

The Treasury

Ministry of Social Development Baseline Review Information Release

June 2019

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MSD Baseline Review Interim Report
Slide pack for Minister of Finance and Minister for Social Development
11 December

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Baseline Review Themes

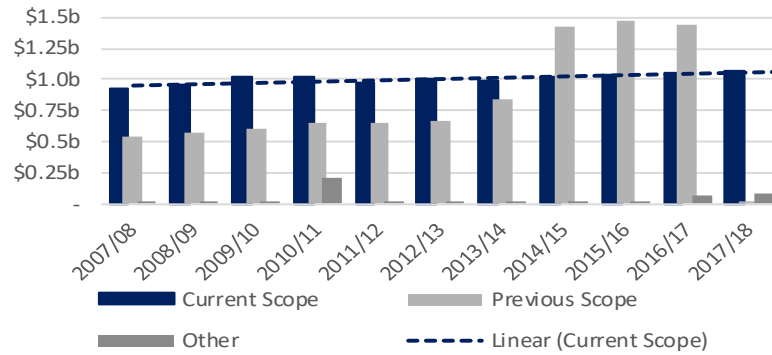
The themes below draw together the common threads within the interim report.

Cost pressures (Slide 5-6, 11, 12, 13)	<ul style="list-style-type: none"> • There is limited scope to manage future cost pressures within baselines without making trade offs, such as reducing staff of contracted spend. Over the last 10 years MSD has self-funded significant cost pressures without a corresponding increase to baselines. • While Budget 19 cost pressure bids will address current cost pressures, any potential future efficiency savings have not yet been factored in, as the Te Pae Tawhiti and Better Everyday changes are still in the early stages of development.
Efficiency (Slide 8, 10, 12)	<ul style="list-style-type: none"> • Within its current processes and systems, MSD is broadly efficient at administering the welfare system, the current Technology systems carry significant risk. Reforming its processes and systems provides an opportunity for both efficiency gains and outcome improvements for clients. Though, further work and investment will be required to realise these gains. • A broader cross sector review of contracting is needed to lift the efficiency and coordination of Government community spending.
Effectiveness (Slide 9, 10)	<ul style="list-style-type: none"> • Optimised effectiveness of employment outcomes can only achieved when investment is balanced between reactive transactional processing, proactive case management and employment readiness programmes. Increasing demand and processing complexity is crowding out proactive support. This is driven by increasing housing costs relative to main benefits. There are choices to be made to increase employment funding, accept declining proactive assistance or alter main benefit levels. • Lack of evidence does not mean that investment has lower value. There is good evidence supporting the effectiveness of investment in employment outcomes. Community-based investment however is less well evidenced as data is of a lower quality or in some case not available. Evidence is also generally harder to source. • New investment in employment and community programmes should be looked at in the context of the total existing spend with a cohort and its effectiveness.
MSD's role (Slide 10, 13)	<ul style="list-style-type: none"> • MSD's role in the social sector needs clarification. For example: <ul style="list-style-type: none"> • what is MSD's role in achieving outcomes in communities, and how does this intersect with the role of other social sector agencies? • what is MSD's role in providing policy advice in terms of core welfare system policy versus wider social/community development policy, and also its role in providing cross-sector policy advice? • MSD's scope has changed a lot over the past four years. Constant change can have negative efficiency impacts.
Future direction (Slide 15)	<ul style="list-style-type: none"> • A significant opportunity exists to build on the gains from Simplification (a programme that simplified and automated some processes) through Te Pae Tawhiti and the Better Everyday programme to improve efficiency and client outcomes. • Scope for improvement will require a coordinated change in people, process, delivery channels and systems. This will also require major up front investment.

Understanding MSD

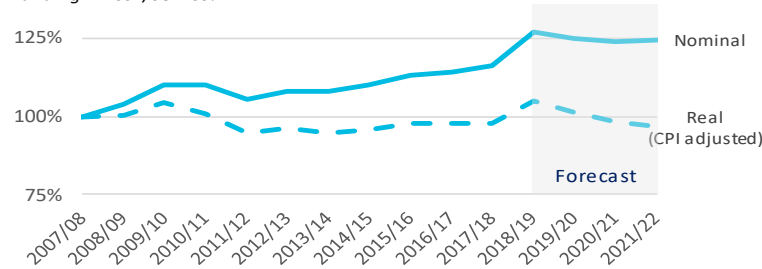
Where has MSD come from?

Scope changes mean MSD is a different organisation from a decade ago



MSD's funding has increased slightly to fund increased scope

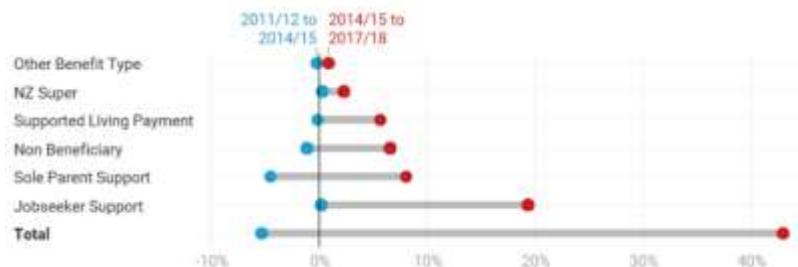
Funding in 2007/08=100%



Source: Treasury analysis

Hardship Grants have grown significantly since 2014/15

Contribution to growth over 3 year periods (%)



Significant changes that have impacted on the organisation's operations and functions include:

- creation of Oranga Tamariki
- broadening MSD's scope to include housing
- creation of the Ministry of Housing and Urban Development, and
- the Welfare Reform programme, including the introduction of Multi-Category Appropriations, providing flexibility to manage employment and community spend.

The funding for core Ministry activity has increased by around 25% since 2007/08, however, **in real terms funding has declined slightly**. Funding increases have been associated with an increase in the scope of services for core clients (such as housing).

MSD has adopted a number of strategies to manage its cost and demand pressures. **There is limited scope to continue these cost management strategies into the future (see next slide).**

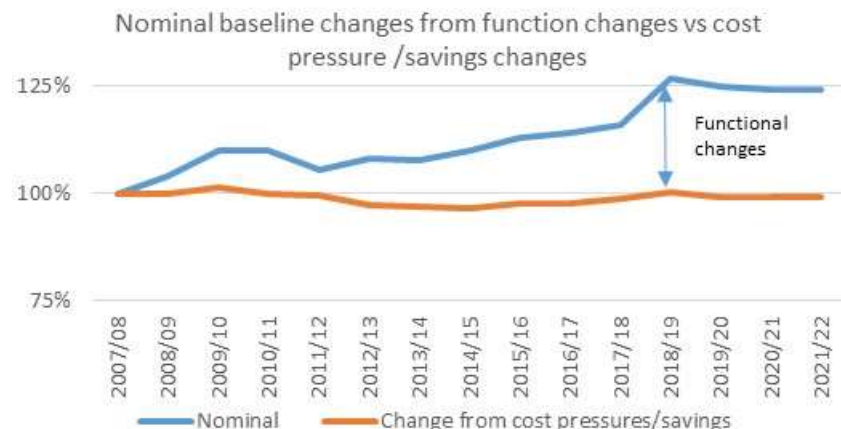
MSD's resources to support its clients are under increased strain. Client needs have become more complex over the last decade. Increasing use of tier 2 and 3 benefits, which require more effort to administer than main benefits, and responsibility for facilitating emergency housing support is placing more demand on MSD's resources.

The number of clients on tier 1 benefits (excl. NZ Super) has increased over the last 2 years, returning to 2013 levels. The number of clients receiving NZ Super has steadily increased over the last decade. MSD can manage this demand through straightforward processes, and increasing use of digital channels.

Growth in more administratively intensive transactions is driving greater effort in administering the welfare system. There has been more than 40% growth in applications for tier 3 benefits (e.g. hardship grants) since 2014/15. Application growth has occurred across all benefit groups. These transactions represent a more complex client need, and more demand on MSD to understand need and provide support. One example is the emergency housing grant, where a client may require an immediate housing solution.

Increased administrative effort and complexity of client need is currently being addressed reactively, with MSD decreasing proactive work focused engagement. This approach is notionally cheaper in the short-term, but likely more expensive and less effective over the long-term. Increased volumes of applications are being handled online or over the phone (25%) but this is not enough to take pressure off of the frontline.

How has MSD managed its cost pressures?



Net changes to MSD's baseline have come from funding to increase the scope of operations. Any additional funding for cost-pressures has been balanced by savings initiatives that returned funding to the centre.

MSD has been fully or partially meeting cost pressures over this period through efficiencies (for example, shifting more transactional processes online through MyMSD) and through the deferral of spending. Some cost pressures have been compounded by a loss of economies of scale in the splitting out of Oranga Tamariki and some housing functions.

There is limited scope for MSD to continue these cost management strategies into the future, without additional investment.

The table below outlines MSD's previous cost-management strategies.

	Cost Management Strategy	Savings (\$)	Comment
Repeatable	Automation	>\$20m pa	Only repeatable with significant investment. Further savings related to process/rule changes and new technology are possible. Likely that this would occur through implementation of Te Pae Tawhiti
Non-repeatable	Reducing capital charge	\$80m (capital)	MSD returned capital to lower capital charge. This is one of the drivers related to the recapitalisation budget bid.
	Delaying capital expenditure	<\$10m	MSD capping capital expenditure. "Sweating assets" to reduce depreciation is no longer feasible without increasing asset risks. This is one of the drivers for the capital budget bid.
	Carrying forward underspends	<\$20m	Treasury has an expectation that these underspends are returned to the centre.
	Minimising wage growth and tech investment	<\$20m	These strategies are related to the remuneration and capital bids.
	General Surplus	1-2% of annual baseline	These surpluses have not been possible in the last 5 years.
	Value-for-money project	<\$5m	Current prioritisation exercises have a similar objective, though funding is returned to centre.
	Other efficiency drivers "totem-poles"	<\$10m	The savings were mainly in discretionary expenditure –publications, travel and catering and an internal redistribution to meet cost pressures in other areas. Limited scope for further savings.

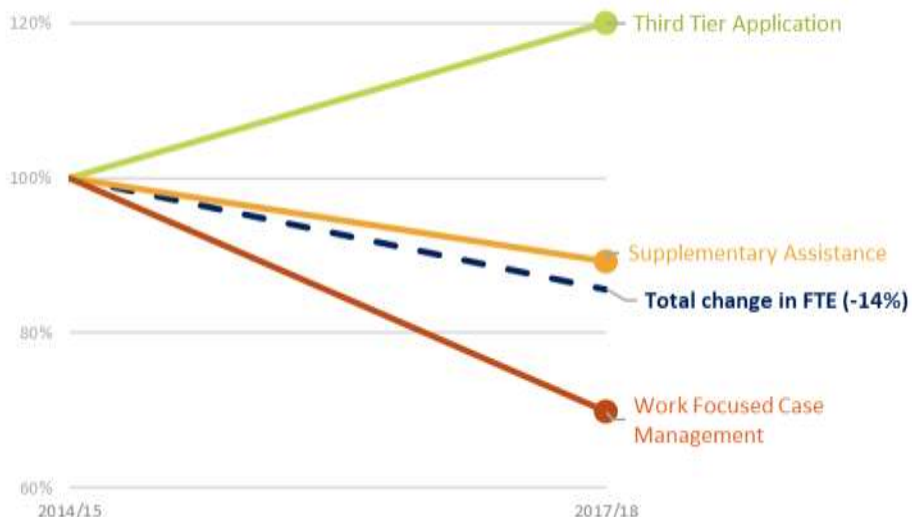
Areas of Focus

I. Area of Focus: Administration & Delivery of the Welfare System

Where has MSD come from?

Case manager time (FTE) by activity - (indexed to 2014/15)

Changes between 2014/15 and 2017/18



Simplification has broadly reduced the frequency of simple tasks and the duration of complex tasks for frontline case managers.

Increased demand for Supplementary Assistance and complexity to administer 3rd Tier assistance (i.e. hardship grants) crowds out the time available for proactive employment conversations (i.e. WFCM). This crowding-out has seen engagement rates fall from 45% in 2014/15 to 22% in 2017/18. This rate shows the share of clients receiving proactive work-focussed engagement from their case managers over the month.

Funding for *Administrative and Delivery* is budgeted to remain flat through to 2022/23. **Population growth and increased scope/complexity has added to baseline pressures**, including the 2016 introduction of Special Needs Grant for Emergency Housing that are driving a large increase in hardship assistance demand.

Despite overarching gains from simplification, efficiencies have lagged in specific areas. For instance, applications for student loans and support have decreased 13% and 22% respectively since 2012/13, despite funding increasing 5%. Performance is falling – quality/accuracy measures are trending downwards. Impacts of fees-free reforms yet to fully realised.

Where is MSD now?

MSD's initial bid is for [8] over 4 years. Indicative Treasury analysis shows funding has mostly been allocated to increasing engagement rates to 2014/15 levels, with the remainder meeting demand growth over the period.

Existing systems will struggle to sustain the gains in productivity and client experience from Simplification. Customers continue to demand end-to-end service integration. **Current rules and process changes, as part of *Te Pae Tawhiti*, are a significant opportunity for both efficiency gains and improved client outcomes.**

In real terms, the value of Main Benefits have decreased over the past decade or so, while housing costs have increased. **This has shifted people towards administratively resource intensive Tier 2 & 3 benefits schemes.**

Well understood demand pressures from ageing populations. However, current cohort of pre-retirees are less able to transition to retirement compared to previous cohorts:

- Home ownership of pre-retirees is falling, and will continue to fall for decades.

Benefits system designed on assumption that ~80% of people own their homes outright by retirement age. Inadequate benefits system shifts people into Tier 2 & 3 benefits that are more resource intensive for MSD to service. Data from 2018 Census (released in 2019) to shed further light on extent of problem.

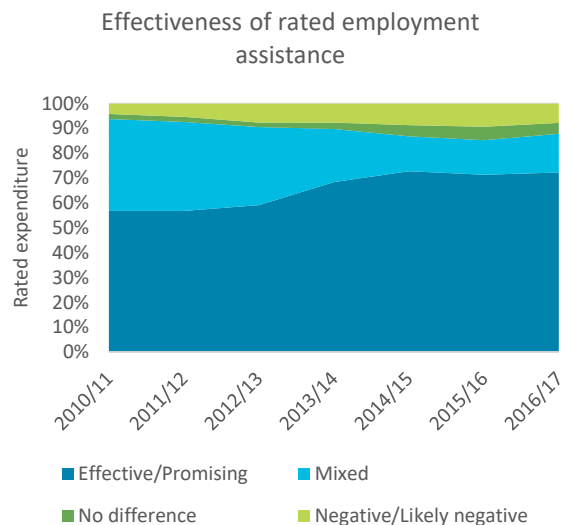
Component (\$m)	2019/20	2020/21	2021/22	2022/23	Total
Lifting Engagement	[8]				
Meeting Demand					

Preliminary conclusions

- Some rules/process changes currently underway, but flow-on impact to demand pressures is still unclear. Unquantified risk of impacts on BORE payments, but possibly improved outcomes. Possible legislative changes required.
- There is strong case for new FTEs to improve engagement, but the quantum of current shortages is less certain. If rules/process changes are successfully implemented, new FTE requirements are likely overstated.
 - Consider how IT/channel strategies will flow into decreased demand pressures and ongoing productivity gains.
 - Consider scaling the number of new FTEs required in 2019/20, consistent with likelihood and ability to fill positions.
- Growing need to assess the longer term implications for falling home ownership and increased indebtedness of retirees on benefits system and MSDs ability to respond.

II. Area of Focus: Investing in Employment Outcomes

Where has MSD come from?

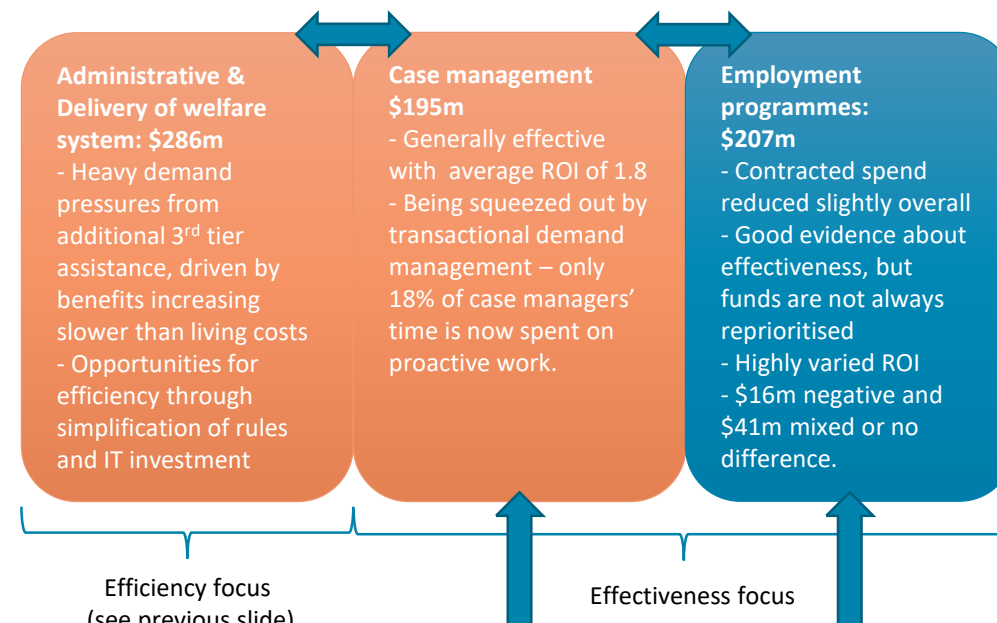


- **Introduction of the MCA for employment outcomes has created a focus on continuous improvement.** However, changes to overall effectiveness have been incremental (see figure above) and the mix of administrative, case management and contracted investment (right) has not been rebalanced in response to changing demand pressures.
- **Effectiveness has been heavily focused on BPS targets over the last decade.** A broader definition of effectiveness is now being introduced, with a focus on wellbeing. There is also a greater focus on the sustainability of employment outcomes, rather than simple off-benefit transitions.

Preliminary conclusions

- For employment assistance, there is **good evidence of effectiveness and processes to respond to new information** about effectiveness. MSD is one of the better-performing parts of Government in this area.
- There is a **pattern of lower effectiveness for some cohorts**, even where there is a large per-person spend. MSD explicitly addresses this in the *Employment and Social Outcomes Investment Strategy 2018–2021*. Other agencies may have more effective interventions for some cohorts, while others have no available alternative.
- **Spend is not optimised.** Where possible, baseline expenditure should be shifted toward higher-value activities (whether internal or external) before seeking additional funding, including for case management.
- **Measuring more outcomes with the new focus on wellbeing has a risk of greater measurement error**, resulting in difficulty determining whether programmes are effective (more “mixed”). Priorities will need to shift toward *highest value* rather than *valuable/not valuable*.

Where is MSD now?

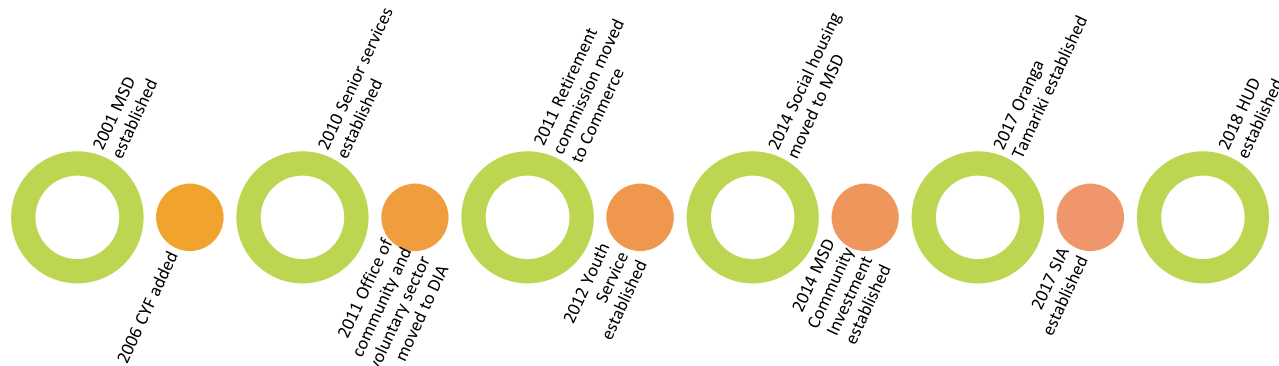


[8]

III. Area of Focus: Investing in Community Outcomes

Where has MSD come from?

- **Changes in MSD's role have increased complexity**, creating challenges to efficient contracting or gathering evidence of effectiveness.
- **A number of parts of MSD's role in delivering community outcomes have changed but are not completely resolved**, including the boundary with Oranga Tamariki, MSD's role in cross-social sector policy and commissioning relative to the SIA, and the role of different agencies in cross-sector delivery (e.g. Family and Sexual Violence services)

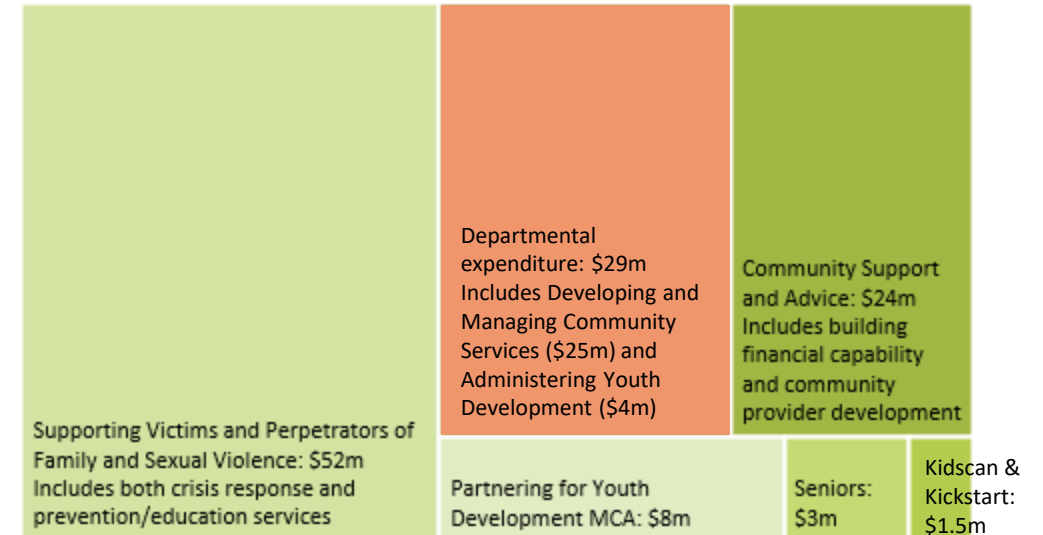


Preliminary conclusions

- **Community outcomes expenditure is inefficient and inconsistent.** Frontline service providers consistently report overlaps, low quality and a proliferation of contracts for community services, for some of which MSD is the owner. There is a need for a specific project to streamline contracts and reduce compliance costs. A broader cross-sector contracting review is needed, but this does not preclude MSD initiating its own review.
- While analytics and evidence in MSD's employment spend is leading Government, **more/better data needs to be collected in the community outcomes area.** This should begin by putting the right IT solutions in place for interoperability between MSD/OT and providers, to minimise risk and compliance costs, while addressing privacy concerns. This could improve MSD's capability to manage cross-sector initiatives and lead in this area.
- **Clarification is needed on the role of MSD as a centre of analytics, policy and contracting across the social sector.** Providing clear roles is a prerequisite to driving greater efficiency and resolving problems created by excessive change in this area.

Where is MSD now?

Community Support Services and Partnering for Youth Development MCAs: \$117m



What is MSD seeking through Budget 2019?

[8]

- **The Family and Sexual Violence Joint Venture provides opportunity for partnering to improve effectiveness across the social sector.** Benefits will likely take several years to materialise and will require examination of overlaps with other agencies and possible collective impact investments.

IV. Area of Focus: Remuneration

Where has MSD come from?

From 2004 to 2017, MSD self-funded increases in remuneration costs (i.e. it received no additional funding through the external Budget process, apart from for CYF, which has since left MSD). MSD estimates the increase in remuneration costs it has funded internally is approximately \$137m (based on the difference of average salaries between 2004/05 and 2017/18)

Where is MSD now?

The table below summarises the funding MSD received in Budgets 2017 and 2018 for remuneration cost pressures. In both Budgets, MSD did not receive funding for the cumulative increases in remuneration costs.

Budget	2017/18	2018/19	2019/20	2020/21	2021/22	4 year total	% of funding sought that was received
Budget 2017	\$8.45m	\$8.45m	\$8.45m	\$8.45m	\$8.45m	\$33.8m	50%
Budget 2018	-	\$12.49m	\$12.49m	\$12.49m	\$12.49m	\$49.96m	100%

MSD has just settled the collective agreement for National Office. **Bargaining has commenced or been initiated for other Ministry collective agreements in 2018 including Service Delivery.** This agreement makes up the largest portion of MSD's remuneration bid.

MSD is undertaking a series of role reviews in Service Delivery to better reflect and describe the work people do. The first review is completed, and enacted a 6% increase in remuneration for client facing roles. The focus is now on processing roles and then any remaining roles.

What is MSD seeking through Budget 2019?

[6]

Where is MSD going?

MSD's new strategic direction – Te Pae Tawhiti – means MSD's workforce will look different in the future, particularly to deliver the key shift of Mana Manaaki (a positive experience every time). MSD is in the early stages of implementing Te Pae Tawhiti, including determining its future business and operating models. Amongst other things, this will involve developing people and workforce strategies to outline the required skills and capabilities to support clients and their needs across various channels, as well as how MSD will support its staff. The Better Every Day programme is also an opportunity to make system improvements to help people carry out their roles.

[6]

Preliminary conclusions

- Remuneration is a non-discretionary cost pressure for MSD. The value of the collective agreement settled with the PSA will need to be funded regardless of MSD receiving additional external funding. However, there are implications if MSD has to self-fund some or all its remuneration cost pressures. Trade-offs will need to be made, which involve either reducing the number of staff or number and/or value of contracts.
- While MSD's workforce will look different in the future, this is expected to happen over the medium-long term. Based on MSD's current assumptions and the wider environment, we think the Ministry's remuneration costs look reasonable.

[6]

V. Area of Focus: Technology

Where is MSD now?

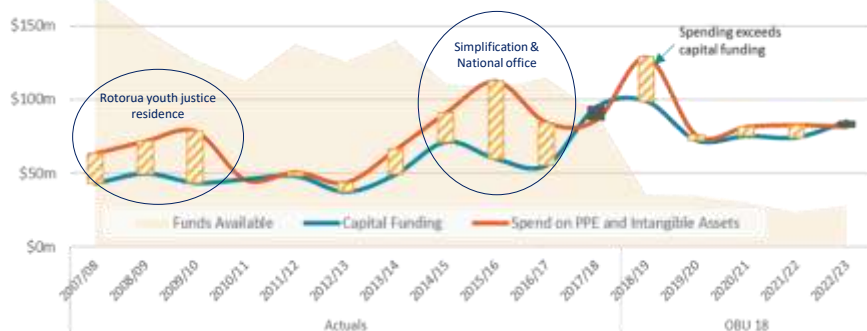
The current challenge for MSD is escaping the legacy system trap in IT.

Government IT investment decisions tend to be **reactive and prioritise based on risk**. The expense of maintaining existing systems means less proactive investment decisions are being made.

The status quo is being maintained as the **risk of service failure is greater than the risk of not having optimised systems aligned to organisational strategy**. The consequence of being stuck in the legacy system trap is that IT has become an inhibitor of organisational agility.

Capital sustainability is becoming an issue for MSD (note the related B19 bid). Since 2007/08, investment in assets has continually outpaced capital funding. Accumulated depreciation has been diverted to other priorities to build the asset base, (such as Simplification) while existing assets, particularly in IT, have been sweated. Changes in internal governance have allowed for better use of constrained capital.

MSD has funded significant projects from the balance sheet over the past decade but cash reserves are now low



Where is MSD going?

MSD needs to present a future state operating model that presents a shared vision for how the organisation will deliver on the strategic intent.

Te Pae Tawhiti provides an opportunity to revisit the approach to many existing processes (e.g. administration of the benefit system). The potential scale of transformation for the business is significant. We understand work will begin shortly to operationalise this strategy.

A number of parts of the organisation have developed strategies (including data/analytics, channel & technology). However, without a **common understanding of the direction of travel**, there is a risk these may be inconsistent.

What is MSD seeking through Budget 2019?

There is significant need for technology investment to deliver on the strategic intent.

There are significant pain points in the current IT environment that are being felt across the system. These directly affect the quality and efficiency of services delivered to clients. Complexity also makes implementation of policy changes difficult (which has implications for WEAG/Welfare Overhaul). Following Simplification, the criticality of digital channels for delivering key services has increased, leading to a commensurate increase in risk as these systems age.

The proposal in Budget 2019 is to replace a number of systems that have been **assessed to be at most risk**. The need for investments of this nature will likely persist as the level of risk becomes too high across other components of the systems. Approx. 60% of current applications are not fully supported. The main choice for Ministers in Budget 2019 is around **appetite for risk**.

The concern in investing ahead of the higher level operating model decisions is the potential for implicit lock-in through investment decisions that may constrain the option set for the target operating model. We are working with GCDO to address any concerns in this area ahead of Budget 2019 decisions.

Any and all investment must deliver value for clients. This requires both deliberate planning and the organisation having the requisite capability to deliver. MSD have acknowledged a number of areas where improvements are needed with respect to its IT capability. Progress made in response to these recommendations (**including delivery on current projects**) will help ensure further investment enables the organisation to deliver value for clients.

Bid		2019/20	2020/21	2021/22	2022/23	Total
Preventing failure of critical services to clients	Capital	[8]				
	Operating					

VI. Remaining Areas of Focus: Overheads, Property, & Policy

Property

MSD's property footprint is the second largest across government, with over 220,000 sq. metres. Rental costs per sq. metre are, however, one of the lowest in the public sector. There are three property types across the MSD portfolio, each with different drivers. Total rent expenditure is \$72.5 million p.a.

1. **National Office** [approx. 25% of rent]
2. **Contact centres/regional offices (non-frontline)** [approx. 20% of rent]
3. **Frontline sites** [approx. 55% of rent]

MSD has a significant regional presence, with 126 frontline sites. A comprehensive top-down assessment of the role of the frontline sites was conducted as part of Simplification, however **the opportunities identified for consolidation were not adopted by Ministers.** [3]

[3]

Assessing the requirements for a frontline site is considered within the broader strategic context, rather than just as a property decision. The Government also relies on the network in emergencies. Maintaining the status quo across the regional footprint has meant that the enduring need for sites in their current state is validated without explicit consideration of the future role of the frontline.

The cost of maintaining the status quo is increasing, and risks of lock-in are particularly high when procuring new buildings.

- **Costs have been managed in part through staying in the same site (with less focus on site suitability).**
- As leases expire, there has been greater scrutiny of site suitability. In a number of locations, **lack of viable options has necessitated a new build which means costs become decoupled from typically low rent levels in the area.** For example, rent for the New Plymouth site increased by 50% following relocation.
- As part of the broader security and service culture work streams, MSD has had agreement for major investment in frontline sites to ensure adequate safety and security configurations (Future State Physical Environment). We understand that MSD may seek additional funding through B20.

What is MSD seeking through Budget 2019?

[8]

[8]

Overheads

MSD's overheads look reasonable given the size and scale of the organisation (BASS data). MSD currently provides shared services to Oranga Tamariki to the value of \$75m per annum (as at OBU 2018). **The establishment of Oranga Tamariki and the Ministry of Housing and Urban Development has created some diseconomies of scale for MSD** (currently \$7.8m per annum), as some of MSD's costs have not reduced proportionately in the short term, due to the fixed nature of the costs.

MSD and Oranga Tamariki Chief Executives agreed in September 2018 to separate the provision of some shared services between the two agencies, with other services continued to be provided until there is a natural investment point that requires a decision. **While the net effect of the split in dollar terms is currently being worked through, the separation will involve some changes that aren't fiscally neutral.**

There is a choice about whether some shared service functions that MSD provided, such as, social services accreditation, should be delivered at an all-of-government level in the medium-long term.

As MSD implements Te Pae Tawhiti and changes its service, business and operating models, there are likely to be some efficiency gains. However, **some overhead costs will be fixed, and therefore, savings may take some time to be realised.**

Policy

Since 2015/16, policy advice resources have shifted out of MSD to: SIA (social sector strategy), Oranga Tamariki; and MHUD. **These shifts reduced MSD's policy function by 64 FTEs (47%), while also requiring MSD to provide ongoing policy advice in these areas.**

MSD has managed its workload pressures by trading off work, including some high priority work, and deprioritising strategic analysis, pro-active work and future capability building. It has also been constrained in its ability to input to other agencies' work, and wider social and economic development work in support of the wellbeing agenda.

Ministerial demand is a key demand driver for MSD's policy function. **MSD could work with its Ministers to gain a shared understanding of its role, both in terms of core welfare system policy versus wider social/community development policy, and also its role in providing cross social sector policy advice.**

The anticipated Policy Advice appropriation for 2019/20 is \$12.6m. Of this funding, \$8.5m is for 73FTEs in the MSD Policy branch, excluding overheads. MSD's budget bids suggest they are 14 FTEs [8] – short of the minimum resources needed to deliver its current work programme. A further 11 FTEs [8] – would allow MSD to respond to its expected future work programme.

Future Direction

Where is MSD going?

MSD has a new strategic direction, Te Pae Tawhiti, which signals MSD's intentions for delivering its purpose and achieving its outcomes for New Zealanders.

MSD purpose	We help New Zealanders to be safe, strong and independent		
MSD outcomes	New Zealanders get the support they require	New Zealanders are resilient and live in inclusive and supportive communities	New Zealanders participate in society and reach their potential

As part of Te Pae Tawhiti, MSD has agreed three key shifts it needs to make:



Mana manaaki
A positive experience every time.



Kotahitanga
Partnering for greater impact.



Kia takatū tātou
Supporting long-term social and economic development.

MSD has signalled that a transformation package will be submitted in Budget 2020 to help deliver Te Pae Tawhiti, which will be informed by a programme level business case.

In the lead up to Budget 2020, there is a lot of work for MSD to undertake. This includes agreeing a medium-long term target operating model with a detailed understanding of Te Pae Tawhiti's impact on people, property, systems, and processes. It will be important to ensure these areas are based around a common direction of travel but with options and choices for the Government.



Q: what's the Government's appetite for MSD developing a business case to seek investment in B20 to deliver Te Pae Tawhiti?

MSD is also facing uncertainty across several areas, which could have strategic, operational or fiscal impacts for the organisation:

- the overhaul of the welfare system, including recommendations from the Welfare Expert Advisory Group
- outcomes from the inquiries into state abuse and mental health
- the Joint Venture on Family and Sexual Violence
- clarifying MSD's role and mandate in the social sector (and connections with the economic sector) →

Q: what role does the Government see MSD playing across the social sector?

While there is still work to be done and some uncertainties, MSD is focused on continuous improvement. For example, through the Better Every Day programme, which is using systems thinking to understand and improve processes at the frontline.

