The Treasury

Budget 2011 Information Release

Release Document

June 2011

www.treasury.govt.nz/publications/informationreleases/budget/2011

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[2] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[3] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[4] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information

[5] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

[6] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

[7] 6(a) - to prevent prejudice to the security or defence of New Zealand or the international relations of the government

[8] 9(2)(h) - to maintain legal professional privilege

[9] 6(c) - to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial

[10] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand

[11] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, an [8] appearing where information has been withheld in a release document refers to section 9(2)(h).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Office of the Minister of Finance

Memorandum for Cabinet

Budget 2011: Assignment of Efficiency Dividend Proceeds to "Better Services for Less" Initiatives

Proposal

1. This paper proposes that $6 million of the $868 million (over five years) of funding released by the termination of central funding for state sector employer contributions to retirement income schemes be assigned to two new one year funding pools designed to test a pipeline of cross-agency investments to generate ongoing savings and accelerate the pace of the government's "Better Services for Less" agenda. If this test demonstrates value by delivering "Better Services for Less" savings I will seek to extend funding for outyears.

Executive Summary

2. The companion paper "Efficiency Dividend for Budget 2012' seeks Cabinet's agreement to the broad design parameters of an efficiency dividend on core government administration that will apply from 1 July 2012 but will be announced as part of the forthcoming Budget. The dividend will be a key tool for both incentivising – and capturing a share of the benefits from – the transformation of public services. A significant share of the cashable savings generated by the efficiency dividend will be applied to government priorities, including debt reduction.

3. The other companion paper "Budget 2011: Making Kiwisaver More Cost-Effective" is seeking – amongst other measures – Cabinet's agreement to the termination of central funding for state sector employer contributions to Kiwisaver, the SSRSS and TRSS from 1st July 2012. In practice the termination of this funding represents the 'first tranche' of the efficiency dividend. It is therefore appropriate that Cabinet concurrently considers whether any portion of these savings should be assigned to testing an ongoing pipeline of cross-agency investments that will generate ongoing savings and contribute to the government's "Better Services for Less" agenda.

4. Senior Chief Executives have stated that a well telegraphed baseline funding reduction is a preferable way of generating seed finance for cross-agency initiatives than the repeated 'top slicing' of departmental baselines at short notice. There is also concern that in the absence of a central pool of seed finance many promising ideas to deliver "Better Services for Less" across the public sector are lying dormant.

5. While progress has been made in pursuing some cross-agency ICT investments such as the Infrastructure as a Service (IaaS) initiative, dedicated funding for common ICT capability development is now exhausted and a suite of promising initiatives has stalled. For other functional areas, such as human resources and

finance, there has been no progress in developing common capabilities due to the lack of a developmental pipeline.

6. Assigning funding to the development of an ongoing pipeline of cross-agency investments will provide greater assurance that the ambitious efficiency dividend targets will be achieved. In many cases the achievement of the efficiency dividend savings will necessitate significant transformation towards business models that leverage scale across the public sector, rather than just incremental efficiency adjustments.

7. This is a new approach and requires testing to demonstrate value. Subject to this funding delivering value by delivering further “Better Services for Less” savings I propose to seek further outyear funding to support this approach in Budget 2012.

8. I propose that in the 2011/12 year $6 million of the $868 million (over five years) of savings released by terminating central funding for state sector employer contributions be reassigned to test the value of two new cross-agency investment pools:

    - a Vote: Internal Affairs appropriation to fund the development of a portfolio of potential cross-agency ICT investments from conception through to detailed business cases ($3 million); and

    - a new “Better Services for Less” 2011 Budget tagged contingency to fund a development pipeline of cross-agency initiatives to reshape the efficiency and quality of public services, including initiatives relating to procurement, human resources, finance, insurance, property, corporate & executive services, policy advisory services, and frontline services ($3 million).

9. This paper sets out the intended uses and governance associated with these two funding pools.

Background

Efficiency Dividend

10. The companion paper “Efficiency Dividend for Budget 2012’ seeks Cabinet’s agreement to the broad design parameters of an efficiency dividend on core government administration that will apply from 1 July 2012 but will be announced as part of the forthcoming Budget. The dividend will be a key tool for both incentivising – and capturing a share of the benefits from – the transformation of public services. A significant share of the cashable savings generated by the efficiency dividend will be applied to government priorities, including debt reduction.

[2]

12. There may be some refinement to this base as the detailed design of the efficiency dividend progresses.

Termination of Central Funding for Kiwisaver, SSRSS and TRSS

13. The companion paper "Budget 2011: Making Kiwisaver More Cost-Effective" is seeking – amongst other measures – Cabinet's agreement to the termination of central funding for state sector employer contributions to Kiwisaver, the SSRSS and TRSS from 1st July 2012. In practice this represents the 'first tranche' of any efficiency dividend, not only for the departments that fall within the scope of the proposed dividend, but also for those departments and Crown entities that fall outside its scope.

14. Given the termination of central funding for state sector employer contributions to retirement income schemes is effectively the first tranche of any efficiency dividend it is appropriate that Cabinet concurrently considers whether any portion of the consequential savings should be assigned to testing the value of a pipeline of cross-agency investments that contribute to the government's "Better Services for Less" agenda.

'Better Services for Less'

15. The fiscal discipline generated by ongoing cost pressure, coupled with the forthcoming efficiency dividend, should be sufficient to incentivise the creation of a developmental pipeline of projects ongoing savings at the individual agency level. This will; also be the case for some projects involving small clusters of agencies.

16. The pace of transformation is likely to accelerate as agencies respond to the latest round of administrative and support benchmarking data. Recent benchmarking by the Better Administrative and Support Services (BASS) team within Treasury indicates that a reduction in variability in efficiency across agencies could, conservatively, reduce A&S spending by $236 million annually for the 33 participating agencies.

17. Existing cross-agency initiatives have demonstrated the potential to make significant savings by leveraging scale and building common capabilities across the public sector:

    - The government procurement reform programme is projected to save $115 million over five years;

    - The one.govt communications services are projected to save $230 million of direct benefits over 10 years. If indirect benefits are included the savings increase to $400-$600 million;

    - The ICT Infrastructure as a Service (IaaS) initiative is projected to save around $200 million over 10 years; and

18. In most cases dedicated funding has been made available to develop these projects, including procurement reform, one-govt and IaaS. The Department of Internal Affairs has now exhausted its dedicated funding for common capability development. As a consequence a suite of promising ICT initiatives has stalled. For other functional areas, such as human resources and finance, there has been no progress in developing common capabilities due to the lack of a developmental pipeline.

19. Without some central coordination and funding there is unlikely to be sufficient investment in the development of a cross-agency developmental pipeline that leverages scale across the public sector. This is because of:

- **Unknown benefits**: agencies face weak incentives at the individual level to invest in a developmental pipeline of cross-agency projects where, ex-ante, they can't accurately estimate how any benefits will fall across the affected agencies – this will only be clear upon the completion of detailed business cases for projects;

- **Dispersed benefits**: the option of assigning a lead agency to invest in a cross–agency developmental pipeline is unlikely to succeed because that agency is won't anticipate receiving a significant share of the benefits and can't be confident of recouping its investment. The 'free rider' problem associated with cross-agency initiatives means a collective response is appropriate.

- **Transaction costs**: where lead agencies try to generate seed finance through subscription models they generally incur substantial costs due to the senior management effort associated with fund raising, and the associated delays in getting work underway. The initial stages of the procurement reform suffered from this.

- **The absence of appropriate mandates** means there is a tendency to settle on lowest common dominator solutions that satisfy as many agencies as possible rather than those that maximise savings across the public sector.

20. Even in the case of small clubs of agencies pursuing 'Better Services for Less" progress can be significantly adversely affected by the uncertainty of future resource commitments. The Managed Desktop initiative being led by the Department of Conservation and New Zealand Transport Agency is a good example.

21. Senior Chief Executives have signalled that a well telegraphed reduction in baseline funding is a preferable way of generating seed finance for cross-agency initiatives than the repeated 'top slicing' of departmental baselines at short notice. The use of ad-hoc approaches can be disruptive to departmental financial planning.

22. Allocating specific funding will provide a clear signal across the state sector that Ministers are serious about a long term programme of reform, will result in an acceleration of the reform programme, and will engender greater participation by a wider range of agencies in cross-agency reform initiatives such as those on the Common ICT Capability Roadmap.

23. It is proposed to test the returns from a developmental pipeline over a one year period before committing outyear funding to this approach.

Proposal

[2]

- a new Vote: Internal Affairs appropriation to fund the development of a portfolio of potential cross-agency ICT common capability investments from conception through to detailed business cases ($3 million); and

- a new "Better Services for Less" 2011 Budget tagged contingency to fund a development pipeline and ongoing investments in cross-agency initiatives outside of the ICT roadmap, including initiatives relating to procurement, human resources, finance, insurance, property, corporate & executive services, policy advisory services, and frontline services ($3 million).

Development Pipelines

25. Implementing formal development pipelines draws on established business practice to offer a structured process that filters ideas through managed stages in order to accelerate those with the greatest potential to deliver either cashable savings or significant improvements in efficiency or effectiveness across the state sector. This approach is proven to shorten exploration time (reducing costs) and provides regular off-ramps to jettison unpromising ideas.

26. Assessing ideas in the early stages of the pipeline can cost as little as $20,000 whereas developing the analysis required for a detailed business case can cost up to $2 million. This illustrates the value of filtering ideas at each stage to ensure that only the strongest ideas are progressed.

ICT Capability Investment

27. The ICT Directions and Priorities (CAB Min (10 35/5A) provides a clear mandate for the development of initiatives on the ICT Common Capability Roadmap and ICT Ministers have already established a robust governance structure for these initiatives.

28. Annex A illustrates the development pipeline process and includes specific examples of ICT initiatives that can enter at more advanced stages of the pipeline and, therefore, have the potential to be accelerated through to provide business cases in the next financial year.

29. The Department of Internal Affairs has exhausted available funding to progress a range of cross-agency ICT capability initiatives, including those set out in Annex A.

30. For an expenditure of $3m per annum, the ICT pipeline tests would be expected to deliver an average of five detailed business cases for services with an estimated $10 million cumulative savings per annum. These estimates are based on recent experience with ICT common capability initiatives, and the number of ideas currently at different stages of development that require funding to progress.

31. The ICT Strategy Group, chaired by the Chief Executive of the Ministry for Economic Development and including the Chief Executive of DIA (appointed GCIO) and the Chief Executive of LINZ in its membership, will act as the governance group for the management of ideas through the stages of the pipeline. They will take advice and recommendations on priorities from the newly established ICT Council (independently chaired by Sam Knowles).

32. The ICT Strategy Group will provide ICT Ministers with regular reports on initiatives that are entering and progressing through the pipeline.

33. Each business case exceeding $25 million whole of life costs will proceed through the two step Cabinet approval process for Capital Assets (Ref CO (10) 2).

"Better Services for Less" Tagged Contingency

34. Outside of the Common ICT Capability roadmap, potential savings and service enhancements have also been identified from other common capability initiatives. These include areas such as procurement, human resources, finance, insurance, property, corporate & executive services, policy advisory services, and the transformation of frontline services.

35. For procurement a development pipeline is already in place for the category management of goods and services, but there is no scope to explore opportunities in areas such as "procure to pay" common processes.

36. For the finance function there is no development pipeline, but there are opportunities to explore management information system strategies and processes, debt recovery, financial management capability development, and insurance.

37. For human resources there is no development pipeline,but there are opportunities to explore recruitment, payroll, benefits/allowances, strategic HR capability, training & development, and the establishment of discipline based heads of profession.

38. For Corporate and Executive Services, but there are opportunities to explore legal services, library and document management, and government communications.

39. Unlike the ICT pipeline many of the ideas being generated in these areas are at early stages of development and require significant more work. For this reason, we propose use of a tagged Budget contingency where credible ideas will be approved by Cabinet before funds are drawn down.

40. The Chief Executives Group on Government Business Reform will play a key role in filtering requests to draw down this contingency.

41. Following the standard approach to Budget contingencies this tagged contingency will be extinguished on 1 February 2012. However, should this test deliver the value I anticipate, I will develop a proposal to extend funding in Budget 2012.

Options for Implementation Funding

42. Funding for the implementation of reform initiatives which have been developed to maturity through the pipeline will continue to use the existing guidelines for Cross-Agency Initiatives Processes (CAIP). The current range of options available for implementation funding include;
    - direct charging of the recipients of a service provided;
    - transactional charging as a fee on the purchase of goods or services from a 3rd party; and

- ‘club’ arrangements where agencies share implementation costs across participants, with contributions being in cash or ‘kind’.

43. Decisions on funding of successful business cases will remain with Cabinet, through the Expenditure Control Committee.

Consultation

44. The Chief Executives of the Ministry of Economic Development and Department of Internal Affairs, and the State Services Commission and Department Prime Minister and Cabinet (DPMC) were consulted in the preparation of this paper.

Financial Implications

45. The table below summarises the savings arising from terminating the central funding for state sector employer contributions to KiwiSaver, the SSRSS and TRSS from 1st July 2012, along with the funding sought for the two ‘Better Services for Less” initiatives. The savings outlined in this table are dependent on approval of the companion paper “Budget 2011: Making Kiwisaver More Cost-Effective”

46. I propose that $6 million of the savings from Vote: State Services be notionally brought forward for utilisation in the 2011/12 financial year in order to ensure continuity of work that is already underway.

47. It is proposed the appropriation for Vote Internal Affairs is reviewed in 2012/13 to ensure it has been set at an appropriate level. This appropriation has no outyear implications beyond 2014/15.

Fiscal Savings Vote State Services Minister of State Services (Non Department Other Expense)	**$ m (operating expenses)**				
	2011/12	**2012/13**	**2013/14**	**2014/15**	**2015/16**
KiwiSaver: State Sector Employer Contributions		[2]			
State Sector Retirement Savings Scheme: State Sector Employer Contributions					
Total Gross Fiscal Savings					
Vote: Internal Affairs Departmental Output Expense appropriation Cross-Government ICT Investment Proposals	3.00				
Budget 2011 “Better Services for Less” tagged contingency	3.00				
Total “Better Services for Less” Initiatives	**6.00**				
Total net increase (decrease)	**6.00**	[2]			

Human Rights

48. There are no inconsistencies between the proposal and the Human Rights Act 1993.

Legislative Implications

49. None

Regulatory Impact Analysis

50. This proposal has no regulatory implications.

Publicity

51. No current implications

Recommendations

52. It is recommended that Cabinet:

1. **note** that the companion paper "Efficiency Dividend for Budget 2012' seeks Cabinet's agreement to the broad design parameters of an efficiency dividend on core government administration that will apply from 1 July 2012 but will be announced as part of the forthcoming Budget;

2. **note** that in addition to releasing cash for government priorities, the introduction of the efficiency dividend provides an opportunity to test the development of a pipeline of cross-agency investments that will generate ongoing savings and acclerate the government's "Better Services for Less" agenda;

3. **note** that Senior Chief Executives have signalled that a well telegraphed baseline funding reduction is a preferable way of generating seed finance for all-of–government initiatives than the repeated 'top slicing' of departmental baselines at short notice;

4. **note** that existing cross-agency initiatives have demonstrated the potential to make significant savings by leveraging scale economies and building common capabilities across the state sector;

5. **note** that the companion paper "Budget 2011: Making Kiwisaver More Cost-Effective" seeks Cabinet's agreement to:

   5.1 terminate central funding for state sector employer contributions to KiwiSaver, the State Sector Retirement Savings Scheme (SSRSS) and the Teachers' Retirement Savings Scheme (TRSS) from 1 July 2012;

5.2 the following changes to appropriations, with a corresponding impact on the operating balance, to reflect the termination of central funding for employer contributions to KiwiSaver, SSRSS and TRSS;

	$m – increase/(decrease)				
Vote State Services **Minister of State Services**	**2010/11**	**2011/12**	**2012/13**	**2013/14**	**2014/15&** **Outyears**
Non Department Other Expense: KiwiSaver: State Sector Employer Contributions State Sector Retirement Savings Scheme: State Sector Employer Contributions			**[2]**		
Total Operating					

6. **note** that the termination of central funding for state sector employer contributions to retirement income schemes represents the first tranche of the proposed efficiency dividend, and it is therefore appropriate to consider whether a portion of the savings in recommendation 5.2 should be assigned to testing the development of an ongoing pipeline of cross-agency initiatives;

Cross-agency ICT Capability Investments

7. **note** that Cabinet has established the ICT Council and ICT Strategy Group to develop the ICT Roadmap. The ICT Strategy Group will report to ICT Ministers on initiatives as they proceed through the pipeline;

8. **note** that the Department of Internal Affairs has exhausted available dedicated funding to progress a range of cross-agency ICT capability initiatives, such as those set out in Annex A;

9. **agree** to establish a new Departmental Output Expense appropriation with respective scope statement, for the development of a portfolio of potential cross-agency ICT capability investments, as follows;

Departmental Output Expense	**Scope Statement**
Cross-Government ICT Investment Proposals	This appropriation is limited to developing investment proposals relating to potential cross-government common ICT capability initiatives and detailed business cases for selected initiatives to inform investment decisions by Ministers.

10. **approve** the following changes to appropriations to provide for the development of a portfolio of potential cross-agency ICT capability investments, with a corresponding impact on the operating balance and debt;

	$m – increase/(decrease)				
Vote Internal Affairs **Minister of Internal Affairs**	**2010/11**	**2011/12**	**2012/13**	**2013/14**	**2014/15 Only**
Departmental Output Expense: Cross-Government ICT Investment Proposals (funded by revenue Crown)		3.000			
Total Operating		**3.000**			

11. **agree** that the new appropriation for Vote Internal Affairs be reviewed in 2012/13 to ensure it has been set at an appropriate level;

12. **note** that the governance of initiatives utilising this approach will include the ICT Steering Group, the ICT Council and regular referral of portfolio initiatives to ICT Ministers

"Better Services for Less" Tagged Contingency

13. **note** there is a wide range of cross-agency capability investments, outside of the ICT roadmap, that warrant development as part of the government's "better services for less" agenda;

14. **note** that relevant initiatives include those relating to procurement, human resources, finance, insurance, property, corporate & executive services, policy advisory services, and frontline services;

15. **approve** the establishment of the following tagged 2011 Budget contingency to fund a test of a development pipeline and ongoing investments in cross-agency initiatives of the nature described in recommendation 14 above;

	$m – increase/(decrease)				
	2010/11	**2011/12**	**2012/13**	**2013/14**	**2014/15 & Outyears**
"Better Services for Less" Tagged Budget contingency		3.000			
Total Operating		**3.000**			

16. **note** that The Chief Executives Group on Government Business Reform will play a key role in filtering requests to draw down this tagged contingency;

17. **agree** that this tagged contingency will be extinguished on 1 February 2012.

18. **note** that if this approach delivers the expected value in identifying and accelerating further "Better Services for Less" savings I will develop a proposal to extend this funding in Budget 2012.

Hon Bill English
Minister of Finance

_____/_______/__