

Efficiency and Performance in the New Zealand State Sector: Reflections of Senior State Sector Leaders

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INTRODUCTION AND PROJECT BRIEF

The New Zealand Productivity Commission contracted for semi-structured interviews with both current senior members of the state sector and former members (“wise heads”) with long and in-depth experience of New Zealand’s state sector. Appendix 1 provides a list of interviewees.

The transcripts from these interviews were confidential between the contractor and interviewees.

The interviews were conversations around five general topic areas:

- how state sector leaders and employees think about and conceptualise efficiency;
- the relative importance of efficiency as a goal of state sector agencies;
- the role of performance management in the state sector;
- the challenges of measuring efficiency and the challenges of using efficiency measures in decision-making; and
- how the efficiency of the state sector can be lifted.

The inquiry has been fortunate to secure the input of many exceptional current and past state sector employees. Twenty individuals were interviewed. Most interviews were an hour in length; some were much longer. The indicative interview questions are included in Appendix 2.

Part I of this report presents the views of interviewees on the above five topic areas. Part II provides a summary of the key themes, supplemented by reflections from the interviewer.

PART I: SENIOR LEADER REFLECTIONS ON IMPROVING STATE SECTOR EFFICIENCY

Economic efficiency

A definition

Economic efficiency can be defined as providing goods and services of most value to the community (allocative efficiency), at least cost (productive efficiency), over time (dynamic efficiency). Trade-offs between these three types of efficiency are often encountered when making decisions on resource use, and are usually resolved by reference to the expected impact on total welfare.

Is efficiency well understood?

Interviewees demonstrated a strong understanding of the three types of economic efficiency, although not all conceptualised the concepts using the formal terms. A common misunderstanding was to assume that efficiency was solely about productive efficiency. In this context, some pointed out that productive efficiency alone was too limited to drive government decision making. What was also important, most noted, was making sure government was doing the “right things” to make a positive difference for the community. Similarly, most interviewees commented on the importance of, for example, government investing in finding better ways to do things.

Some of the interviewees with a strong understanding of efficiency came from “social agencies”. This was contrary to the views of an interviewee who thought efficiency may be less well understood in these agencies. A number of interviewees from social agencies had experience working within central agencies (such as The Treasury) and others had come from the private sector.

What did come through strongly in interviews was that social sector leaders and their staff focus on making a difference for their communities. In this context, efficiency often carried with it negative connotations of cost cutting and compromised service delivery. This is commented on further below.

The language of economic efficiency: a liability?

Most interviewees praised the New Zealand state sector’s strong ethic or motivation of wanting to “do the right things” and “make a positive difference” to the communities they served. While no interviewee claimed this motivation was universal, a number of interviewees felt it was a common driver of state employees and, compared to other countries, New Zealand was fortunate in this regard.

However, officials often view the language of efficiency as running counter to motivation of wanting to do the right thing. For example, officials often view efficiency drives as a direct threat to jobs – conjuring up the “sound of chainsaws” for many staff, and reduced services to clients. The result could be staff becoming dispirited – causing them to work against, rather than with, changes to improve performance.

“Terms like *productivity* and *efficiency* will not win the hearts and minds of staff working within government organisations.” – Interviewee.

Some interviewees suggested discussions promoting reform are best couched in the language of the social outcomes sought by government, rather than in the language of economic efficiency. One interviewee noted the appropriate language to support reform was that which best drives the achievement of that reform. This would be situation specific.

Another suggested the Productivity Commission also needed to change its name to something less limiting and more "positively relatable".

How well is the New Zealand state sector performing?

Overall, interviewees felt the performance of the New Zealand state sector was improving. A stronger client-centric focus, better use and uptake of technology, and a growing focus on joined-up services were mentioned. This view, however, was not universal. Some interviewees pointed to a growing list of accountability and performance requirements that added costs for little benefit, and eroded Chief Executive accountability. Others pointed to growing political interference (refer to section below on "Political objectives"). One interviewee cited a long "legacy of performance failure" in their sector, which had yet to be corrected.

Another interviewee felt the state sector was getting better at focusing on programmes that achieve outcomes, but productive efficiency gains had been harder to achieve. In contrast, another suggested there was too great a focus on costs within the state sector, and not enough on results.

Interviewees generally viewed New Zealand as a leader rather than a laggard with respect to the efficiency of our state sector compared with other countries, with considerable interest from overseas in how our state sector operates.

Some suggested there was little to separate the state and private sectors when it came to productive efficiency, although the majority view was private sector productive efficiency was superior. Interviewees with experience of both the state and private sector believed the private sector was more efficient. "It is so much harder to get anything done in the state sector," said one.

Many noted performance across the state sector varied a great deal. One interviewee explained productive efficiency was more relevant for operational agencies where the "what to produce?" question was more settled. Without exception, all interviewees felt more could be done to improve state sector performance.

What objectives compete with economic efficiency?

Political objectives

Interviewees observed that votes and perceptions of public attitudes drive political objectives. As one mentioned, "politicians are very fast followers of public attitudes".

Interviewees gave a number of examples of political objectives working against efficiency objectives. However, interviewees did not see this as simply a binary battle between vote-maximising politicians and welfare-maximising officials.

Government Ministers genuinely want what is best for New Zealand, interviewees observed. More specifically, interviewees noted senior politicians do not want to waste resources, they want their initiatives to be successful, and they want to see improvement over time. This desire to improve provides a great deal of common ground with senior state sector officials - there was often considerable scope to find ways to achieve both political and public interest objectives:

“Sometimes officials need to find options that achieve Ministers’ political objectives as well as public interest outcomes, or at least manage any adverse impact that political objectives may have on public interest outcomes.” – Interviewee

One interviewee remarked it is important not to assume that a political policy option will be inferior to one developed by state sector officials. Democracy entails a form of collective preference revelation that should carry considerable weight, and could be superior to a technocratic option developed by officials. Also, politicians and officials should be thought of as reinforcing components of the same system, rather than as competing systems. Each component, interviewees said, is necessary for the proper performance of the overall system, and at occasional conflict is a necessary and even useful part of that system.

Several interviewees spoke of their responsibility to deliver free and frank advice to Ministers on Ministerial choices. They mentioned the importance of ensuring Ministers based decisions on full information, and that they properly understand the trade-offs associated with different options.

One interviewee described Members of Parliament (as distinct from Cabinet) as key to significantly improving state sector performance. While Select Committees performed quite well, politicians needed to focus more on incentivising higher performance in state agencies.

Yet some interviewees felt political considerations are taking on greater weight, with political advisors having a growing influence. One interviewee noted that Ministers are becoming less open to free and frank advice, and less willing to hear about risks – if they know about risks, they have to manage them.

Another, who had come from the private sector, complained that politics had too great an impact on performance, and was driving risk-averse behaviour in the state sector.

One interviewee, who had served many governments, said the state sector always needed to “operate above the politics”.

Self interest

Some interviewees commented on how self-interest drivers could impact on the decision making of state sector leaders to the detriment of efficiency. Examples given included status, promotion, and the desire to “avoid unpleasantness”.

Other interviewees commented on the political economy problem of state agencies seeking growth over efficiency, and gaming of the system to achieve agency growth. One suggested this would not be such a problem if central government agencies and Ministers clearly and consistently applied budget rules.

Fairness

Interviewees observed that efficiency goals may conflict with notions of “fairness”. One interviewee explained opposition to a new policy had arisen because the policy would only benefit one group of clients. Limited resourcing meant it was not possible to apply the change to all client groups at once. Opposition came from a part of the system responsible for implementing the policy and this was likely to hinder the policy’s effectiveness.

The role of performance management systems in the state sector¹

The purpose of a performance management system is to promote better performance. Better performance means getting the greatest value from the limited resources available to the state sector.

A performance management system incentivises better performance by making entities accountable (through consequences) for their past performance; and lifts capability by helping identify barriers and opportunities to better performance. To achieve these purposes, the following information may be collected:

- agency/programme performance over time;
- agency/programme performance compared with other similar agencies/programmes; and
- assessment of programmes ex post to see if they achieved what was expected ex ante and, if not, generating information to help understand why not.

Often, a *principal* collects information on the performance of an *agent*. The agent is responsible to the principal for providing specified goods or services, either to the principal or to a third party, in exchange for funding. A performance management system is a tool the principal can use to manage the risk the agent will not perform to the level specified.

¹This section is about intra-agency performance management systems only. Inter-agency performance management is covered below under “Performance and Accountability Requirements from the centre”.

Many interviewees commented that better performance requires strong incentives to perform, and the state sector system lacks such incentives. In this context, some commented that a properly calibrated performance management system would help improve performance. Some noted it is a department's Chief Executive who is responsible for the performance management system and how it is used.

What do good performance management systems look like?

Interviewees offered the following features of a good performance management system:

- good access to high quality information;
- effective and ongoing monitoring to ensure the system continues to perform appropriately;
- principals intervene in a timely and appropriate manner to encourage better agent performance (giving due regard to the importance of maintaining good relationships);
- high quality underlying systems and processes (for example, quality control);
- people with the relevant skills and experience;
- adequately resourced;
- cost-effective to access; and
- integrated, that is, good connections between research, policy, service delivery and clients.

A number of interviewees favoured performance systems where principals contracted with agents for *outcomes*. Agents have responsibility for finding the best ways to achieve those outcomes. Interviewees noted this approach was easier to achieve in some areas compared to others, for example, where outcomes are easy to measure and are realised in the short term, or where accurate and measureable proxies can substitute for outcome measures.

Building on this theme, an interviewee described a performance system that would encourage innovation closer to the “front line”, where local solutions would be developed but learnings shared with others as appropriate, and capabilities built. This system would align the interests of head office functions and front line functions. The system would use benchmarking between entities to help identify issues needing attention.

With respect to performance monitoring of a given task, one interviewee said success depends on:

“... having the right people, going in the right direction to an agreed plan. Progress must be monitored and intervention taken if needed, otherwise people should be left to do what they need to do.” – Interviewee

Building a performance management system

One interviewee described the approach they had taken to build a good performance management system². They had constructed the system around an “information pyramid” designed to meet the information needs of management, governance and stakeholders (for example, the public). The interviewee formed a dedicated strategy and performance unit to develop the system. Performance metrics were agreed with stakeholder input and based on knowledge of historical and offshore experience. The metrics had to be realistic and focussed on the things that mattered and, where practicable, outcomes based. The interviewee deliberately built the system to be collaborative rather than combative between principals and agents. The Chief Executive drove the change, a change that had the purpose of working with and reinforcing the organisation’s client-centric and “making a difference” culture.

To overcome political and organisational resistance to performance measures, another interviewee identified the importance of influential sponsors or champions. Sponsors work with Ministers and state sector staff to demonstrate how performance measures are not a threat, and can help the organisation achieve better performance. The aim is to add value to clients by embedding the use of performance measures into an organisation's culture. Another interviewee noted while leaders are key to achieving a performance culture, clients who are capable and seeking improvements can aid leaders.

How well are New Zealand state agencies doing?

The broad consensus from interviewees was that that state agencies:

- are getting better at collecting and using performance information; but
- vary considerably in the quality of their performance management systems; and
- for the most part, there is a long way to go to get performance management systems where they need to be.

While all state agencies collect performance information, not all use that information well. One interviewee suggested small agencies in particular may be struggling a little more. Interviewees felt performance information systems naturally get better as they mature.

For a number of comparable activities (call centres were identified by some interviewees), the metrics used to assess performance and inform decisions across the state and private sectors are similar. Outside these areas, for example, policy development, performance assessment is more difficult.

² Another interviewee independently identified this performance system to be of high quality.

Interviewees observed agencies often treat performance reporting as a compliance exercise, rather than a strategic tool for encouraging accountability and improving performance.

“Performance measures are not always designed with a view to their likely utility, too often being produced to meet what are viewed as compliance exercises.” – Interviewee

The reasons why agencies may not be collecting and using performance information well are discussed below.

Measuring and using efficiency data: Challenges

Interviewees raised several challenges to the measurement and use of efficiency measures. The key challenges were:

- collecting good data;
- getting the balance right between data value and cost;
- the risk that poor quality measures would reduce performance;
- the need to balance holding agents to account and protecting relationships;
- developing agency capability and capacity to measure and use efficiency data;
- getting Ministerial support; and
- supporting the social investment approach.

Collecting the right data

One interviewee commented:

“Performance information needs to be timely, relevant, accurate, and link activities to outcomes.” – Interviewee

Interviewees often mentioned, collectively, government holds a tremendous amount of data. They described some information as relatively easy to collect, such as:

- transactional data, for example, call centre volumes;
- operational data, for example, time before Emergency Department patients are seen; and
- “soft” information, such as from experienced and trusted front line staff.

Interviewees said the following valuable information was difficult for agencies to collect:

- the evidential support for existing interventions;
- the evidential support for proposed interventions;
- the link between activities and outcomes;

- the comparisons of value of competing projects across different agencies (for example, with respect to new Budget bids); and
- robust proxies for real world outcomes that are appropriate, reliable and complete.

One interviewee said, in their organisation, operational transactions generate the data they need automatically. There is little need for new data to supplement what the system already collects. It is, however, important people know what data is collected.

On the other hand, an interviewee from a data rich agency identified challenges of getting some of the information they needed. As the *principal*, the interviewee sometimes found that:

“Collecting information could be difficult due to privacy concerns and suspicion with respect to how the information would be used, which means there’s also onus on departments to demonstrate the benefit and be transparent about what we’re doing with the information.” – Interviewee

A number of interviewees pointed out that good decisions relied on more than just numerical data. For example, they mentioned the usefulness of qualitative information, in particular from experienced and trusted staff operating close to clients.

“This could provide useful context on whether a local initiative might be scalable, whether there is a risk of unintended consequences, and for understanding the nature of what is being dealt with.” – Interviewee

One interviewee suggested if staff want to get the right information, they have to keep asking the question, “how do you know you are performing well?”

Striking the right balance between data value and data cost

Not all the data collected by agencies is useful for performance or accountability purposes. A significant number of interviewees commented agencies collect too much data. One interviewee mentioned, overall, there are too many performance measures, they are poor quality, and do not link well to performance.

Another said governance and managerial demand should drive the collection of data, and agencies should only collect data if they need it and intend to use it. Many interviewees complained that much of the data collected is never used. They suggested tight controls on what was collected, linked to its expected value.

Commenting on complaints about the large amount of unnecessary data collected in one sector, an interviewee gave an example of an exercise that brought people together to rationalise the data being sought. The exercise resulted in *more* data being collected.

The risk that poor-quality measures will reduce performance

A number of interviewees raised the consequences of collecting and disseminating poor quality information. One noted not all efficiency information would add value and improve performance. Poor quality information would do the opposite. One example that came up a number of times was the unsustainability of organisations operating at 100% capacity. Capacity measures needed to take into account factors such as training, annual and sick leave, and the use of temporary staff to manage peak loads.

In a similar vein, one interviewee noted that with better measures demand for better performance is increasing, but sometimes that is unrealistic.

“There is a risk that best practice is becoming the ‘new normal’, yet this level of performance may not be sustainable or able to be replicated in other settings.” – Interviewee

One interviewee commented that using information for benchmarking in their experience had not been successful, as there had been too great a focus on inputs. Another noted the difficulty of comparing inter-organisational performance between sectors - intertemporal information on the same organisation was often more useful. Another said cross-entity or staff comparisons needed to be done with care - for example, such comparisons can lead to top performers reducing their effort if they realise others are putting in less effort than themselves.

Interviewees raised the potential for bureaucracy to devalue performance measures. There is no ‘one size fits all’ to performance measures and using performance measures properly takes real understanding and good judgement. Variance reports, for example, should be the start of a conversation, not a trip wire for punitive action.

Some interviewees mentioned there was a heavy focus on using performance information to drive cost cutting at the expense of focusing on outcomes. Others, however, noted efficiency (productive) information was scarce, and data on effectiveness (achieving outcomes) was more commonly used. The latter group suggested this flowed naturally from a strong culture in many state sector organisations of wanting to make a difference.

Interviewees also identified the following poor practices.

- unachievable performance targets;
- people with the wrong skills analysing and using performance data;
- bias towards things that are easy to measure rather than what is important;
- agents being held to account for things they have no control over.

With respect to the last point, one interviewee commented that centralised decision-making – in particular, wage settlements but also other directives from the centre – had an impact on their ability to control and be responsible for their agency’s performance.

One interviewee mentioned that even if the information generated was of poor quality, it could still be worth collecting.

“This is because going through the process of producing that information helps officials think about and understand how best to improve outcomes - their intervention logic.” - Interviewee

It could also provide a base for improving the quality of information in the future. Similarly, another interviewee commented that:

“Reporting on variance against a target, even if that target is imperfect, can lead to valuable conversations which in turn feed into strategy and more effective interventions.” – Interviewee

Getting the balance right: Holding agents to account while protecting relationships

Many interviewees commented on the importance of good relationships between principals who use performance information and agents whose performance is being managed. “Without good relationships, the performance management system will not work”, said one.

In particular, interviewees considered developing collaborative rather than adversarial relationships was critical. One interviewee said too many organisations struggled to have mature conversations. The fault was often on both the agent’s and the principal’s side.

Expanding on the nature of adversarial relationships, principals interviewed perceived agents too often rejected the results of performance information, defending the status quo by arguing the uniqueness of their circumstances. In contrast, an agent’s perspective pointed to principals being too quick to take a punitive approach, and failing to understand the information provided.

Some interviewees felt some performance measures clashed with the common motivation of agencies to do the best they could for their clients, in particular where the “wrong things” are measured. “You get what you measure,” was a warning from one interviewee. Measuring the wrong things could lead to unintended or perverse outcomes for clients and others.

A number of interviewees noted problems arise when principals and agents do not agree on metrics and targets. In one case, neither the agents nor the principal were using a sector’s performance measures despite the cost of producing them. To the extent performance

measures are used, they tended to encourage a combative approach from both sides. One interviewee said the solution was to run an inclusive process to identify:

- the information most needed to support good decision-making and accountability;
- the key trade-offs involving each measure; and
- what the right performance management parameters should be.

Having the capability and capacity to measure and use efficiency data

One interviewee explained it is important to have people who know what information the organisation holds, are able to recognise the value of data, and can “mine” it efficiently. It is then important for managers to be able to understand that information and then use it to drive better performance.

Overall, interviewees felt organisational capability and capacity is not where it needs to be.

“Senior managers need to be able to understand what drives the costs and benefits across the different services, and how to make good choices using that information. Some senior managers lack the ability to properly understand and use performance information.” – Interviewee

Two interviewees spoke of a general shift of resources from “back office” to “front line” staffing, and how this is negatively impacting agency ability to put good systems in place to collect and assess data. In contrast, other interviewees commented favourably on organisations that have made a significant investment in performance management.

One interviewee commented on the importance of accessing the views of internal and external auditors. Auditors often have an in-depth understanding of systems, processes and organisational risk. Another interviewee observed that organisations are often “scared” of auditors and seek to move them on as quickly as possible. Organisations fail to properly access the value add perspectives auditors have, for example, with respect to ensuring systems are in place and appropriate to the organisation.

A number of interviewees felt there are opportunities to raise capability by providing and offering examples of good practice within organisations. Some commented this is a goal they themselves have set for their organisations (to provide a good example).

Ministerial support for efficiency measures

Generally, interviewees felt Ministers are increasingly demanding performance information, and information of the right type.

One interviewee commented that Ministers are setting “realistic to tough” targets for the important outcomes they are seeking. Further, Ministers are explaining the targets and variance from targets to the public, who are engaging with the policies and results. This interviewee did not think there is a material risk that these performance measures will result in unintended or perverse results.

However, other interviewees spoke of political objectives dominating efficiency objectives and undermining the usefulness of performance measures. One suggested:

“While good information is increasingly put into the public domain, much still isn’t. A barrier could be the lack of comfort the Minister has in making that information available.” - Interviewee

Supporting the social investment approach

The social investment approach was explained by one interviewee to involve working back from significant social harm to identify its causes and, from this, finding the most appropriate solutions (in terms of both effectiveness and cost) for reducing this harm. Another explained that the current challenge was to join advice and initiatives across agencies to deal with new and more complex issues than government has had to deal with previously. The old state sector frameworks providing for Chief Executive accountability, departmental budgets and annual appropriations were appropriate for their time; but today these arrangements struggle to accommodate bigger and more complex issues, such as child poverty and environmental degradation. Increasingly, as interviewees explained, government is facing issues which have strong vertical (long time horizons) and horizontal (many organisations contributing to the same outcomes) dimensions. The social investment approach accommodates these dimensions.

Many interviewees spoke favourably of more joined-up delivery of government services when tackling significant social issues. Many also commented on the importance of lining up governance, accountability and funding. Interviewees noted it was important that the performance management system also lines up with the social investment approach. Particular challenges with supporting the social investment approach include:

- many things contribute to outcomes, things that government can control and things it cannot;
- separating causation from correlation can be particularly difficult;
- attributing relative performance shares to the different actors involved is problematic; and
- results may not be seen for many years and useful proxies may not be available.

Despite these difficulties, there was widespread support for continuing and strengthening efforts. As an interviewee put it, "it's hard to do, but everyone wants better accountability".

Opportunities and barriers to better state sector performance

Interviewees were asked to comment on opportunities and barriers to better state sector performance. The comments fell broadly within the topics of leadership, performance and accountability requirements, the Budget process, culture, centralising functions, the social investment approach, cost recovery and contracting, governance, innovation and inefficient standards.

Senior leaders: their role in promoting better state sector performance

Many interviewees commented that the state sector *system* does not provide strong incentives on agencies to be more efficient. Implicitly, much then depends on the capability and motivation of senior leaders in each agency.³

Good leadership is needed to ensure organisations are focused on the right things. An interviewee gave the example of investing in three FTEs to focus on long-term issues, thought leadership, and setting the groundwork for good long-term decision-making. Without this intervention, the organisation would have remained reactionary and focused on short-term outcomes.

Many interviewees felt the quality of governance relationships depended heavily on the quality of senior leaders – Ministers, board members and Chief Executives.

An interviewee commented on the importance of Chief Executives working openly and honestly with Ministers.

“These behaviours set the tone for the rest of the organisation, teaching staff what behaviours are important and how things are done, and therefore it has a large impact on the organisation’s performance.” - Interviewee

Similarly, another interviewee noted senior leaders need to be of a high calibre to effectively navigate “the system” and political risks.

One interviewee with long time experience of the state sector suggested that the quality of Chief Executives had fallen. Another interviewee commented that:

“The original State Sector Act, which had been effective at providing strong and focussed accountability, has increasingly been diluted by additional requirements that have reduced its effectiveness. This is not to say that horizontal cooperation is unimportant, clearly it is.” – Interviewee

³ This point was implicit in the comments of many interviewees.

The interviewee went on to say that “if Chief Executives are not performing, they should be removed and this does not happen enough today”. Another interviewee spoke of the importance of not “recycling failed Chief Executives” through the state sector.

On the whole, interviewees felt senior leaders focus on achieving the right things and are highly motivated and capable. However, one interviewee commented that although the quality of management at the top level seemed to have improved, there are still senior leaders in the state sector who do not have the right skills and personal attributes. This problem is mitigated somewhat when leaders employ complementary senior managers, but this does not always happen.

Another interviewee suggested that the basis for selecting Chief Executives has changed.

“Chief Executives used to be promoted on the basis of their technical competency. Many failed. Today the focus is more on people skills, character, ability to deliver a “stewardship” role, and ability to manage people.” – Interviewee

One interviewee noted New Zealand state sector leaders tended to have greater and broader responsibilities from a younger age than most of their counterparts overseas. Gaining experience from a younger age was an advantage.

Interviewees identified a range of characteristics they considered state sector leaders should have, including:

- willingness to be a thought leader, but not so much that Ministers and staff are left behind;
- the ability to motivate staff – optimism is important;
- being capable of realistic self-reflection;
- the ability to manage for results;
- people skills: “relationships are what it is all about”;
- character: able to speak truth to power;
- absolute focus on their people: hiring, developing, motivating;
- stewardship: playing “the long game”;
- being a clear thinker;
- being forward looking;
- an understanding of how the system works and understanding the strengths and the weaknesses of different models that may be applied to managing the state sector; and
- the ability to monitor developments and think about the wider implications of those developments for the state sector.

Some interviewees commented on personality characteristics that could work against performance, including bullying and egotistical behaviour.

With respect to “entry” of good and “exit” of poor Chief Executives, a number of interviewees commented that, ex ante, it was difficult to know how a Chief Executive would perform, but it was easy to judge their performance ex post.

One interviewee considered senior leaders in New Zealand work well together. For example, when leaders are doing the right thing but “trip”, their peers support them. Similarly, peers recognised leaders’ investment in best practice, stewardship and innovation - such investment can have widespread and long-term benefits.

Another interviewee commented that reputations matter greatly and this motivates the behaviour of senior leaders.

Performance and accountability requirements from the centre

The key purpose of performance and accountability requirements imposed by central agencies (for example, The Treasury, the State Services Commission) and the Office of the Auditor General⁴ is to hold state agencies accountable for their use of state funds and powers, and encourage good performance.

Overall, interviewees felt accountability and performance requirements administered by central agencies are excessive. Although the requirements are designed with the intention of driving better performance, the requirements too often imposed excessive compliance costs for little benefit. One interviewee described an organisation they had previously worked in as “fundamentally good” and trying to do the right thing for its clients. The accountability and performance requirements, however, did not help the organisation do better. In fact, they consumed resources that the organisation could have applied to higher-value tasks.

The interviewee also explained that:

“Accountability and performance requirements are generating ‘hard’ performance measures. But there are no consequences for good or bad performance against those measures.” - Interviewee

Instead, if action is taken, it is more likely to be in response to “soft” measures. But these measures do not generate strong incentives on Chief Executives and organisations to perform. The interviewee went on to say:

“The solution is to find ways to strengthen the incentives on Chief Executives to improve the performance of their organisations, but this is not easily done. It

⁴ The Office of the Auditor General is a Parliamentary Office, so is not a central agency.

requires moving their incentives beyond budget risk, legal and political risk and the risk that new initiatives will fail.” - Interviewee

A minority of interviewees felt performance and accountability requirements from the centre are about right. One interviewee singled out four-year plans as useful, but said other requirements were less so. They commented that it would be beneficial if there was greater flexibility on when and how requirements are applied. Several interviewees said the State Services Commission’s Performance Improvement Framework (designed as a performance improvement rather than an accountability tool) and Chief Executive reviews were useful, with one noting the State Services Commission was getting better at driving internal systems improvements in agencies.

Some interviewees felt Crown agencies would benefit from tighter controls from the centre, although others felt the answer was instead to replace poorly performing Chief Executives and boards. Two interviewees commented that if Crown agencies are to be tightly controlled from the centre, it may be better to roll these agencies back into departments.

One interviewee noted relationships with central agencies are very person-dependent, and central agencies are not always clear about what information they want. This wastes a lot of resources, often generating information that no-one reads or uses. Another interviewee said the central agencies themselves are not well joined-up and coordinated, and believed more should be done to remedy this.

A small number of interviewees mentioned the importance of trust. One used the adage “trust is hard to gain but easily lost”. A central agency had approached the interviewee's organisation, saying it wanted to work with the organisation to constructively identify and manage problems. When an issue arose, the central agency took punitive action. The interviewee said they would not make the mistake of being so open with the central agency again. Other interviewees commented that central agencies can be guilty of encouraging an adversarial rather than collaborative approach with some organisations.

Another interviewee said the reforms of the late 1980s had made it easier for Chief Executives to manage their resources and to be held accountable. Any moves to centralise whose accountabilities and functions needs to be done with some care to ensure the purpose of the original reforms are not put at risk.

Two interviewees commented on the potential for major or “bedrock” reforms to atrophy. One commented:

“‘Bedrock’ reforms such as the State Sector Act and the Public Finance Act tend to atrophy over time, through incremental and sometimes ad hoc reforms eroding their original purpose and clarity.” – Interviewee

At least two other interviewees touched on this issue. They suggested a “re-boot” is necessary from time-to-time to ensure the underlying framework of reforms remained fit for purpose.

Budget processes: is it promoting better performance?

For the most part, government budgets involve:

- appropriating money each year based on and indexed to the funding provided for the previous year; minus
- any appropriation for activities that are expected to cease that year; plus
- any new appropriation for approved new policies or where funding is demand driven (for example, Ministry of Social Development benefit payments).

State agencies are not permitted to overspend without specific approval.

Some interviewees felt government budget disciplines provide a strong incentive for innovation, in particular with respect to productive efficiency. One described how, when confronted with *severe* budget constraints, an organisation may have to think outside the square to prevent organisational failure or severe hardship for clients.

One interviewee suggested efficiency only becomes a top priority when entities are in trouble - for example, when they are at risk of overspending. Another said the tighter budget constraints accompanying the global financial crisis had encouraged efficiencies.

However, most interviewees criticised the Budget process. Interviewees with private sector experience were particularly critical. One found the “myopic” focus on the Budget process a barrier to better performance. For example, the Chief Executive’s remuneration:

“... is too much about organisational size - getting a bigger budget. Also, there is no “Government Inc. culture” and inter-agency competition for funds can detract from a focus on shared outcomes.” – Interviewee

In contrast, in the private sector there is a strong culture of money being available for high value services, but that money often comes from activities deemed to be contributing less value. One interviewee with a private sector background went so far to suggest there is plenty of money for government to achieve its objectives. It just needs to use the existing money in the right way.

Another interviewee described prioritising goals as a particularly difficult exercise in the state sector compared to the private sector. Others spoke of the importance of senior state leaders being seen to be busy and contributing things, even if those things were not the best use of resources.

Another interviewee with considerable private sector experience characterised the difference between state and private sector agencies: In the private sector, the operations section earns the money and the finance section keeps a check on spending. In the state sector, agencies deliver various outcomes and The Treasury tries to keep an eye on the spending. This setup, the interviewee said, did not work well.

The interviewee suggested an option may be to allow state sector agencies to keep a proportion of their savings, or be positioned higher up the “pecking order” for new expenditure when savings are achieved.

One interviewee spoke of the need for good “systems leadership”. Too often, they said, agencies focused on new funding for “shiny new things”. When added incrementally to existing programmes, this can result in an ad hoc and poorly performing arrangement of services.

Some interviewees noted similar incentives apply to Ministers, that is, to simply get more money to do more things. One interviewee evidenced an occasion where they offered up savings to their Minister, only to have that offer declined. “Waste is not always top of mind,” they said.

Getting the right culture

Many interviewees stressed the importance of culture for good performance. Being motivated to “make a positive difference” was a common theme.

“The state sector needs to be client and outcome focused, and driven by a strong desire to see ongoing improvement.” – Interviewee

With the right culture, significant delegation was possible - which, in turn, enables innovation and better outcomes at lower cost. One interviewee said it was important to achieve a genuine culture of innovation, one in which it was safe to fail, but where those failures provide learnings to influence future design and delivery.

A number of interviewees felt their organisations had achieved the proper culture. Interestingly, at least one interviewee praised their organisation's “grass roots” culture while at the same time criticising its senior management culture, which was shaped by the influence of the Budget process (refer “Budgets: are they promoting better performance?”).

While supportive of staff motivated to “make a difference”, one interviewee emphasised the importance of retaining a good understanding of inputs and outputs. A sole focus on outcomes would not provide a solid foundation for driving improvements in efficiency.

Many interviewees stressed the importance of leaders driving culture. In this context, a number gave examples of setting high personal standards. Examples included:

- achieving “to time and budget”;
- not wasting tax payer money; and
- “Failure is not an option”, that is, getting the project done should not be negotiable.

One interviewee said it was much harder to get the culture right in an organisation with diverse Votes compared to one Vote. In comparison, in a unified organisation with a unified culture it was easier to promote a high level of performance. This interviewee had experience with both approaches. Another interviewee, however, felt a unified culture was less important, and we should expect organisations to have a number of different cultures. Provided these cultures are positive, and they are unified under a single purpose, that organisation should perform well.

Interviewees provided a number of examples where organisations had failed their clients, but had improved through changing their culture and capability. One interviewee told of an organisation that was performing poorly, with managers attributing poor performance to factors beyond their control, such as the type of ‘clients’ they had to work with and the amount of funding they were given. Yet, when a new leader was appointed to run the entity performance improved - despite the clients and resources remaining unchanged. The new leader instilled a strong culture of making a difference with what was available. Other organisations in the sector then followed suit, lifting performance more generally. This demonstrates that having the right performance information across the system coupled with the ability and willingness to learn, are important for driving overall system performance.

Centralising functions: opportunities for efficiency?

Many interviewees commented on the current trend to centralise government functions. One interviewee explained that a devolved system can result in wasteful duplication and lost opportunities for learning. Another felt there remained good opportunities to improve whole-of-government performance by further centralising government functions.

However, other interviewees felt centralising government functions remained a “work in progress” and more effort was needed to reap additional efficiency gains. Centralised procurement, in particular, was often mentioned. Interviewees said:

- centralised procurement was working well in places, but there was less confidence this was the case across the board;
- a “whole of New Zealand” focus was needed when making decisions to centralise procurement; for example, the impact on regional economies of changing to more centralised suppliers;

- it was important to have flexible and well-calibrated systems in place to ensure differences between organisations were appropriately taken into account; and
- judging the success of central procurement needed to be measured against the likely alternatives (ie, the counter-factual), and this was not always done.

A number of interviewees said centralised pay setting was detracting from state sector performance, although one commented it had helped to keep a “lid” on pay increases in Auckland agencies.

The social investment approach: An efficiency perspective

The social investment approach, together with the Better Public Service targets were supported by all interviewees who commented. Interviewees noted that these approaches are driving greater collaboration between agencies and improving performance. Joint funding bids are becoming a reality, approaches are becoming more client focused, and a range of outcomes (not just fiscal) are used to assess performance. The model was considered by some to be developing its own momentum. Some worried a change of Ministers might slow that momentum.

Some interviewees said for the social investment approach to work properly, it is necessary to de-emphasise inputs (for example, how best to achieve a given outcome), but ensure clarity on the outcomes expected. Head offices “giving up control to gain control”, as one interviewee put it, was expected to encourage innovation and better performance closer to the front line.

One interviewee identified their sector as an exemplar of the joined-up social investment approach, while acknowledging it still has much to do to achieve its goals. Interviewees from other agencies in the same sector shared this view. The reasons given for this sector being an exemplar were:

- the sector had a common, unifying purpose for staff to rally around and aid cross agency coordination;
- it had been purposefully working cross agency for longer than most other sectors;
- a common work programme across the state agencies in this sector had been developed, with matching funding and accountability;
- the implementation of the social investment approach was well resourced (in this case, the agency had made 10 FTEs available);
- the sector had a strong focus on evidence-based decision-making, and applied considerable effort to evaluating results;
- shared learnings were actively and strategically promoted between organisations; and
- the sector invested a great deal in making the wider network of relationships implicit in the social investment approach work (“relationships are everything”).

Another interviewee, from a different organisation in the same sector, also identified the importance of having capable Ministers who worked well together. Depending on the project, individual Ministers would come forward as appropriate to lead joint projects.

In contrast, an interviewee from a different sector felt the social investment approach, while needed, has only been tinkering to-date and was “mostly talk”. Another questioned whether government is collaborating on the right things, and whether collaboration is happening at the lower levels of organisations. This interviewee also noted the considerable time and effort required to “change the conversation” and establish trust to make the new approach work. Another interviewee noted the state sector system can feel “joined up” in Wellington but if it is not joined up away from the centre, then failure will result. Others claimed the link between outputs and outcomes is still not well understood, limiting the effectiveness of the social investment approach.

Another interviewee commented that the collaboration process that sits beneath the social investment approach needs to be efficient. Collaboration, they said, can be a “mess”. To avoid this, the right people needed to be involved. The private sector, the interviewee noted, was better at valuing time during such processes, and a similar drive was needed in the state sector. To a similar point, another interviewee said consultation could be done better. Resources continued to be wasted because agencies are not sufficiently focused on the purpose of consultation, and how best to achieve its purposes.

On the general point of cross agency collaboration, one interviewee noted there are more opportunities for state agencies to work together, and for senior staff to operate in governance-type roles with other agencies.

One interviewee, while supporting the social investment approach, noted its effectiveness depended on the ‘social licence’ given to government. Managing the most difficult cases could require, for example, intrusive personal profiling of clients and government being prepared to intervene aggressively at an early stage. This could become increasingly controversial as the social investment approach moved to target the most difficult areas.

Another interviewee said state sector officials should not be allowed to run their own agendas - for example, pursuing single issues at the expense of all else. Another said single issue organisations are becoming a thing of the past. That is, today, organisations have to incorporate all impacts into their policy advice, not only the impact on the sector they are responsible for developing advice on. This had perhaps helped to set the foundation for the social investment approach.

Cost recovery and contracting for services

Some interviewees felt cost recovery⁵ is a useful spur for encouraging a client-centric focus, efficiency in service delivery, and better performance. Technology was identified as an enabler of productivity improvements. Two interviewees said agencies with a strong client focus were perhaps better at adopting new technology.

A small number of interviewees, however, identified the risk that cost recovery is used inappropriately to circumvent the more rigorous oversight applied to new funding bids during the Budget process. They were also concerned some state agencies treated their paying clients as a “cash cow”. At least one interviewee felt cost recovery could reduce an organisation’s incentives to be efficient. One interviewee discussed the types of settings where cost recovery might be useful: for example, where clients are influential and capable enough to drive efficiencies in the provider; or where cost recovery may lead to the establishment of competitive markets, that is, competing organisations providing government services.

On a related issue, one interviewee mentioned the importance of using contestable markets to drive efficiency.

“Markets are useful for driving efficiency gains. For example, government procurement, using multiple suppliers, helps to test and drive improvements in productive efficiency.” – Interviewee

Another interviewee mentioned opportunities to drive greater efficiencies by making contestable funding available to competing social service providers in their sector.

“While the government has been moving in this direction in recent years, there remain many opportunities to achieve higher levels of innovation and cost saving through more competitive market arrangements, in preference to a single state provider.” - Interviewee

Governance issues

Governance is important for an organisation’s performance. For example, governance sets the strategic direction for the entity, and provides an important sounding board for senior management.

One interviewee noted that department Chief Executives tended to have greater scope and responsibility for organisational performance and efficiency than Chief Executives of a Crown entity operating under a board. The relative strength of these two models depended

⁵ Cost recovery occurs when a government agency seeks to recover some or all of the cost of providing a service from the users of the service.

on a number of things but, in particular, the relative capability of the Minister and board members, can vary greatly.

Two other interviewees suggested the State Services Commission could usefully become more involved with monitoring Crown entities. One suggested a well-resourced unit within the State Services Commission would be preferable to the poor level of monitoring currently undertaken via government departments. Another interviewee suggested the Crown entities model is overused and the state sector is more complicated than it needed to be.

Some interviewees felt central government controls are increasingly applied to Crown entities. This was not always helpful, sometimes detracting rather than contributing to performance. While Crown entities could be “difficult”, they believed the answer was not to impose more controls from the centre, but to replace the board, which would usually result in the Chief Executive going as well.

Many interviewees commented on the importance of departments' relationship with Ministers. The quality of those relationships depended on factors such as goodwill, trust, honesty, motivation, and capability. Several interviewees identified the need for state agencies to establish credibility with their Ministers (building up “credits”) and being clear with Ministers about the impact their decisions would have.

The seniority and capability of Ministers made a big difference for interviewees.

“Good Ministers could be significant catalysts for improving performance, challenging established thinking, identifying clearly what they want and to what level, providing good direction and cutting through the ‘bullshit’ ”. - Interviewee

A downside risk, however, was Ministerial priorities could lead to less focus on other important areas, resulting in these areas not being managed appropriately by state agencies.”

Interviewees' most common criticism of Ministers (with respect to governance) related to an inability to clearly articulate what they wanted, and tendency to stray into agencies' operational workings.

One interviewee outlined an approach whereby external stakeholders presented to the Minister and board on the value of an organisation's spend. The information provided by the stakeholders was described as “telling”.

Innovation, failure and the role of pilots

Overall, interviewees felt government is too risk averse. In their experience, politicians and the public both tended to overreact to failure, even when failure was a small part of total activity and is necessary for innovation. This led to state agencies becoming reluctant to try

new things in case of failure, and not sharing information on failure even though it may be useful to others.

One interviewee said we tend to learn more through failure than success. As they put it, failure itself is okay, but failure to learn from it is not. To illustrate, the interviewee told the oft-quoted story of an employee who lost a business \$5 million. The employee apologised for their mistake and tendered their resignation. The employer refused the resignation, commenting that it would be a waste of \$5 million.

Early in the interview schedule, the issue of pilots was raised by interviewees. Pilots are a tool to promote innovation and efficiency in a low-risk, low-cost way. The interviewer asked about pilot programmes in subsequent interviews.

There were divergent views about the value of pilot programmes. Many felt they are not working. A sizable minority felt they are working well, at least in their sectors.

One interviewee thought that post-implementation review of pilots was of poor quality and useful information on “failures” virtually non-existent. Another suggested pilots have not led to system-wide changes. Some said it is difficult to stop pilots that do not work - although one suggested this is getting easier. Another said some pilots are not given enough time to demonstrate positive results.

The latter perspective is consistent with the view that government is increasingly grappling with long-term issues. One interviewee suggested the social investment approach is contributing to a better use of pilots, and realising learnings in general.

On the potential benefit of pilots, another interviewee noted:

“There is a tendency in government to invest in projects that are ‘too big to fail’. Carefully designed pilots are one approach that might provide the information needed to avoid costly mistakes prior to the so-called ‘point of no return’.” - Interviewee

Some interviewees noted that pilots may not be amenable to scaling; that is, they are successful in only a limited range of circumstances. These are not true pilots but “localised solutions”.

Pilots can face a negative perception that people are treated as “lab rats”. One interviewee said their organisation had established an ethics committee to manage this perception and any human rights and privacy issues.

Two interviewees commented that, rather than running pilots, it may be better for the state sector to strive for well-designed and monitored, but incremental, change to the system.

One interviewee suggested the model for funding pilots should be revisited.

Efficient organisations and inefficient standards

A number of interviewees noted that irrespective of how efficient a government agency is, if the regulations they are administering are inefficient, the outcome would ultimately be inefficient. And one interviewee commented:

“It is important that standards are frequently reviewed to ensure they are up-to-date, in particular in the face of technology advances. This requires a deliberate effort to overcome government organisations’ reluctance to trying something new.” - Interviewee

Part II: Barriers and opportunities to improving the efficiency of the state sector

Introduction

Part I presents the views of interviewees on five topic areas. Part II offers comments from the interviewer and presents findings on measuring and improving state sector efficiency.

The state sector has limited resources to achieve good results or outcomes for the community. The challenge is, how does the state sector get the most value from its limited resources? That is, how does it deliver those state sector goods and services of greatest value to the community, at least cost, now and into the future? This is the three-part question posed by economic efficiency – allocative, productive and dynamic efficiency.

The state sector is a complicated system directed to achieving numerous, often conflicting objectives. There are many interrelated moving parts. Good information on state sector performance is hard to find and can be difficult to generate. In some areas, it takes many years to see the impacts of government action. Pathways between resources, what is produced, and the impacts of government action on communities are uncertain.

This is not unique to New Zealand; these problems occur in every state sector around the world.

Setting the scene: How well is the New Zealand state sector performing?

Many interviewees commented on how well they thought the New Zealand state sector is performing. This provides useful context for considering the specific challenges to improving and measuring state sector efficiency as identified by interviewees.

Over time: There were a range of views on whether state sector performance was improving over time. Those who felt there has been improvement commonly identified the social investment approach, an approach they suggested offered a better way to tackle substantive and complicated problems, such as child poverty and drug dependency. Also, interviewees suggested a more prevalent ‘outcome-based’ culture and stronger client-centric focus were drivers of better performance.

Not all interviewees agreed state sector performance is improving. Some commented on the growth of a “one size fits all” system that, in places, was imposing more cost than gain, and others on a system that increasingly acted to weaken Chief Executive and agency accountability. Interviewees also mentioned politicians having a greater adverse impact on agency performance than in previous decades; and the growth of a more permissive environment with less guidance for public servants, which can pose risks to inter and intra-agency performance.

Differences between state sector agencies: Interviewees commonly observed that performance across the state sector is “variable” and “patchy”. Implicit from interviewee comments was the observation of a large performance gap between laggards and exemplars. The characteristics of agencies are likely to have a large impact on performance. Specifically, better performing agencies have effective leadership, strong culture, appropriate accountability mechanisms, and good information to drive better performance.

State sector compared to the private sector: Interviewees generally considered the state sector is not performing well, compared to the private sector. “It is so much harder to get anything done”, was a common observation from those who had experience with both. Further, in interviewees' experience, the private sector had comparatively strong incentives to deliver low cost goods and services most valued by clients. Over time, the private sector entity's survival depended on this. Also, compared to many of the social objectives pursued in the state sector, the private sector profit object was relatively easy to measure and hold people to account for, and did not conflict with the objectives of owners, boards or shareholders in the same way that efforts to improve state sector efficiency could conflict with political objectives.

New Zealand compared to the world: Compared to public sectors around the world, interviewees felt the New Zealand state sector performed well. For example, an interviewee mentioned the delegations who visited to learn from New Zealand.

Finding 1: Interviewees generally felt state sector performance is improving is good compared to the rest of the world. However, the performance gap between “leaders and laggards” and between the state and private sectors suggest there are opportunities for significant gains in performance.

The language and understanding of efficiency

All interviewees understood the importance of basing their decisions on the concepts underlying economic efficiency, although some were less familiar with the technical terms. In particular, many attributed efficiency to mean *productive* efficiency only. Most interviewees felt the understanding of efficiency across the state sector is poor. Almost all agreed the language of economic efficiency was neither well understood nor necessarily well accepted as an appropriate objective for the state sector.

By way of further explanation, many interviewees noted most employees in the state sector are strongly motivated to “make a positive difference” to the community. Seeking greater efficiency, in contrast, is often viewed as a threat to services and, therefore, community wellbeing. It is likely state sector employees undervalue the opportunity cost inherent in inefficiency. That is, they do not place a high value on the alternative services and benefits that could be achieved when savings are made. This is because these benefits are likely to

be out of sight to employees, especially where those benefits accrue beyond the agency's clients.

Finding 2: Allocative, productive and dynamic efficiency are important concepts for improving state sector performance. Yet, these concepts are not well understood within the state sector. For many officials, the term "efficiency" has negative connotations. This view may act as a barrier to improving state sector performance.

Finding 3: Proponents of improving state sector performance, in particular senior leaders, need to understand efficiency well enough to persuade others of its importance. In particular, senior leaders must be able to explain the connection between efficiency and achieving broader community outcomes. A formal training programme for current and aspiring state sector leaders may be required. This should include training in the measurement of efficiency and the use of efficiency indicators in state sector contexts.

Competing objectives

Political

There are many objectives in the state sector that can compete with efficiency objectives.

At the top of the list for the interviewees were political objectives. It would be easy to portray politicians' vote maximizing behaviour as conflicting with the intrinsic welfare maximising motivation of public servants. But the story is more nuanced. Some interviewees spoke of politicians who wanted to cut down on waste, ensure their interventions are successful, and encourage innovation in the public interest. Interviewees provided specific examples of Ministers being the catalysts of performance improvement. However, interviewees also provided examples of Ministers not wanting to:

- be associated with failure (a necessary accompaniment to innovation);
- be seen supporting initiatives that would harm their supporters; or
- back policies that were unpopular with sections of the community (even if those policies produced the greatest net benefit for the community).

All interviewees sought to actively manage the conflict between political and efficiency and welfare objectives, although some came across as more active managers than others. This perhaps spoke to the "art" of effective relationship management between senior state sector leaders and their Ministers. That art, interviewees said, includes building up credibility and trust with the Minister, free and frank advice ("speaking truth to power"), making sure Ministers understood the policy trade-offs, and adjusting options to better accommodate political objectives in a way that posed less threat to the efficiency of

government services or overall welfare outcomes. Managing the relationship successfully is not easy - it is not the path of least resistance.

Leaders with neither the skill nor the character to manage the relationship with Ministers, interviewees noted, risk losing the respect of peers and staff, and compromising organisational culture.

Finding 4: There can be conflict between efficiency objectives and political objectives. A good relationship between Ministers and senior leaders can help to reduce these conflicts. Building good relationships is difficult. Those leaders who do it poorly risk, not just state sector performance but also the respect of peers and staff, and a strong positive organisational culture.

Giving the appearance of being busy and focusing on shiny new projects

Interviewees commented some senior officials are motivated by “being seen to be busy”, and are often distracted by “shiny new projects”. Both these motivations detract from the performance of the agency. These motivations may be linked to senior officials wanting to be seen as hard working and innovative, and be rewarded with career progression as a result.

Of course, laziness should not be rewarded - but nor should being busy doing the wrong things. Rather, the state sector needs to pursue activities that are highly valued by society. If resources are not employed in their highest value use, they should be reallocated.

Even if motivated to surrender resources, the senior leader can be thwarted. One interviewee gave the example of offering up savings because there were no high value agency activities deserving of the funding, only to have that offer rejected by the responsible Minister.

Some interviewees felt there are many opportunities to allocate resources to high-value activities. One example was the pioneering work on regulatory models and cost benefit techniques undertaken by the Ministry of Transport in the late 1980s. This work laid the foundation for performance improvements across the state sector, and well into the future. While some Ministers may not give a high priority to such work, one interviewee explained that many state sector leaders recognise and value these investments.

Finding 5: Senior officials can be motivated by “being seen to be busy” or can be distracted by “shiny new projects”. Both these actions can detract from a focus on the efficiency of the state sector. Peers recognise these behaviours.

Making a difference

Contrary to populist views about a public service work ethic characterised by minimal effort, interviewees said state sector employees are more often than not strongly motivated by a desire to make a positive difference to the community - for example, by reducing crime, and improving health and education outcomes. Interviewees mentioned agencies with motivated staff increasingly applying a client-centric and outcome focus to their work.

For the most part, staff motivation was viewed by interviewees as a positive driver of state sector performance. However, one weakness was identified: Staff may give disproportionate weight to the wellbeing of *their* clients at the expense of overall welfare. This could result in a failure to:

- identify and remove waste (improving productive efficiency); and
- cease low-value activities to free up resources for spending elsewhere in the economy (allocative efficiency).

Finding 6: State sector staff are often motivated to make a positive difference to their clients. While senior leaders should welcome and support this motivation, it is important leaders do not allow it to become an obstacle to eliminating agency waste and low-value activities.

Self-interest

Some interviewees alluded to the pursuit of self-interest among senior leaders at the expense of efficiency objectives. Comment has already been made of career prospects (above). Similarly, interviewees mentioned competition for “Budget funding” to build organisational size and, therefore, the status of individual leaders. This is commented on further below under “System-wide accountability and performance requirements”.

State agency performance management systems

Introduction

Two strong themes emerged from the interviews that frame the following discussion on performance management systems.

- Systems wide performance and accountability requirements produce little in the way of positive incentives on government organisations to improve performance
- Much depends on the action taken by senior leaders (Chief Executives, Ministers and boards) to actively put in place initiatives that will drive better performance.

With respect to an organisation's performance management system, interviewees generally believed that, when designed and implemented well, these systems can be a powerful aid to improving performance.

A good performance management system

Working back from objectives, a good performance management system will:

- provide effective incentives on organisations and their constituent parts to realise higher levels of performance; and
- collect information to inform decisions on:
 - reducing waste;
 - opportunities to produce higher value goods and services; and
 - whether to continue with specific initiatives or programmes.

Interviewees identified the need for:

- good systems and processes (for example, systems that are well integrated);
- good people adequately resourced for the task;
- collecting the right information and ensuring it is easily accessed;
- using the information to inform decisions and motivate performance; and
- ongoing monitoring to ensure the performance management system remains fit for purpose.

Building a performance management system

Performance management systems will be unique to every organisation. Below is an attempt to draw out the common themes identified by interviewees likely to apply when building performance management systems in the state sector.

The first step in building a good performance management system is commitment from the Chief Executive and, ideally, the Minister. Avenues for collecting information on the suitability of the existing performance management system include:

- the senior management team;
- internal and external auditors;
- specialist external advisors;
- stakeholders, in particular, clients, but also the Minister; and
- other Chief Executives (including the organisation's previous Chief Executive), in particular those who have successfully implemented their own performance management systems.

Achieving buy-in from key stakeholders

Interviewees identified staff buy-in as important to the success of a performance management system. Some staff may view a performance management system as a threat, either to them personally or to the organisation's ability to make a positive difference to the community. For example, staff may believe performance management is motivated solely by cost cutting. These negative attitudes place the effectiveness of a performance management system at risk, and need to be carefully managed. This may include identifying from staff feedback whether there is a problem and managing that problem with situation-specific communication.

Staff should be heavily involved in the development of performance management systems. This will facilitate staff buy-in and the useful exchange of information. One interviewee identified the use of champions to facilitate two-way communication on a performance management system's development. A dedicated unit accountable for developing a performance management system, with good connections to the rest of the organisation, was also pointed to as a useful step.

Ministers also need to come on board. Some interviewees said Ministers may be concerned about the threat a performance management system may pose - for example, through exposing organisational failure for which they are responsible. However, other Ministers will themselves be the spur for ensuring an adequate performance management system is in place, to improve the quality of their decisions and to lift organisational performance to achieve better outcomes.

Deciding on the information to collect for performance management

Information collected needs to relate to the organisation's purpose. Ultimately, the organisation's performance will be judged against that purpose.

One interviewee commented that information must first meet the needs of management. Management need to be consulted on what information is needed to best make decisions on resource use, and to hold others to account. At the beginning, this should focus on a "need to have" rather than a "nice to have" threshold. Over time, information can be added to and removed as the environment changes and the performance management system evolves.

At the next level, governance information needs to be made available to Ministers and boards. This should be a summary or aggregation of the management information. At least a portion of this is then made available to the public.

Once there is a good feel for the information that needs to be collected to support the performance management system, it is necessary to look to what information is already

collected. All entities will hold transactional data and data for keeping track of input and output costs. In many cases, this may be sufficient.

However, to ensure the right goods and services are being provided and in the right quantities, information on outcomes is necessary. In some areas, this is relatively straightforward. For example, there is very good information on road fatalities and causes. However, in other areas, getting outcome information can be costly, and the information generated inaccurate and incomplete. For example, establishing causation and relative outcome shares across the many factors contributing to mental health is difficult.

If the expertise necessary to provide a good foundation is not available in-house, contracting external expertise for advice might be necessary. Similarly, in many areas, community-based social service providers are delivering services on behalf of government agencies and should be consulted.

Developing performance metrics and targets

Performance metrics need to relate to what matters to an organisation's performance, rather than what is easy to measure. Several interviewees supported a greater use of performance targets and metrics. This, however, needed to be done well if perverse outcomes were to be avoided.

The relevant metrics need to be agreed between the main stakeholders, interviewees said. Without that agreement, stakeholders are likely to be distracted by arguing the relevance and reliability of the measures rather than using them to improve performance. One interviewee explained in some detail how this had happened in their sector. Additionally, simply imposing measures from the top down risked fracturing the relationships between principals and agents. If necessary, an agreed process for arriving at the metrics should be put in place.

In the early stages of developing an effective performance management system, it may not be practicable or sensible to introduce performance targets. The information may not be reliable enough at that point, and the risk of unintended consequences may not be well understood. As performance information comes in, it needs to be discussed with key parties to ensure it is robust enough to use without excessive fear or driving performance in counterproductive ways.

To the extent performance targets can be identified and agreed at an early stage, it is important they are not too ambitious, and that any action taken in response to negative variance errs on the modest side while people get used to those measures, and how they operate and impact behaviours. This differs from aspirational targets, for example, eliminating child poverty⁶.

⁶ One interviewee explained the use of aspirational targets for motivating and focusing staff effort.

The social investment approach

A performance management system that supports the social investment approach is in principle the same as for a single state agency, only much harder. A performance management system demands collaboration and coordination across agencies with different cultures, capabilities, priorities and accountabilities. To do it well requires commitment, investment, openness and trust.

There is one design feature that may increasingly be looked to as the social investment approach takes on greater prominence. One interviewee spoke of the 'social licence' needed for government organisations to profile clients and intervene as intrusively in their lives, as might be required for those interventions to be successful. Another spoke of an ethics committee established to consider issues relating to privacy and human rights issues as an input into pilots.

Such a committee may also explicitly consider and advise on issues relating to 'social licence' issues. If the expertise needed does not reside in-house, government organisations may consider grouping together to provide the expertise to ensure these issues are appropriately managed.

Using and improving the performance management system

Relationships are important

It is clear from interviewees that good relationships between those generating the information and those using it are vital. Without good relationships, performance management systems will struggle to improve organisational performance.

One interviewee said the starting point is to assume that both sides to the performance relationship, principals and agents, are wanting and trying to do what is right. These parties are typically Ministers, boards, Chief Executives, staff and contracted providers (supplying inputs to the government organisation, or goods and services directly to communities).

Mutual respect between the parties is important, as is a desire to build a mature relationship focused on the shared goal of improving performance. Improving performance is the touchstone all parties should be united by, guiding all decisions *ex ante*, and on which decision-makers should be ultimately judged, *ex post*.

Using performance information

Performance information is used to hold parties to account for their performance (incentives), and to better inform decisions to aid future performance (capability).

At the early stages of developing a performance management system, it is best to focus on the latter, at least until there is a robust and shared understanding of what the information being generated means and what the appropriate metrics may be. One interviewee commented that to be useful for decision-making, information needs to be timely, complete, accurate and relevant. Efforts need to be made to understand weaknesses in the information and the risks in using it. Strategies must be put in place to manage these risks and weaknesses.

Value does not come from the information generated alone. The process of deciding what information is most needed and interrogating information weaknesses (through engagement with stakeholders and research) should result in a better understanding of the organisation's activities, and the contribution those activities are making to the organisation's purpose. One interviewee commented on how working through this process would strengthen government's intervention logic.

When using performance information to incentivise good performance, one interviewee said it is important to use variance from the target as a *starting point* for dialogue. For example, in seeking social outcomes, performance information will rarely be complete enough to act on without dialogue to understand why targets are not being met. Another interviewee said soft information from experienced and trusted parties is often helpful to supplement hard data. Those on both sides of the performance relationship need to be sufficiently skilled and motivated to enter into this dialogue in a mature way.

Senior leaders interviewed identified a number of risks to manage in using performance targets. Targets should be achievable, otherwise they will fail to motivate, and may even dispirit organisations and staff.

Similarly, holding organisations to account for things they are not responsible for can cause ill will and strain the relationship between principal and agent. Controls on agency input mix and centralised wage setting were examples identified by interviewees. Also, targets based on what is easily measured rather than important is a risk that must be managed because "you get what you measure."

Further, releasing performance information to the public should, ideally, promote better organisational accountability and performance. However, if the information is incomplete, is not understood, or is used inappropriately by stakeholders (including the media), there is a risk the organisation will be encouraged to behave in ways that could be counter to good performance.

While acknowledging this risk, where possible, organisations should err on the side of releasing information and front footing how that information should be used by stakeholders. This approach is more likely to promote a healthy internal culture and to lift public and stakeholder understanding of state programmes. It is the responsibility of senior

leaders, in their governance and stewardship role, to spearhead the correct use of performance information relating to their agency.

As noted above, agents have a role to play in making the relationship with principals work. Interviewees identified the importance of having skilled people manage that relationship, approaching it in good faith, and being transparent. Specific approaches may include notifying principals of issues early - for example, before issues are picked up in the performance information, and proactively and collaboratively working to find solutions.

It is advisable for agents to avoid the distraction of defending performance, and to remain focused on achieving good outcomes. Ultimately, the principal is responsible for the performance measures chosen and for the consequences if measures are inappropriate or used inappropriately. The agent should provide free and frank information on those risks, but otherwise remain focused on their performance.

Finding 7: Properly designed and implemented performance management systems are a powerful aid to improving performance.

Finding 8: An effective performance management system will have robust systems and processes, skilled and adequately resourced people, and access to good quality information.

Finding 9: Building a good performance management system requires the buy-in of stakeholders, being clear about the information needed to drive improvement, and agreeing on the metrics and targets appropriate for the agency.

Finding 10: Performance management systems require regular review to ensure: the use of the information collected is having the desired impact and the relationship between those providing and those using the information is constructive. This is the responsibility of the Chief Executive.

Systems-wide accountability and performance requirements

State agencies are subject to many accountability and performance requirements. The purpose of these requirements is to hold agencies to account for their use of taxpayer funds and the exercise of regulatory powers, and to encourage better performance with respect to both.

Few interviewees could point to effective system incentives for government organisations to reduce waste, produce the right things, or take the risks necessary to innovate. Instead, interviewees told of an environment which encouraged: a costly scramble for resources, siloed thinking, the appearance of being busy, risk averse behaviour and short-termism. Clearly, the architects of the accountability and performance measures did not intend this. Too often, however, the wrong performance information was provided to central agencies,

or the information provided was used in the wrong way or not at all. These concerns came from interviewees across the state sector, including those with experience in central agencies.

Some interviewees pointed to the Budget process as a possible tool for improving performance, through:

- a gradual tightening of departmental budgets to find cost efficiencies; and
- a severe budget shock, forcing the agency to revisit what and how it delivers services.

However, interviewees also identified failings arising from the Budget process and requirements, including encouragement of:

- short-term thinking based on annual appropriations;
- an inward state agency view rather than a joined-up “New Zealand Inc” perspective;
- a bias towards agencies competing for Budget resources rather than collaborating to fund higher value joint Budget initiatives; and
- excessive resource claims, due to a perception Chief Executive rewards are based on budget size rather than performance.

Others interviewees felt the Budget process was too inflexible - for example, preventing agencies from using savings in one area to fund activities elsewhere (although this may not be the reality).

Finding 11: There was widespread concern from interviewees that accountability and performance requirements on government agencies are costly and fail to provide strong incentives to improve performance.

The requirements

There appear to be strong similarities between the concerns raised by interviewees and the concerns raised by business leaders in the private sector with respect to the government requirements businesses must comply with. Drawing on the standard approach used by government to deal with business compliance costs may suggest the following.

- Preparing a stock take of performance requirements. This may quickly lead to the culling of the least value requirements - for example, where there is double-up or no central agency or other grouping (for example, Select Committees) using the information produced. Next, the requirements could be mapped to each other to see if there remains unnecessary duplication or gaps, or to see if the relevant information can be collected through a more coordinated and streamlined approach.

- More thoroughly reviewing the remaining performance requirements to determine their utility, including considering the risk they may be working against primary regulatory frameworks (such as the State Sector Act 1988) and reducing Chief Executive accountability.
- Ensuring performance requirements are fit for purpose. In particular, the social investment approach was supported by interviewees. However, the accountability and performance requirements are not well-g geared to supporting this approach. Appropriations, accountability and organisational structure all work against a more joined-up approach.

Finding 12: Concerns from interviewees suggest there may be merit in reviewing the stock of performance and accountability requirements on state sector agencies. There may be something to learn from reviews of compliance requirements on the non-government sector.

Implementation

The performance and accountability requirements imposed on state agencies are important but so is their application and enforcement. Interviewees frequently complained this is not always done well.

Many interviewees spoke of enforcement too often being undertaken by staff who lacked the needed experience and skills, who applied a tick box, one size fits all approach, and who sought to “catch out” and punish state entities. There tended to be a presumption of bad faith held by central agencies with respect to the behaviour of agencies.

Some interviewees alluded to a more principle-based implementation as a preferred model. Where principle-based approaches work well, they are likely to be superior to input-based approaches. In particular, principle-based approaches enable innovative and superior ways of meeting requirements compared to prescriptive input-based approaches.

Similarly, there is considerable difference between a gate keeper who polices standards and punishes those that fail to meet the standards, and the facilitator who considers it their job to help agencies and individuals meet the standards in the most efficient way possible. It is important central government agencies should aspire to the latter level of service. The Productivity Commission’s Regulatory Institutions and Practices inquiry report (2016) covers this issue, and has other lessons that may equally be applied to better management of the state sector.

An important prerequisite to successful implementation of principle-based approaches is having highly capable and motivated staff, who are able to establish and retain positive relationships, and make difficult judgments on when and how best to apply the levers available to them.

One option is to draw together multi-disciplinary teams from across central agencies, tailored to the entity and the issues to be considered. This would help to reduce duplication of effort and compliance costs, enhance effectiveness, and reduce the likelihood of organisational capture. Further, Chief Executives themselves could be able to call on these specialist external teams.

Finally, agencies themselves, in groupings appropriate to the issue being dealt with (mental health, for example), should be encouraged to come up with the appropriate accountability, performance and funding infrastructure to best achieve their joint policy objectives.

Finding 13: Change is required to system-wide accountability and performance requirements on state agencies if those requirements are to contribute significantly to lifting state sector performance. There may be lessons for what that change may look like from work on regulatory models outside government.

State sector leadership: responsible for lifting state sector performance

State sector accountability and performance requirements are not seen as strong drivers for better performance. However, leadership does appear to be a strong driver. This is supported indirectly by interviewees' comments and by observations of variance in agency performance across the state sector and over time.

Senior leadership comes, in particular, from Ministers, Chief Executives and boards. In general, interviewees believed the difference between the top and bottom performing leaders could be characterised as character (values), passion, and capability; the latter encompassing both experience and hard work⁷. The “luck of the draw” plays a part in allocating good leaders across agencies.

The right leadership will promote the culture needed to support good performance. Good leaders will put in place effective performance management systems and set high standards, and will protect against objectives in the state sector that can work against efficient performance.

Finding 14: In the absence of strong incentives from existing performance and accountability requirements, the state sector is reliant on good leadership to drive agency performance. Leadership appears to explain much of the difference between high and low performing agencies.

⁷ This is similar to a standard institutional analysis framework; that is, incorporating incentives, capability and capacity, but with character or values substituting for incentives. The purpose of this framework is to help answer the question, “what institution is best placed to perform a given function?”

When thinking about the leadership *capability*, *capacity* and *incentives* needed to drive agency performance, it is useful to think about the three distinct stages of: getting the right people into the top positions (entry): removing senior leaders who need to be moved on (exit); and enabling and supporting high performance by senior leaders (ongoing).

Entry

One interviewee emphasised the important role introspection plays in identifying personal flaws that may impede promotion to more senior roles. By inference, second tier leaders need to engage in careful introspection, perhaps assisted, to identify gaps and devise the most appropriate ways of closing those gaps. (*capability building*)

Some interviewees said they provide mentoring. Both the supply of and demand for mentoring within the state sector should be encouraged. The dialogue possible with mentoring, and the ability to tailor it to individuals and specific circumstances makes it a valuable mechanism for encouraging personal development in leaders. What was clear from the interviewees was the rich resource available for mentoring in our current and past state sector leaders. (*capability building*)

A number of interviewees commented on their experience in the private sector. It seems likely state agencies are increasingly seeing that experience as valuable for contributing to their performance. There may be merit in providing senior state sector managers with placements in private sector organisations as another way of developing that expertise. (*capability building*)

Not all senior managers have the expertise and confidence to use performance (efficiency) information well. All managers aspiring to senior leadership positions should ensure they have the training necessary to fill these gaps so they are able to use performance information effectively. Looking forward, it is reasonable to assume this expertise will be increasingly valued and expected in state sector leaders. (*capability building*)

Ongoing

As discussed above, there is a risk that centralising accountability and government functions will reduce Chief Executive and board accountability. This needs to be factored into central agencies' decision-making when they review the existing stock of accountability requirements, and consider imposing new requirements. (*improving incentives*)

Further, accountability and performance requirements on state agencies are not strong drivers of agency performance. In this context, any systematic review of the stock of agency requirements should also explicitly consider the risk that existing requirements are diverting senior management time towards low-value activities. (*improving capacity*)

A number of interviewees said poor performing senior leaders were recognised by their peers and others. In some cases, it was apparent from the interviews that senior leaders help each other. However, this may not universally be the case. “Bullies” and “untrustworthy” leaders, for example, were less likely to receive peer support. Again, introspection is an important trait of leaders. (*improving incentives and capability*)

Exit

Interviewees identified a number of important, positive characteristics for leaders. Senior leaders are ideally placed to identify the characteristics that matter the most (a list is provided in Part I). These characteristics need to be considered when making decisions on whether to remove a senior leader from their position for poor performance. A few of these characteristics are touched on below. (*improving incentives and capability*)

- Learning from failure is important. The consequences of failure were identified as a problem in the state sector that can result in overly risk averse behaviours. Bringing these two messages together, it may be concluded that it can be acceptable for a leader to fail, but not acceptable for a leader not to learn from that failure.
- The importance of leaders establishing and maintaining good and productive relationships was identified by many interviewees. Many factors feed into whether a leader will be successful at relationship building, including people skills, understanding different perspectives and honesty.
- A number of examples were provided of leaders who blamed their poor performance on things they considered beyond their control - for example, budgets, the clients they had to work with, and Ministers. Successful leaders seemed to have an ability to look beyond the constraints and focus on what they could change, which in some cases included the constraints they had to work with.

A number of interviewees felt the state sector system is not sufficiently rigorous in removing poorly performing senior leaders. Too often, these leaders are allowed to continue, or are shifted to other roles. The bar on acceptable performance needs to be lifted. Assumptions underlying these comments include: there are better leaders available elsewhere; or, raising the bar will encourage better leadership performance overall.

Finding 15: Senior leaders are well placed to identify leadership problems and provide solutions to those problems. A range of options for improving incentives on, and the capability and capacity of leaders have been identified. These options would contribute to better state agency performance.

Inefficient regulatory standards

A number of interviewees identified outdated regulatory standards⁸ as a key barrier to better performance of agencies undertaking regulatory functions. The broad point made was, it doesn't matter how efficient the state agency itself might be, if the standards it administers are inefficient, the outcome will also be inefficient.

An example of where a regulatory standard has changed is the extension in the period between WOF checks on newer vehicles. This is because improvements in vehicle technology have made frequent inspections of newer vehicles of marginal value.

It is not just changes in technology that can produce inefficient standards. Changing community attitudes, emerging issues (such as climate change), and growing knowledge of better ways to regulate activities can all make existing standards outdated and inefficient. This problem is compounded by a rapidly growing stock of regulation against a relatively fixed capacity of the state (Parliament, Cabinet and individual Ministers and Chief Executives) to keep regulatory standards up-to-date.

Much has been written on what efficient regulation looks like. The Productivity Commission has been leading this discussion in many areas in recent years. This section of the report offers comment on only two aspects: the greater use of standards that accommodate change, and making it easier to update standards.

Encourage greater use of performance, principle-based and deemed-to-comply regulatory standards. One advantage of these types of standards is they better accommodate change and are less likely to become outdated than input-based standards. They do not, however, work well in all situations, and can produce inferior results if, for example, regulators lack the capability to administer them correctly. There may be merit in reviewing government standards setting to see if there are inappropriate barriers to performance, or principle-based and deemed-to-comply regulatory standards that should be addressed; and, if so, how best to remove those barriers.

Recalibrate upwards the threshold between primary and tertiary regulation. As a rule, tertiary regulation does not require as much Parliamentary or Ministerial time to approve as primary regulation. By adjusting the threshold upwards, Ministerial and Parliamentary capacity constraints will become less of a barrier to updating regulatory standards. This, however, could be at the expense of democratic accountability, and could increase the flow of regulation. An alternative but similar approach may be to put in place a 'lighter' regime, with fewer checks for regulatory amendments of a routine or mechanical nature. There may

⁸ It is recognised *outdated regulatory standards* is only a subset of *poor quality standards*. The wider topic is covered in a voluminous amount of literature. Only outdated standards, identified by a number of interviewees, is commented on here.

be merit in exploring these and other options that address the growing problem of outdated and inefficient regulatory standards.

Finding 16: State sector performance is a function of the efficiency of state agencies but also the quality of the regulatory standards being administered by those agencies. Some interviewees pointed to the problem of outdated regulatory standards. It appears this problem is growing and action should be taken to manage it.

Competitive market structures

A number of interviewees commented on the role competitive markets can have in encouraging better state sector performance.

It is generally accepted that, in most circumstances, better performance is achieved where multiple providers compete to provide a good or service, compared to a single provider supplying the same good or service⁹. Allocative, productive and dynamic efficiency should all be superior in competitive markets compared to a statutory monopoly provider. This is a key difference between the state and private sectors – departments do not compete with each other, except for budget funding. The strong efficiency disciplines in the private sector, competition and survival, are virtually non-existent in the public sector.

In the New Zealand state sector, over the last several decades, there has been a general move towards competitive markets to supply state goods and services. This has been enabled by two approaches.

- Contracting with state and private agencies to provide services, for example, universities and social housing providers.
- Cost recovery for state-provided “private goods”¹⁰. Once a cost recovery regime is in place, it then becomes possible for non-government agencies to compete to provide that service, with the government role usually reduced to licensing and monitoring those providers.

Competitive markets provide:

- choice between providers to better meet differing needs and preferences;
- a credible threat of exit for poor performers;
- entry for more efficient providers;
- strong incentives for providers to perform (survival); and

⁹ The exception is in markets where the marginal cost curve slopes sharply downwards. In this case, the gain from superior productive efficiency will exceed the losses in dynamic and allocative efficiencies.

¹⁰ Goods or services where the benefits of consuming that good or service accrue almost exclusively (are *private* to) the consumer.

- the opportunity to collect and use high quality comparative performance information.

The introduction of competitive suppliers can create risks that need to be managed. These were identified in the Productivity Commission's 2015 inquiry *More effective social services*. Typical risks may include:

- funding set at a level insufficient to cover high value investment in training and innovation;
- inadequate monitoring of provider performance and unintended consequences;
- agent opportunism, for example, gaining competitive advantage through cherry picking low cost clients;
- too little certainty for agents to invest in innovation; for example, due to the short length of the contract; and
- being unable to promote the dissemination of key learnings from one provider to its competitors and potential competitors.

A key message from interviewees was the importance of relationships, at all levels. This also applies to competitive markets. One interviewee mentioned, for example, the difficulty of collecting some performance information from parties they were contracting with, because those parties were concerned by how the information might be used. Issues relating to commercial sensitivity and privacy concerns might be examples.

With respect to cost recovery, some interviewees pointed to the risk that it could be used by government organisations as a soft option to increase revenue. One commented that central agencies do not exercise the same oversight of third party-funded services compared to taxpayer-funded services. No one suggested all government services should be cost recovered, or that all should be taxpayer funded.

That said, a number of interviewees pointed to cost recovery, even absent competitive market structures, as a mechanism to encourage a stronger client-centric approach and better organisational performance. One interviewee provided an example where the government provider was able to approach its clients to inform its decision on achieving the most appropriate balance between cost, accuracy and timeliness. This was possible only because the payee and the beneficiary was the same party.

Finding 17: Cost recovery and contracting for the provision of state sector goods and services can be a catalyst for improving efficiency. It is likely opportunities for improving efficiency through these approaches remain untapped and new opportunities continue to emerge - for example, as technology makes direct road charging a possibility.

Pilots

Many interviewees said the state sector is too risk averse. For example, the potential fallout from the failure of new initiatives was heavily weighted. Yet, all interviewees pointed to the importance of trying new things as a driver of future improvements in state sector performance.

Pilots provide an opportunity to test, on a small scale, the cost effectiveness of new initiatives prior to those initiatives being applied more widely. If unsuccessful, the pilot ceases and any learnings are taken and applied elsewhere. To work as intended requires careful planning, in particular with respect to how the pilot is assessed.

Many interviewees said pilots are not working as intended. Key criticisms included that pilots were not properly assessed, were not ended when it became clear that they did not meet their objectives or were *inefficient* in meeting their objectives, and were often not scalable.

Finding 18: The performance of pilots in the state sector has been mixed. It may be timely to review state sector experience with the way pilots are undertaken and assessed.

Appendix 1: List of people interviewed

Name of interviewee	Current position and selected previous experience
Helen Anderson	<p>Former Chief Executive of the Ministry of Research, Science and Technology.</p> <p>Current Chair of the Building Research Association of New Zealand and Director of DairyNZ, Antarctica New Zealand, and the National Institute of Water and Atmospheric Research Ltd. Member of external advisory committees for the Department of Internal Affairs and the New Zealand Police.</p>
Murray Bain	<p>Current Chair of Open Polytechnic and Top Energy Ltd. Deputy Chair of TSB New Zealand Ltd.</p> <p>Former Chief Executive of the Ministry of Science and Innovation, the Foundation for Research Science and Technology, and Catalyst Insurer Services. Former Assistant Governor of the Research Bank of New Zealand.</p>
Dame Margaret Bazley	<p>Former Commissioner of the State Service Commission and Secretary for Transport. Former Director General of the Department of Social Welfare and Chair of Environment Canterbury.</p> <p>Appointed to numerous commissions of inquiry including the Commission of Inquiry into Police Conduct and the Royal Commission on Auckland Governance.</p>
Nic Blakeley	<p>Deputy Chief Executive (Insights and Investment) at the Ministry of Social Development (MSD). Former Deputy Chief Executive (Social Policy) at MSD.</p>
Ruth Bound	<p>Deputy Chief Executive (Service Delivery) at MSD. Former General Manager (Retail) at Contact Energy.</p>
Debbie Chin	<p>Chief Executive of Capital & Coast District Health Board.</p> <p>Former Chief Executive of Standards New Zealand, Deputy Director General at the Ministry of Health and Partner KPMG.</p>
Belinda Clark	<p>Current Law Commissioner.</p> <p>Former Chief Executive of the Tertiary Education Commission. Former Secretary for Justice and General Manager (Policy and Planning) at the Accident Compensation Corporation. Former Victorian Public Sector Commissioner (Australia).</p>
Geoff Dangerfield	<p>Former Chief Executive of the New Zealand Transport Agency and the Ministry of Economic Development. Former Deputy Secretary at the New Zealand Treasury.</p> <p>Current Executive Chair of the New Zealand Festival and Director of Payments NZ. Chair of the Major Outsourced Contracts Advisory Board</p>

	for the Department of Corrections, independent member of the Vulnerable Children’s Board and Director of Wellington Water.
Howard Fancy	Former Chief Executive of the Ministry of Education and the Ministry of Commerce. Former Acting Chief Executive of the Ministry for the Environment. Former Deputy Secretary at the New Zealand Treasury and Executive Director at Motu Economic Research. Current Director of Arts Access Aotearoa and Cognition Education Ltd.
Michael Hundleby	Current Director Critical Projects at the Ministry of Health. Former Acting National Director of the National Health Board. Former General Counsel at the Canterbury District Health Board and Acting Chief Executive of Hutt Valley District Health Board.
Jeremy Lightfoot	Current Deputy Chief Executive of the Department of Corrections. Former Managing Director Parkwood Consulting Services.
Struan Little	Current Deputy Secretary (Budget and Public Services) at the New Zealand Treasury. Former Deputy Commissioner of Inland Revenue. Former Advisor to the Executive Director at the World Bank.
Colin Lynch	Deputy Chief Executive (Sector) at the Ministry of Justice. Former Deputy Government Statistician. Former Deputy Secretary (State Sector Performance Group) and Manager of the Health Section at the New Zealand Treasury.
Karen Poutasi	Chief Executive of the New Zealand Qualifications Authority. Director of Network for Learning. Former Director-General of the Ministry of Health.
Lyn Provost	Current Controller and Auditor-General of New Zealand. Former Deputy Commissioner of Police and former Acting Chief Executive of Archives New Zealand.
Paul Reynolds	Former Chief Executive of the Ministry for the Environment and Deputy Director General at the Ministry of Agriculture and Forestry. Former Chief Policy Adviser at the Ministry of Research Science and Technology. Current Deputy Chair of Landcare Research New Zealand, Director of AgResearch, and Trustee of the Eastland Community Trust.
Mike Scott	Current Assistant Auditor-General (Performance Audit) at the Office of the Auditor-General New Zealand. Former Audit Manager at the National Audit Office (United Kingdom).
Murray Sherwin	Former Chief Executive and Director General of the Ministry of Agriculture and Forestry and Deputy Governor of the Reserve Bank of New Zealand. Former Chair, Canterbury Earthquake Recovery Commission, member of the Board of Executive Directors of the World Bank and Member of the Prime Minister’s Advisory Group.

Audrey Sonerson	Current Deputy Commissioner (Resource Management) at the New Zealand Police. Former Deputy Chief Executive and General Manager of Sector Strategy at the Minister of Justice.
Paul Stocks	Current Deputy Chief Executive (Labour, Science and Enterprise) at the Ministry of Business, Innovation and Employment. Former Deputy Director-General (Policy) at the Ministry of Primary Industries.
Dallas Welch	Current Deputy Commissioner (System & Agency Performance) at the State Services Commission. Former Deputy Government Statistician at Statistics New Zealand, Acting Chief Executive of the Ministry of Women's Affairs.

Appendix 2: Indicative list of interview questions

How state sector leaders think about and conceptualise efficiency

What do you think agencies understand efficiency to be? (Alternative) How do agencies conceive of efficiency?

The relative importance of efficiency as a goal

In your experience, how important is the goal of improving efficiency relative to other goals or priorities? (both within your current organisation and other organisations you have worked in)

What factors influence the relative priority of efficiency?

What would it take to increase the relative importance placed on efficiency within your organisation and within the state sector more generally?

The role of performance management in the state sector

Thinking about the performance measures within your organisation, what performance information is most often “front of mind” for managers?

What is it about this information that makes it important to them?

Once a performance system is in place, does it tend to evolve naturally towards better practice, or are there things senior managers, control agencies or Ministers need to do to ensure ongoing improvement? What are those things?

The challenges to measuring efficiency and using efficiency measures in decision-making

In your view, what are the major challenges to expanding the development of efficiency measures across the state sector?

What would need to happen to overcome or remove these challenges?

Which government organisation (in New Zealand or overseas) are leaders in the area of efficiency measurement?

Have you had experience trying to introduce efficiency measures? Tell me about it?

What would it take to embed efficiency information as a tool that managers use to improve performance?

What areas of the state sector do you think efficiency measures would be most easily applied and helpful? Can you explain why you think this?

How the efficiency and productivity of the state sector can be lifted

What are the major obstacles to improving efficiency in your organisation?

More generally, what are the challenges across the state sector?

What steps could be taken to address these obstacles?