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Reform of the State Sector Act 1988 Discussion Document  
State Services Commission  
P.O Box 329  
WELLINGTON 6140

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Infrastructure New Zealand is the peak industry body for the infrastructure sector and promotes best practice in national infrastructure development through research, advocacy and public and private sector collaboration. Infrastructure New Zealand members come from diverse sectors across New Zealand and include infrastructure service providers, investors and operators.

This submission represents the views of Infrastructure New Zealand as a collective whole and may not necessarily represent the views of individual member organisations.

## Infrastructure New Zealand feedback on the Reform of the State Sector Act 1988 Discussion Document

Infrastructure New Zealand (Infrastructure NZ) commends the State Services Commission (the Commission) on leading the discussion on reform of the public service and development of a clear and succinct discussion document (the Document).<sup>1</sup>

### Overview

We support the review of the State Sector Act 1988 (the Act).

We agree that public services are not being delivered in an integrated and holistic way which prioritises public outcomes and that reform is urgently required to achieve this.

We consider that the proposals set out in the Document will improve the provision of public services.

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<sup>1</sup> State Services Commission, Reform of the State Sector Act 1988: Directions and Options for Change, September 2018.

However, we do not consider that the proposals will address the core state sector problem of weak integration, overemphasis on inputs and a bias towards short term decision making.

As long as departments are funded centrally and charged with delivering a defined portfolio within a defined budget, cross-department integration will be compromised, investment in New Zealand's future will be constrained and public service decisions will be made which prioritise inputs over outcomes.

To meet the objectives of the review, structural changes are required which integrate public services at the point of delivery and reward service providers for strong outcomes-based performance.

The State Services Commission should view this review process as the first stage in a much more substantive review of the delivery of public services.

A more substantive secondary phase of reforms to central and local government bodies will, in our view, be required to address the public service issues set out in the Document

Infrastructure New Zealand seeks the support of the State Services Commission in launching a major constitutional review of domestic governance in New Zealand, including the structures, funding and responsibilities of local and central governing bodies and departments.

### **We support the review of the State Sector Act 1988**

The case for change set out in the Document (Chapter 2) highlights issues with the Act, most notably with respect to:

1. Fragmentation of the public service, otherwise described as the "silo effect";
2. Senior leadership capability; and
3. Political neutrality

We agree that each of these groups of issues is significant, but this submission will focus on what we consider to be the most significant and far reaching of these issues, that of fragmentation.

Organisational efficiency, which has been the hallmark of New Zealand's public service performance in recent decades, has not maximised public outcomes.

Departments structured and funded according to discrete portfolio responsibilities have managed resources responsibly and delivered generally a very high standard of individual public services.

However, like the Commission, we distinguish between a truly high performing public department and a department which simply manages its statutory function at budgeted cost.

Public departments exist for the wider societal outcomes they deliver, not for the sake of themselves.

Under the current system, the state sector has been guilty of sacrificing joined-up thinking and wider public outcomes for the sake of departmental priorities.

In areas requiring multi-faceted collaboration across public services, most notably housing, the lost focus on shared outcomes has been damaging.

The public service has not always operated in the best interests of the public and changes to statute may lead to better national performance.

### **The public service prioritises the short term over the long term**

We wish to add that the focus on organisational efficiency has not only come at the cost of joined up public services, but also long term thinking.

In the infrastructure sector, capital investment decisions are required which carry intergenerational repercussions.

Such investment decisions should in principle be made on the basis of long term net public outcomes.

There will always be challenges understanding the wider economic, social and environmental value of an asset over its life and whether this is greater than the financial cost to build, fund, operate and maintain the asset over that time.

Nevertheless, the principle remains that if the asset is reasonably expected to deliver more value than the aggregate of these costs, it should be delivered.

Clearly, this has not occurred.

Whether the issue is congestion in our cities, an under supply of housing, hospitals in urgent need of repair, students in temporary classrooms or over crowded prisons, we are unaware of anyone who believes New Zealand's long term investment decision making has kept pace with the value society places on infrastructure services.

Evidence is not just anecdotal, but is reflected in every available study and independent piece of research on New Zealand's political economy. New Zealand always features at or near the top of global indices of public service efficiency, transparency and performance, and is equally always ranked much lower on infrastructure service provision.<sup>2</sup>

New Zealand has systematically underinvested in public infrastructure since the Act was passed in 1988. This is not exclusively the result of the State Sector Act 1988, but it is clear that the Act has been unable to prevent the deterioration of New Zealand's capital stock in recent decades.

### **We support the changes set out in the Document**

We agree that the principal challenge under the current state sector system is that public bodies do not collaborate, coordinate and integrate their activities to deliver a holistic "public service" based on the long term value of public activities.

Departments operate in siloes, not as a cohesive whole. Priority is given to organisational objectives, not public outcomes. Capital spending decisions are made independently, not as part of a coordinated public investment programme.

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<sup>2</sup> See, for example, World Economic Forum, Global Competitiveness Report, 2017.

This must change if we are to rise to the challenge posed by complex 21<sup>st</sup> century challenges, including:

- Urban growth and housing
- Climate change
- Resilience
- Environmental sustainability
- Intergenerational and cross-cultural equity

We agree that reforming the Act is critical to achieving this and we support the proposals set out in the Document, including:

- the revised purpose, principles and values set out in Chapter 3;
- initiatives to better engage and meet the needs of Maori;
- wider efforts to support diversity and make the public sector more inclusive and representative of the people it serves;
- changes to organisational arrangements, including more options for departments to organise in ways that improve the outcomes and services for New Zealanders, Public Service Executive Boards, joint ventures, executive agencies and statutory officers;
- initiatives to strengthen leadership in the public service; and
- efforts to improve the capability of the public service to serve successive governments, including requirements for long term insights and investment needs.

### **We do not believe the identified reforms will be sufficient**

However, we do not consider that these reforms will address the problem which has precipitated the review.

That is, we consider that, even if all proposed changes in the Document take effect, the state sector will continue to operate in silos, prioritising inputs over outcomes and managing budgets to achieve short term objectives.

There are two principal reasons why:

1. The structures of funding and decision making will remain the same.
2. The reforms only affect part of the public sector.

### **Funding and decision making structures**

The two underlying causes which have led public bodies to operate in silos and prioritise internal fiscal management above holistic public services are:

1. Public services are organised as “vertically integrated” portfolio structures, reducing the need for organisations to cooperate to deliver on core departmental objectives.
2. Funding is rationed through the Vote process and allocated to portfolios, providing a compelling incentive to focus on organisational cost minimisation.

In both cases, the effect is to frame the “world view” of the respective organisation not in terms of public outcomes but in terms of a defined and prescribed service.

Except at the Cabinet level, where on-balance judgements can be made on the largest initiatives, there is limited scope for public service decisions to be made holistically.

Even with new direction to require collaboration included in a new Act, departmental priorities will continue to be driven by the source of funding and internal priorities will supersede agreed outcomes.

This is, we observe, exactly what happened in Auckland under the pre-2010 governance arrangements. Statute required the region’s eight councils to negotiate and agree regional objectives and priorities. Despite signed agreement, these plans were never implemented and the region failed to respond to growth. The reason for this was that when delivery agencies (city and district councils) who agreed plans at a strategic level had to make difficult allocative decisions with their communities, the priorities of local voters and ratepayers carried greater weight than regional commitments. City and district councils, in short, could not act in the wider regional interest because it was not in their (short term) local interest. The structures of governance prevented integration, alignment and coordinated planning and delivery.

We are less familiar with the example cited in the Document with the Senior Executive Service, but its failure appears to exemplify the challenge of prescribing integration and cooperation without putting in place the fundamentals which incentivise and enable it.

To overcome the issues which gave rise to the review of the Act, the Commission should look not only at the principles, purpose and direction given to the public service, it should look at the underlying structures which incentivise and shape how departments act.

Such changes will require reform to legislation beyond the State Sector Act 1988, but it is important that the Commission leads this discussion now to avoid years of delay as authorities observe the impact of incremental changes.

### **There is a bigger problem: local government**

The proposals set out in the Document are not only too minor in terms of the degree of change proposed, they are mooted for a too narrow section of the public sector.

By leaving critical public sector bodies out of the scope of the reform, the Commission risks entrenching for another generation different objectives and guidelines for public agencies who otherwise work together to achieve common outcomes.

The most notable of these public sector bodies are New Zealand’s 78 local authorities.

Just as an average citizen does not distinguish between different arms of central government, in many cases that same citizen does not distinguish between a public service provided by a council and one provided by a ministry.

Local government is as much the public service as any Government department.

Moreover, Government departments depend upon the collaboration and cooperation of local authorities to deliver core services in their communities.

In the infrastructure sector, the relationship of public departments and local authorities is integral to the delivery of every single public service. Whether by operating the roads and water which service hospitals and schools, consenting the state highways, zoning state housing or collaborating on events, economic development and social issues, local government is an essential partner of the public service on every Crown capital investment activity.

Further complicating the delineation of the “public service”, as defined in the Document, and local government is the fact that local government is not a constitutional entity, as in some other countries; it is an extension of the Government.

As a product of legislation (just like public departments), local government can be, and is, established and disestablished according to Government policy.

The Commission will be aware, therefore, that exactly the same issues affect local government services as affect the public service, as outlined in the Document.

That is, councils focus on inputs above outputs, integration with Government and private sector is wanting and decision making has become fragmented.

Indeed, these challenges are significantly more advanced at the local government level where funding is tighter and capability more limited.

New Zealand has 78 spatial silos focused on transport, water, community facilities and planning which are not functioning well with other parts of the system, resulting in severely reduced public outcomes.

The “frontline” of this failure is the housing crisis. Under-resourced, capacity constrained councils have sought to manage increasing cost pressures by underfunding growth infrastructure, leading to an undersupply of developable land and, in turn, house price inflation.<sup>3</sup>

The result has been severe housing unaffordability.

In the case of Auckland, for example, the price of an “average” home has moved from around \$500,000 to around \$1 million in recent years.

Yet even the highest estimates of council infrastructure cost per dwelling do not exceed \$150,000, suggesting that the Auckland Council’s efforts to save \$1 may have cost residents wanting to buy a home \$3, before social impacts are considered.

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<sup>3</sup> Productivity Commission, Report into Housing Affordability, 2012.

It is notable that this rise in land costs and housing unaffordability has occurred while the Auckland Council has successfully and effectively managed its fiscal accounts, retaining a “strong Aa2” credit rating from Moody’s.<sup>4</sup>

The protracted failure for not only successive Auckland councils but local authorities across New Zealand to recognise the wider value of their services to New Zealand and respond accordingly makes reforming the local government sector even more urgent than reforming Government departments.

In fact, surveys conducted by Local Government New Zealand (LGNZ)<sup>5</sup> suggest that much of the public has now lost confidence in councils to act in the public interest.

It is our strong view that the Commission’s work to better align the objectives of the public service with the objectives of the public is urgently required across both central and local government.

If local government does not operate under the same broad principles and with the same general purpose and objectives of public departments, for their respective communities, the delivery of essential public services will not be joined up and outcomes will be compromised.

We strongly encourage the Commission to investigate how the reach of the reforms set out in the Document can be expanded to include local government.

### **Achieving public outcomes**

In order to deliver on the objectives of the review, as set out in the Document, the Commission needs to go much further.

It needs to set out a process for addressing the underlying causes of the silo effect and it needs to do so across the entire public service, including both central and local government.

Addressing the underlying causes means amending not only the written prescriptions for what departments “should” do but reforming the structures which determine “why” they do it.

If the objective of public services is to deliver good outcomes over the long term, then a structure is required which combines the funding of different public services, the performance objectives of public departments and lines of accountability for outcome achievement.

Changes must, however, result in improvements which do not compromise the efficiency benefits which have been gained from a strict focus on performance and departmental services.

The tension between focusing on holistic and often difficult to measure outcomes versus defined, yet limited, departmental services is one which we think needs significant consideration in the design of a reformed public sector.

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<sup>4</sup> <http://ourauckland.aucklandcouncil.govt.nz/articles/news/2018/10/moody-s-and-sp-reaffirm-auckland-council-credit-ratings/>

<sup>5</sup> In its latest public survey, LGNZ found that the reputation of local government was rated just a 3 out of 10, see LGNZ, New Zealand Local Government Survey 2017.

Drawing on our experience of overseas infrastructural systems, we observe that this balance is normally promoted (to varying degrees of success) via a greater dependency on local government.

Under such an approach, “place” becomes the mechanism to align and integrate the array of public services and local government bodies the “owners” of local public outcomes.

### **Shifting to an outcomes-focused public service**

Public services, whether healthcare, education, transport, welfare, economic development or law enforcement overwhelmingly take effect in an identifiable location.

There may be consistency of issues across the country, but the actual implementation of policy and delivery of services takes effect locally.

This is most obvious in the infrastructure sector, where infrastructure is, by definition “fixed” to a location and its impacts – both good and bad – spatial.

But it is equally notable in non-infrastructure public services including, for example, addressing domestic violence; domestic violence may be an issue nationwide, but the response can only take effect at the local, in this case household, level.

A “place-based” approach to public services offers the opportunity to put the outcomes of a defined spatial area first, and then coordinate the range of public services to achieve those outcomes.

This can be contrasted with the current “portfolio-based” approach to public services, which seeks instead to provide a high and consistent level of service across each portfolio (for example, health, education, etc) across the country.

Both approaches are not without their weaknesses.

Under a place-based approach oriented around local outcomes, there is a risk that levels of service will become inconsistent, and in some cases weak, across parts of the country.

Under a portfolio approach oriented around strong public services there is the risk, now realised in New Zealand, that outcomes will be subordinate to a defined service.

The ultimate objective of the reform process should be to achieve the optimum balance of the two approaches so that both services and outcomes are promoted.

### **A public sector which balances outcomes and services**

We have not finalised our views on an ideal framework.

However, with major reviews of water, local government funding and resource management all underway, we emphasise the current opportunity to take a wider look at the entire system.

We will be developing our thinking over coming months, but think that the Commission occupies a unique position within New Zealand’s governing framework and could lead this discussion.

We would like to see, for example, an investigation into a greater role for place-based decision making to promote public outcomes.

This could include increased funding for local government.

Higher funding at the local level would necessitate lesser resources at the national level, with central agencies potentially taking on a stronger regulatory and oversight role.

Alternatively, central agencies could retain funding powers and local areas, potentially regions, could compete for resources on the basis of compelling business cases.

Not only these, but even much more fundamental questions of governance need now, in our view, to be posed and discussed:

- Is local government doing what local government should do?
- Is central government doing what a central government is best placed to do?
- Are there public services which are neither “local” nor “national” which are underserved by the existing two-level system?

We would like to see the Commission, as the only body with the expertise and independence to robustly consider these questions, expand its review to incorporate “macro” governance issues.

### **Resource Reform New Zealand and wider public sector reform**

In 2017, Infrastructure New Zealand, along with industry partners the Employers and Manufacturers Association, Environmental Defence Society, Property Council of New Zealand and Business NZ formed a coalition *Resource Reform New Zealand (RRNZ)* calling for a first principles review of the Resource Management Act 1991, Local Government Act 2002 and Land Transport Management Act 2003.

The group has invested significant time and resource into understanding governance issues at the local level and think there would be value in engaging with the Commission on related issues at central government level.

Only by integrating and aligning public service decisions across the whole public sector can New Zealand tackle the most challenging issues confronting the country and communities today.

We thank the Commission for this opportunity to submit.