whether the Apprenticeship Levy is sustainable in its current form.

CHAPTER 5: TAXING TIMES

A positive spin on the Levy

Manufacturers have a proven track record of delivering high-quality apprenticeships. Apprenticeships have been ingrained within manufacturing businesses for decades. Some manufacturers see the benefits of the Levy as demonstrating the value of apprenticeships.

- A quarter of manufacturers think the Levy could increase the quality of apprenticeships.
- A quarter think the Levy could attract more young people into apprenticeships
- Three in ten think that the Levy gives them the opportunity to increase the number of apprenticeships within their business.

Manufacturers also see the potential of having greater purchasing power from the Levy than they currently have now. The Levy is a significant shift away from FE colleges and providers drawing down funding and deciding what training they sell to employers and towards an employer-driven market, where employers decide where to spend their Levy funds. As a result, a quarter of companies believe the Levy will increase the responsiveness of providers to deliver relevant training, and three in ten say they will benefit from the purchasing power to buy the apprenticeship training their business needs.

Taxing times

Despite some positive findings on what the Levy could achieve, more than a third of manufacturers (34%) see no benefits of the Apprenticeship Levy. Manufacturers are far more likely to cite their concerns about the Apprenticeship Levy than they are to cite the benefits. Manufacturers feel that the Levy is being imposed on them, when they have historically been offering high-quality apprenticeships. Many feel that they have been tarred with the same brush as other employers that do not train or have been free-riders to training to date.

Despite the positive wins for the industry around additional funding for STEM and specific engineering apprenticeships, manufacturers do not think they will be able to get back what they pay into the Levy.

To this end, the Levy is continued to be seen by some as a tax only.

of manufacturers say getting back the value of their Levy liability is one of their biggest concerns about the Apprenticeship Levy

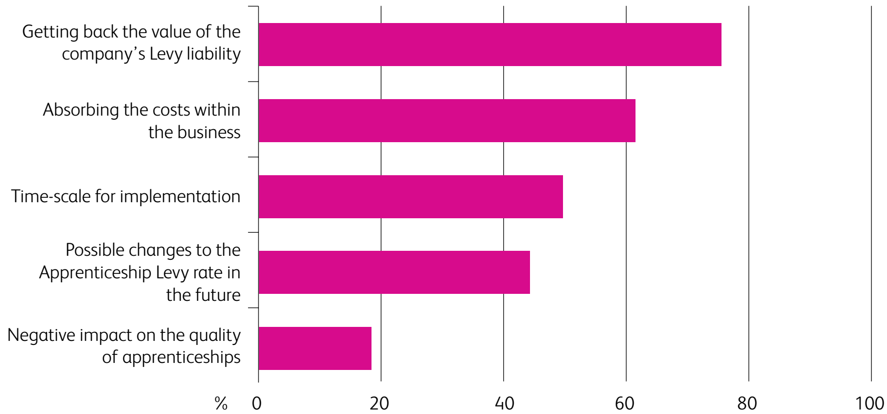
of manufacturers see no benefits to the Apprenticeship Levy

Other key issues:

- **COST.** More than six in ten (61%) of companies say they are concerned about absorbing the costs within the business. As mentioned previously, 2017 will be a year of significant employment costs at a time when the industry continues to face a high degree of economic and political uncertainty.
- **TIME TO PREPARE.** A vast amount of information has been published, yet employers are struggling to digest this information, and increasingly queries are now on a case-by case basis. Half of companies say they are concerned about the timescale of implementation. The number of companies that have not yet taken quite basic actions of determining their Levy liability is concerning given we are now just months away.
- **UNCERTAINTY.** Manufacturers do not feel confident that the funding rules and rates will not change. The funding rules themselves are just for the year ahead, and provide employers with little certainty about the future. As a result, 44% of firms are concerned about possible changes to the Apprenticeship Levy rate in the future.

Chart 6: Manufacturers have major concerns around the Levy

% companies citing biggest concerns of the Apprenticeship Levy



Source: EEF Apprenticeship Levy Survey 2016-17

Recommendation 9: The funding rules and rates only apply for the year 2017-18. This does not give employers the certainty they need. The Government should confirm that the funding rules and rates, including the rate at which the Levy is set and allowances are set, will not change over the course of the Parliament, and will remain in place for the lifetime of each Apprenticeship. In addition, the funding bands should increase in line with inflation.

SUMMARY:

- Manufacturers see some advantages of the Apprenticeship Levy. Primarily these are around having greater purchasing power for the provision they need. Others believe the Levy will provide their business with opportunities to create more apprenticeships within their company.
- However, the disadvantages far outweigh these benefits, with a third of manufacturers seeing no benefits from the Apprenticeship Levy.
- The Levy is still viewed by many as a tax, with a worrying three-quarters of manufacturers saying they are concerned that they will not get back what they put into the Levy, no matter how hard they try.
- Other key concerns focus around the cost, time to prepare and uncertainty, all of which need to be addressed by the Government.

CHAPTER 6: CONCLUDING REMARKS

At the beginning of this report, we looked at what manufacturers wanted from an apprenticeship system. We must take this together with the Government's aim – to create three million apprenticeships in England. If the Levy is to achieve either, let alone both, of these aims, action must be taken now and continue to be taken in the future to amend and evolve this brave new world of apprenticeship funding.

We have always said that apprenticeship funding policy (the Levy), should not be taken in isolation. Employers cannot dramatically increase entry-level talent within a pipeline of young people applying for their apprenticeship vacancies. Equally, employers cannot continue to up-skill and re-skill existing employees if there are no relevant standards to meet their needs or certain other training is legally compulsory and does not fit into an apprenticeship standard.

We are sceptical that the Levy will help meet the Government's three million target, and even more sceptical that it will create three million quality apprenticeships. All we do know is that manufacturers are looking to step up to the plate wherever they can.

There is more that the Government could do to support employers with the introduction, implementation and utilisation of the Levy. Various announcements in recent months have demonstrated that the Government is showing willing and wants to incentivise more high-quality apprenticeships. But the Government must also demonstrate that it is willing to continue to work with employers, and that the Levy, and the accompanying digital infrastructure that surrounds it, will evolve over time.

Our report has lifted the lid on the Levy. We now need a firm commitment from the Government to evolve the policy to be responsive to employer needs, and a commitment from employers to embrace the changes. But only time will tell whether the Levy has been a help or a hindrance.

CHECKLIST

Before paying into the Levy you should have:

- ✓ determined whether you are a connected company and have decided how the allowance will be split
- ✓ calculated your Levy liability
- ✓ estimated what proportion of your pay bill equates to those employees who live in Scotland, Northern Ireland and/or Wales
- ✓ checked your employee records are up to date
- ✓ estimated your Levy credit (what you'll get back in digital funds)
- ✓ checked your payroll systems are able to manage the new Levy

Before getting ready to register for the Digital Apprenticeship Service you should know:

- ✓ your Government Gateway login details for any PAYE schemes you want to include in your account
- ✓ your Companies House number or charity number (if your organisation has one)
- ✓ how you want to structure your account to manage your apprenticeships if your organisation is part of a group of connected companies
- ✓ who in your organisation will register for your DAS account
- ✓ who in your organisation will manage your DAS account
- ✓ who in your organisation will have access to (and be able to view) your DAS account

Before spending your digital funds you should have:

- ✓ undertaken a skills diagnostic within your business, including what skills you need now and in the future and where apprenticeships could fit within the business
- ✓ had a look at the list of apprenticeship standards and frameworks available and the funding bands of these
- ✓ aligned your apprenticeship recruitment needs with your Levy credit forecast
- ✓ determined when is best to start your apprentice enrolments based on your Levy credit forecast and when your digital funds will expire
- ✓ considered the HR implications for any workforce re-organisation

EEF LEVY SERVICES

At EEF we are here to help you through each step of the Apprenticeship Levy.

We offer a range of services from providing you with a skills diagnostic to managing your Digital Apprenticeship Service (DAS) account to a complete end-to-end Apprenticeship Levy managed service.

With two state-of-the-art technical training centres and a portfolio of UK wide training facilities, we support all aspects of training needs. We are specialists in the recruitment, upskilling and training of engineering and manufacturing apprentices.

For more information:

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EEF is dedicated to the future of manufacturing. Everything we do is designed to help manufacturing businesses evolve, innovate and compete in a fast-changing world. With our unique combination of business services, government representation and industry intelligence, no other organisation is better placed to provide the skills, knowledge and networks they need to thrive.

We work with the UK's manufacturers from the largest to the smallest, to help them work better, compete harder and innovate faster. We're committed to developing the engineering skills of the future. That's why we've invested in two multi-million pound, purpose built training centres in Birmingham, which deliver world-class apprenticeships and technical skills training.

And, because we understand manufacturers so well, policy-makers trust our advice and welcome our involvement in their deliberations. We work with them to create policies that are in the best interests of manufacturing that encourage a high growth industry and boost its ability to make a positive contribution to the UK's real economy.

Our policy work delivers real business value for our members, giving us a unique insight into the way changing legislation will affect their business. This insight, complemented by intelligence gathered through our ongoing member research and networking programmes, informs our broad portfolio of services; services that unlock business potential by creating highly productive workplaces in which innovation, creativity and competitiveness can thrive.

www.eef.org.uk

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