

Chair
Cabinet Committee on State Sector Reform and Expenditure Control

AMENDED DIRECTIONS TO EXTEND FUNCTIONAL LEADERSHIP TO CROWN ENTITIES, FOLLOWING CONSULTATION

Proposal

1. This paper provides revised directions to extend Procurement, ICT and Property functional leadership requirements to Crown entities, taking account of consultation with the affected entities. It recommends that Cabinet endorse the text and scope of these directions, and note that the Ministers of State Services and Finance intend to issue them.

Executive summary

2. This paper reports back to Cabinet on the outcome of consultation with relevant agencies on three directions, under section 107 of the Crown Entities Act 2004, to extend Procurement, ICT and Property functional leadership requirements to specified Crown entities [CAB Min (13) 43/3 refers]. These directions are intended to improve public services, secure economies and efficiencies, and develop expertise and capability (among other purposes).
3. The main themes from the consultation process were:
 - widespread support for the intent of the directions
 - concerns about impacts of the directions on board decision rights and authority, with a few entities raising questions about the overall legal framework for the directions
 - need for greater clarity on the requirements in the directions, on their application, and on how the requirements may be varied
 - need for clear disputes resolution and escalation processes
 - concerns about additional costs for entities compared with benefits
 - need for adequate timeframes for introduction, and capability for implementation, and
 - some questioning of coverage (many entities are already complying on a voluntary basis, and some would prefer this to continue).

4. The consultation process has highlighted some areas for legislative tidying up, which could be progressed as the opportunity arises. —

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Changes to the text of the directions will improve certainty for entities in terms of what they are required to do and, in certain areas, reduce the level of discretionary power conferred on functional leaders.

5. We want to draw ministers' attention to the fact that extending the mandate of functional leaders to Crown entities does affect the duties, responsibilities and operating model of a Crown entity board and its responsible Minister. Paragraphs 17-20 elaborate on this aspect. Before the directions come into force, officials will engage directly with entities that raised concerns about the legal framework for the directions and the impact on an entity's responsibilities. The processes of up-front engagement as well as on-going engagement on implementation details, together with options for escalation and dispute resolution should suffice to resolve particular issues.
6. In line with the consultation feedback, the directions have been modified to improve clarity and reduce areas of uncertainty and, where applicable, include an explanation of how changes to existing requirements may be made. The paper proposes that any disputes about how the directions are applied should be resolved between the entity and the functional leader wherever possible, with assistance from the Head of State Services, but may be escalated to responsible Ministers and then to the Ministers of State Services and Finance should the area of dispute remain unresolved. Explanatory material on the directions will be published on the State Services Commission's (SSC)'s website, after they have come into force.
7. The information provided by functional leaders on costs and benefits for entities and the system indicate that a decision to extend functional leadership requirements to Crown entities will be fiscally positive overall. There will be transitional costs for some entities, depending on the extent of their current alignment with the requirements specified in the directions.
8. Responding to particular concerns about implementation timeframes and capability, we propose that the Procurement direction should not take effect until 1 February 2015. This allows time for entities to adjust their internal processes, and for the Procurement Functional Leader to develop further tools and processes for implementation support and make minor adjustments to the Rules for clarification. Most of the ICT direction would take effect on its coming into force under section 109 of the Crown Entities Act. However, officials recommend that the ICT assurance requirements in respect of District Health Boards (DHBs) be staged to take effect from 1 July 2015. This is to ensure that sufficient ICT assurance capability and capacity can be developed within the GCIO, and to deal with the more complicated nature of health sector ICT governance and decision-making. The Property direction would take effect from 1 July 2014, as originally intended.
9. We are proposing that the NZ Blood Service be removed from the scope of the Property direction because, as in the case of DHBs, all office space is going to be within operational sites. Appendix 1 sets out the coverage of the amended directions.

10. We recommend that you endorse the revised directions, and note that we intend to issue them and direct the Head of State Services to notify the affected entities as soon as possible on our behalf. We will also present the directions and explanatory material to the House of Representatives, for referral to the Finance and Expenditure Committee (FEC). The next steps are:
 - FEC reports back to the House (12 sitting days after referral).
 - The directions come into force (15 sitting days after referral) unless the House resolves to disapply one or more of them. The date for a direction to take effect can be specified as part of the direction.
 - The directions are published in the Gazette and on the Internet (SSC's website) as soon as practicable.

Background

11. On 9 December 2013, Cabinet noted that benefits would be achieved from extending Procurement, ICT and Property functional leadership requirements to specified Crown entities and directed the Head of State Services to put in place a process for coordinated consultation on directions under section 107 of the Crown Entities Act 2004 (the Act). Cabinet invited the Ministers of State Services and Finance to report back to SEC by 31 March 2014 on the outcome of consultation on the three directions [CAB Min (13) 43/3].
12. A direction to support a whole of government approach under section 107 of the Act can be used where the government has decided on a multi-agency approach for some activity, and there are benefits from applying this to some or all Crown entities (except Crown entity subsidiaries and Tertiary Education Institutions) and/or to companies listed in Schedule 4A of the Public Finance Act 1989 (which are treated as Crown entities for this purpose). Crown entities must give effect to a section 107 direction as soon as it comes into force (or where the directions itself specified a later date), except that Crown Research Institutes only have to have regard for these directions.
13. The Ministers of State Services and Finance may jointly direct Crown entities to support a whole of government approach by complying with specified requirements for purposes set out in the Act. These purposes include improving public services, securing economies or efficiencies, and developing expertise and capability (among others). The process to be followed in issuing a direction is specified in the Act, and outlined in Cabinet Office circular CO (13) 4.
14. All of the entities covered by the directions were invited to participate in the consultation process. About 80 entities engaged in consultation on one or more of the directions (as applicable) through combined briefing sessions, individual meetings and/or phone calls. Written submissions were received from 37 entities. Oral feedback has also been taken into account in responding to the consultation feedback.

Analysis of consultation feedback

15. The main themes from the consultation process were:

- widespread support for the intent of the directions
 - concerns about impacts of the directions on board decision rights and authority, with a few entities raising questions about the overall legal framework for the directions (paragraphs 17-28)
 - need for greater clarity on the requirements in the directions, on their application, and on how the requirements may be varied (paragraphs 29-31)
 - need for clear disputes resolution and escalation processes (paragraph 32)
 - concerns about additional costs for entities compared with benefits (paragraphs 33-36)
 - need for adequate timeframes for introduction, and capability for implementation (paragraphs 37-43), and
 - some questioning of coverage – many entities are already complying on a voluntary basis, and some would prefer this to continue (paragraph 44).
16. Officials' advice and our recommendations for responding to the feedback are provided below.

Impact on board decision rights and authority

17. We want to draw ministers' attention to the fact that extending the mandate of functional leaders to Crown entities does affect the duties, responsibilities and operating model of a Crown entity board and its responsible Minister.
18. While the Crown Entities Act 2004 (the Act) stipulates that all decisions relating to the operation of a statutory entity or Crown entity company must be made by or under the authority of the board, the board will not have full authority for certain decisions or actions imposed by a functional leader. If the directions are applied to Crown entities, then a functional leader could effectively prevent an action that the board would otherwise authorise (eg, to enter a contract¹) or cause the board to take an action that it would otherwise not undertake (eg, to purchase specified software for common ICT capability purposes, or provide procurement planning documents to the Ministry of Business, Innovation, and Employment (MBIE) for review).
19. While the entity would be accountable for *how* it complies, it would not have full control over particular decisions and issues. Responsibility for *what* decisions and actions are imposed would rest with the functional leader. Consistent with established practices concerning limits on ministerial involvement in operational and internal governance matters, different ministers would be answerable in the House for different aspects of functional leadership where required, as depicted in the following table.

¹ For clarity, purchasing from all-of-government contracts is mandated by Cabinet, rather than the Procurement Functional Leader, at the time that approval is sought for the proposed contract.

Minister of State Services and Minister of Finance	Minister responsible for Crown entity	Minister responsible for functional leader
Answerable to the House for functional leaders' overall mandate as it applies to Crown entities	Answerable to the House for Board's performance in complying with specified requirements	Answerable to the House for functional leader's performance
SSC and Treasury	Entity Board	Functional leader
Responsible for quality of advice on overall mandate for functional leadership as it applies to Crown entities	Responsible for performance of entity in complying with specified requirements	Responsible for quality of advice on content of specified requirements and scope of application. Responsible for leading the application of the specified requirements to entities as appropriate

20. There is a provision in the Act that will help to clarify the scope of an entity's activities affected by any requirements imposed by a functional leader. Section 151 requires an entity's annual report to include information on "any new direction given to the entity by a minister in writing under any enactment during that financial year, as well as other such directions that remain current". A full account of the activities affected by a requirement will assist ministers, the Office of the Auditor-General and Parliament to understand where responsibilities lie for particular activities of the entity.

Legal framework for the directions

21. Some submissions queried how the directions fit within the overall legal framework provided for in the Crown Entities Act 2004 (the Act). Specifically:
- whether the extent of discretion granted to others was permissible (eg, requiring entities to seek approval from other officers for various things)
 - whether some specific directions may breach the statutory restriction in s113(1)(a) of the Act prohibiting directions in relation to a statutorily independent function, and
 - whether some specific directions may breach the statutory restriction in s113(1)(b) of the Act prohibiting directions "requiring the performance or non-performance of a particular act, or the bringing about of a particular result, in respect of a particular person or persons".

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Need for greater clarity on the requirements in the directions, and on processes for variation

Clarity of directions

29. Our view is that, in line with consultation feedback, the requirements imposed on entities by the directions should be clearly specified at the date the directions are issued. Respondents wanted to understand how changes could be made to requirements, for example how new common capabilities could be made mandatory.

Process for removing requirements

30. Directions under s107 cannot be issued to only 1 or 2 Crown entities (nor disappplied in the case of only 1 or 2 entities). However, if a group of 3 or more entities is no longer required to apply a particular requirement after we have issued the directions, then the process to disapply the requirements will have to go through a further section 107 direction process (effectively, to issue a new or amended direction to the entities in question). This does not preclude an administrative agreement between a functional leader and an entity about how a particular requirement might apply.
31. There were numerous other requests and suggestions for clarification of the wording of the requirements under the directions. The amended text for the directions is provided in paragraph 45 below.

Dispute resolution and escalation process

32. We expect any concerns about the application of functional leadership requirements to be resolved at the lowest decision-making level possible. The functional leader and entity chief executive and/or board have joint responsibility for resolving such concerns wherever possible by consensus or other mutually agreed process. Our expectation is that this process of engagement should suffice in almost every case. The parties may call on the Head of State Services to help resolve concerns before any escalation to ministers. However, if that

does not resolve matters, then our view is that the remaining area of dispute should be escalated first to the responsible Ministers for the entity and functional lead area, and ultimately to joint Ministers.

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Costs for agencies

33. Many entities commented that whole of government arrangements (particularly procurement) have already offered significant opportunities for entities to benefit from economies of scale and standardised approaches. Six mainly small entities expressed concern in their submissions that the directions would pose additional costs, including transaction costs in terms of new processes and capability requirements for compliance, which they may find difficult to meet given small budgets. Some of these entities were also concerned that the Procurement requirements were tailored for large organisations, and would impose an additional burden or be insufficiently tailored to the requirements of small entities. There may also be increased costs to the Treasury (eg, the Portfolio Performance Management function) from the increased scope for ICT and other areas of functional leadership resulting from the directions.
34. Some of the DHBs, in particular, expressed concern about the potential for duplication of processes (eg, around investment approvals and assurance for major ICT projects, and around the existing activities of Health Benefits Ltd and healthAlliance). The DHBs and a small number of other entities also expressed some concern about potential adverse impacts on operations, stating the need for adequate lead-in times and signalling of any changes to arrangements.
35. Functional leaders are already addressing many of these concerns, for example through streamlining processes, developing implementation tools, ensuring alignment with other initiatives to avoid duplication, or ensuring that entities understand that the Procurement Functional Leader can approve an exemption from purchasing from an all-of-government contract where the entity can demonstrate there is good reason not to.
36. The long-term sustainable funding model to support ICT functional leadership is still being developed. As previously advised [SEC Min (14) 3/4], the Department of Internal Affairs and central agencies expect to complete design work on funding mechanisms for ICT all-of-government initiatives by August 2014. The concerns expressed by the small Crown entities in particular, for example about the user-pays model, will be factored into that work.

Implementation timeframes and capability

37. In response to feedback on the directions, including concerns about capability requirements, we have made some adjustments to the timing for implementation.

Implementation timeframes and capability - Procurement

38. In the case of Procurement, we propose that agencies have until 1 February 2015 to bring the Government Rules of Sourcing into operation. This would ensure a successful implementation of the Rules by allowing entities sufficient time to undertake their change management processes, including internal communications and staff training, and updating internal policies and procedures. In addition, it would enable wording clarifications to be made to the Rules, and

implementation support tools to be developed. DHBs also sought reassurance that a direction to comply with the Government Rules of Sourcing did not increase the risk of litigation by unsuccessful suppliers, which MBIE officials will work through with them. The Procurement Functional Leader's intention is to support the entities to achieve better procurement outcomes through applying good procurement practice, not to hold up their processes.

Implementation timeframes and capability – ICT

39. The GCIO is in the process of building capability for the ICT functional leadership role, and expects the direction will significantly increase the scope of its operations, especially in the system-wide ICT assurance area.
40. The impact on the GCIO's operations of implementing the direction in respect of ICT common capabilities is not expected to be substantive, as the GCIO already works with agencies outside the core Public Service. A number of Crown entities already uptake common capabilities, and the revised direction specifies that timeframes for implementing ICT common capabilities will, if relevant, be negotiated with the GCIO, which also allows the impact to be managed over time.
41. The impact of implementing the direction in respect of ICT assurance will be greater as this function is still in its start up phase, with the role introduced in June 2013, and workload is more directly impacted by numbers of agencies covered. To respond to concerns in the feedback about capability to deliver on the ICT assurance function, and to ensure the GCIO has the capacity to deal with the substantial increase in scope, we propose the implementation of this part of the direction in respect of DHBs will take effect from 1 July 2015.
42. Officials have advised that staged implementation for DHBs is required to ensure that sufficient ICT assurance capability and capacity can be developed within the GCIO, and to deal with the more complicated nature of health sector ICT governance and decision-making. The National Health IT Board currently provides some assurance and monitoring functions across ICT in the health sector. Ministers can also request that particular high risk projects are part of Gateway and Major Projects Monitoring regimes if they have specific concerns.

Implementation timeframes and capability - Property

43. The Property Functional Leader has already been engaging with most Crown agents on a voluntary basis, so the direction does not represent a large shift in capability in their case. As set out in the direction for consultation, we are recommending that the Property direction be implemented from 1 July 2014.

Coverage

44. The coverage for each direction was carefully considered, as explained in the submissions to Cabinet in December 2013 (see suite of papers at www.ssc.govt.nz/whole-of-govt-directions-dec2013). In general, nothing in the consultation process suggested that the coverage should be changed apart from removing one Crown agent from the scope of the Property direction (the NZ Blood Service, as explained in paragraph 46 below). In addition, the NZTA's statutorily independent function under Part 2 of the Land Transport Management Act 2003 to approve procurement procedures cannot legally be subject to the

procurement direction. NZTA's processes already largely align with the Government Rules of Sourcing, and MBIE will continue to work with NZTA on increasing alignment. The balance of NZTA's procurement activities, however, will be subject to the direction.

Proposed directions

45. Taking account of the consultation feedback we propose revised wording for the three directions, as set out below.

Procurement direction
<p><i>The Minister of State Services and the Minister of Finance, pursuant to section 107 and subject to the provisions of section 113 of the Crown Entities Act 2004, direct all entities subject to a direction as a group under section 107 (2) and section 107 (2A) of the Act, except School Boards of Trustees, as follows:</i></p> <p><i>In order to complement Procurement Functional Leadership in supporting a whole of government approach to procurement policy and practice, and in order to secure economies and efficiencies and develop procurement expertise and capacity, all entities subject to a direction under section 107 (2) and section 107 (2A) of the Crown Entities Act 2004, except School Boards of Trustees, are directed to apply the Government Rules of Sourcing (as amended and published from time to time with approval by Ministers), with effect from 1 February 2015.</i></p> <p><i>The entities are further directed to be guided by the Ministry of Business, Innovation and Employment, as Procurement Functional Leader, in any issues arising in the application of the Rules.</i></p>

ICT direction
<p><i>1. The Minister of State Services and the Minister of Finance, pursuant to section 107 of the Crown Entities Act 2004, direct the entities as follows:</i></p> <p><i>(1) in relation to the Government Chief Information Officer's (GCIO) mandate for functional leadership of government ICT:</i></p> <p><i>(a) entities must secure the agreement of the GCIO to strategic ICT plans and ICT investment intentions before finalising or implementing them;</i></p> <p><i>(b) entities must:</i></p> <p><i>(i) when they have a need for goods or services available through the relevant capabilities; and</i></p> <p><i>(ii) either do not have current contracts for such goods or services or have such contracts that expire or can be terminated without penalty (for example at the end of a current contract term),</i></p> <p><i>adopt, where relevant within timeframes negotiated with the GCIO:</i></p>

ICT direction

- (iii) *the mandatory ICT common capabilities; and*
- (iv) *any new ICT common capabilities contemplated by the Government ICT Strategy and Action Plan to 2017 that the GCIO and Head of State Services specify jointly are mandatory for departments (pursuant to the power of specification to this effect conferred on them by Cabinet (CAB Min (12) 35/4C refers)) (the effect of this clause 1(1)(b)(iv) is that a joint specification by the GCIO and Head of State Services to departments applies automatically, under this direction, to entities);*

(c) *if an entity wishes to be exempt from the requirement to adopt:*

- (i) *a mandatory ICT common capability; or*
- (ii) *any new mandated ICT common capability,*

the entity must secure the agreement of the GCIO or, failing that, the Head of State Services or, failing that, the Minister of State Services and the Minister of Finance;

(2) *in relation to the GCIO's ICT assurance function, the entities must:*

- (a) *if the GCIO requests, provide any information to the GCIO for the purpose of ICT assurance; and*
- (b) *if issues of concern are raised about ICT assurance, work directly with the GCIO on those issues,*

except to the extent that any requirement in this clause 1 would be inconsistent with section 113 of the Crown Entities Act 2004 and provided that District Health Boards shall not be required to comply with clause 1(2) of this direction before 1 July 2015.

2. For Crown agents that are entities, this direction supersedes and replaces the whole of government direction regarding all-of-government shared authentication services dated 21 July 2008 (18 September 2008) 141 New Zealand Gazette 3844. To avoid doubt, that earlier direction continues to apply to Crown agents that are not entities.

3. For the purposes of this direction:

- (1) *"entities" means the Crown entities that are the subject of this direction, being the Accident Compensation Corporation, District Health Boards, the Earthquake Commission, the Housing New Zealand Corporation, the New Zealand Qualifications Authority, the New Zealand Transport Agency, New Zealand Trade and Enterprise, and the Tertiary Education Commission;*
- (2) *"Government ICT Strategy and Action Plan to 2017" means the document by that name (as may be updated from time to time) available at www.ict.govt.nz;*
- (3) *"ICT" includes information management, technology infrastructure, and technology-enabled business processes and services; and*
- (4) *"mandatory ICT common capabilities" means the ICT common capabilities that Cabinet has directed departments to adopt, being one.govt, Infrastructure-as-a-Service, and the login and identity verification services of RealMe (formerly igovt) (SEC Min (12) 10/2) and the security and privacy panel (SEC Min (13) 2/6)."*

Property direction

The Minister of State Services and the Minister of Finance, pursuant to section 107 of the Crown Entities Act 2004, direct all Crown agents², except District Health Boards and the New Zealand Blood Service, to comply with the mandate of the Functional Leader for Property, or their delegated agent³, as it:

- (a) includes office and public interface areas⁴, but*
- (b) excludes operational areas, and areas under the direct control of a Crown agent's investment function and not occupied by the Crown agent itself.*

This direction takes effect on 1 July 2014 as follows:

- (1) Crown agents will cooperate with the Property Management Centre of Expertise (PMCoE), as agent of the Functional Leader for Property, as it consults to develop or update property strategies, principles, standards, tools and processes that will prescribe how Crown agents will develop and manage their individual property strategies. In developing or updating these instruments, the PMCoE must give effect to the national property strategy (including principles) and standards, as approved by Ministers.*
- (2) Crown agents must obtain the approval of the Functional Leader for Property or their delegated agent before entering into contracts for acquisition or disposal (in part or full) of leased or owned office accommodation or public interface accommodation. When deciding whether to give an approval, the Functional Leader for Property or their delegated agent must have regard to the Crown agent's operational requirements as detailed in the Crown agent's Strategic Property Plan, and must base the decision on the instruments developed in paragraph 1 above.*
- (3) Crown agents are required to comply with standards, tools and processes that have been developed and updated by the Functional Leader for Property or their delegated agent, where these have been approved by the relevant authority for each standard, tool or process.*
- (4) Crown agents are responsible for developing agency strategic property plans every two years that align with strategies, principles and standards developed by the Functional Leader for Property, for approval by the PMCoE.*
- (5) Crown agents must, at the soonest practicable opportunity, implement an average workplace density of 12-16 sqm per full-time equivalent. Examples of the soonest practicable opportunity are when Crown agents are relocating offices, developing or changing office fit-outs, or where lease terms allow.*
- (6) Crown agents will adopt and use the integrated workplace management system (IWMS) approved by the Functional Leader for Property or their delegated agent⁵, to populate and maintain property data as required by the Functional Leader for Property or their delegated agent.*

² As defined in Part 1 of Schedule 1 of the Crown Entities Act 2004.

³ Currently the Chief Executive of the Ministry of Social Development, and the Government Property Management Centre of Expertise, respectively.

⁴ Office and Public Interface areas defined in the Government National Property Strategy.

⁵ Currently "Archibus", also known as Government Property Portal or GPP.

Property direction

- (7) Crown agents must use common capability contracts⁶ for property-related goods and services established by the Functional Leader for Property or their delegated agent, as existing contractual commitments allow.
- (8) Crown agents must contribute to any PMCoE cost-recovery model approved by Ministers, which may be updated from time to time in accordance to changes in actual operating costs.
- (9) Crown agents may agree with the PMCoE to transfer property management functions, including the operation and use of the IWMS, to the PMCoE (or their outsourced providers) on a cost-recovery basis.

Nothing in this direction applies to the extent that any requirement would be inconsistent with section 113 of the Crown Entities Act 2004.

46. The main changes from the directions proposed for consultation are as follows:

Changes – Procurement direction

- The date for the direction to take effect is specified as 1 February 2015 (to allow time for entities to adjust their internal processes, and the Functional Leader to make minor adjustments to the Rules for clarification).
- Clarification that ministers approve amendments to the Rules.
- Removal of a requirement for entities to co-operate fully with the Functional Leader in any monitoring of compliance in order to be clear that the aim is to focus on good procurement practice, not to increase risk to entities or to focus on compliance.

Changes – ICT direction

- Most of the ICT direction will come into effect when the direction comes into force under section 109 of the Crown Entities Act. The application of the ICT assurance function in relation to District Health Boards will take effect from 1 July 2015.
- States that the timing for adopting common capabilities is, where relevant, subject to negotiation with the GCIO. This responds to concerns in the feedback about how and when implementation would be required.
- Clarifies that any new mandatory ICT common capabilities will need to be contemplated by the *Government ICT Strategy and Action Plan to 2017*, decisions to mandate them by the GCIO and Head of State Services in relation to departments (pursuant to the power conferred on them by Cabinet, CAB Min (12) 34/4C refers) will apply automatically to the relevant Crown entities under the direction (thereby removing any separate exercise of discretion), and decisions on exemptions will ultimately, where required, be escalated to ministers.

⁶ Previously, and sometimes also, referred to as “all-of-government contracts”.

Changes – Property direction

- Changes were largely to clarify the requirements and make them unambiguous. The majority of feedback on this direction indicated a degree of uncertainty on the intent.
- Clarification that the Functional Leader will have regard to the Crown agent's operational requirements in their property plan when approving it.
- Making it clear that operational areas and areas under the direct control of a Crown agent's investment function (e.g. investment property held by the Accident Compensation Corporation but not occupied by the Corporation) are excluded.
- The NZ Blood Service is now excluded from the direction on the same basis as for DHBs (all office space is going to be within operational sites).
- An explicit requirement that Crown agents must implement the average workplace density of 12-16 square metres at the soonest practicable opportunity (instead of a cross-reference to a Cabinet minute with this requirement).
- Reworded a requirement to state that Crown agents will adopt and use the integrated workplace management system approved by the Functional Leader (rather than calling it by name "Archibus" because the provider could conceivably change).

Risk in relation to element of ICT direction

Withheld under section 9(2)(g)(i) of the Official Information Act

Consultation

50. This paper was prepared by the SSC and the Treasury. The Ministry of Business, Innovation, and Employment, the Department of Internal Affairs, and the Ministry of Social Development's Property Management Centre of Expertise were also involved in its development. Nine other departments that monitor Crown entities affected by the directions were informed of the paper (Culture and Heritage, Education, Environment, Foreign Affairs and Trade, Health, Justice, Maori Development, Primary Industries, Transport). All Crown entities affected by the proposed directions were consulted, and a summary of their views has been reflected in this paper. The Department of the Prime Minister and Cabinet was informed.

Financial Implications

51. The information by entities and functional leaders on costs and savings suggests that a decision to extend functional leadership requirements to Crown entities will be fiscally positive over time, but that some entities may face additional costs especially in the short term through the transition period (see paragraphs 33-36, and Appendix 2). The benefits from including more entities go beyond cost savings and include things such as standardisation to support citizen-centred service design across agencies, and alignment of investment to enable common capabilities to be developed faster, for example.

Human Rights, Gender implications, Disability perspective

52. There are no human rights, gender or disability implications associated with this paper.

Legislative implications

53. This consultation process has highlighted some areas for legislative tidying up, which could be progressed in the longer term, as the opportunity arises. These could include:
- A review of statutorily independent functions conferred on statutory entities, given the expanded purposes for issuing directions to support a whole of government approach. Potentially, some functions that currently have statutory 'immunity' from a direction could be amended to become subject to such directions.
 - A review of board member duties under the Crown Entities Act, to ensure that the relationship between those duties and directions by Ministers are properly described
 - Withheld under section 9(2)(g)(i) of the Official Information Act

- A review of section 107, to consider explicitly stating that "specified requirements" may include reference to processes or administrative decisions made by Ministers or functional leaders (in our view the scheme of the provisions already allows this but it would be helpful for the legislation to be explicit on the point).

Regulatory impact analysis

54. Although a Regulatory Impact Statement (RIS) is not required, because the directions are not primary legislation or disallowable instruments, the substantive information that would be required for a RIS is contained in Appendix 2 (which provides explanatory material for the Select Committee).

Next steps

55. Subject to Cabinet endorsement of the text and scope of the directions, and the intention of joint Ministers to issue the directions, the next steps are:
- Affected entities are notified, the directions are referred to the House together with explanatory material, and stand referred to the Finance and Expenditure Committee (FEC).
 - FEC reports back to the House (12 sitting days after referral).
 - The directions come into force (15 sitting days after referral) unless the House resolves to disapply one or more of them. The date for a direction to take effect can be specified as part of the direction.
 - Joint Ministers publish the directions in the Gazette and on the Internet (SSC's website) as soon as practicable.
56. We propose to direct the Head of the State Services to notify the affected entities that we are issuing the directions, and that they are being presented to the House.
57. Once the directions take effect, subsequent actions are to monitor compliance with the directions, and to review them by the specified timeframe (if in the direction) or 5 years after the direction is given.

Publicity

58. We propose to release the Cabinet paper (subject to any redactions), directions and explanatory material on the SSC's website after the directions have been reported back to the House by the Select Committee (unless they are disapplied).

Recommendations

59. We recommend that the Cabinet Committee on State Sector Reform and Expenditure Control:

- 1 **note** that on 9 December 2013, Cabinet:
 - 1.1 noted that benefits would be achieved from extending Procurement, ICT and Property functional leadership requirements to specified Crown entities
 - 1.2 directed the Head of State Services to put in place a process for coordinated consultation on proposed directions under section 107 of the Crown Entities Act 2004
 - 1.3 invited the Ministers of State Services and Finance to report back to SEC by 31 March 2014 on the outcome of consultation on the three directions

[CAB Min (13) 43/3].

Consultation

- 2 **note** that 102 entities covered by one or more of the proposed directions were invited to participate in the consultation process
- 3 **note** that key themes from 37 written submissions and verbal feedback involving around 80 entities in total were:
 - 3.1 widespread support for the intent of the directions
 - 3.2 concerns about impacts of the directions on board decision rights and authority, with a few entities raising questions about the overall legal framework for the directions
 - 3.3 need for greater clarity on the requirements in the directions, on their application, and on how the implications of the requirements may change over time
 - 3.4 need for clear disputes resolution and escalation processes
 - 3.5 concerns about additional costs compared with benefits
 - 3.6 need for adequate timeframes for introduction (especially for Procurement), and for implementation support, and
 - 3.7 some questioning of coverage (many entities are already complying on a voluntary basis, and some would prefer that this continue)
- 4 **note** that as a result of the feedback, officials have:
 - 4.1 sought advice, including from Crown Law, on the legal issues raised
 - 4.2 amended the wording of the directions to provide greater clarity on some aspects of the requirements
 - 4.3 clarified the processes set out in the directions
 - 4.4 clarified the processes for disputes resolution and escalation relating to the directions, and

4.5 recommended extending the timeframe for introducing the Procurement direction

Risk

Withheld under section 9(2)(g)(i) of the Official Information Act

Financial implications

- 6 **note** there is reasonable evidence that a decision to extend functional leadership requirements to Crown entities will be fiscally positive overall, but will impose some transitional and other operational costs particularly on some smaller entities

Legislative implications

- 7 **note** that, while not urgent, officials will consider how future legislative change opportunities could be used to further improve the operation of directions issued under s107 of the Crown Entities Act 2004

Text of the directions

- 8 **endorse** the text for the section 107 direction to extend the Government Rules of Sourcing (as provided in the body of the paper)
- 9 **endorse** the text for the section 107 direction to extend the ICT functional leadership requirements (as provided in the body of the paper)
- 10 **endorse** the text for the section 107 direction to extend Property functional leadership requirements (as provided in the body of the paper)

Next steps

- 11 **note** the intention of the Minister of State Services and Minister of Finance to issue the directions to extend functional leadership set out in recommendations 8-10 above, notify affected parties, and present the directions and explanatory material to the House of Representatives on or about Tuesday 22 April 2014
- 12 **invite** the Ministers of State Services and Finance to direct the Head of the State Services to notify affected parties on their behalf that they are issuing the directions, which are being presented to the House
- 13 **note** that the material in Appendix 2 of this paper will be provided as explanatory material to accompany the directions when they are presented to the House of Representatives and referred to Select Committee
- 14 **note** that the Ministers of State Services and Finance intend to publish the directions in the Gazette, and to release this Cabinet paper and explanatory material on the State Services Commission's website, as soon as possible

after the directions have been referred back to the House (unless they are disappplied)

- 15/ **direct** the Functional Leaders for Procurement, ICT and Property to report on whether the directions are achieving the intended objectives, and on any lessons learned, as part of regular reporting to responsible Ministers and Cabinet.



Hon Bill English
Minister of Finance



Hon Dr Jonathan Coleman
Minister of State Services

Date:

Appendix 1

Crown entities covered by the directions

Coverage for the Property, Procurement and ICT directions is set out in the table below.

	Property	Procurement	ICT
Group of 7 specified Crown agents (*) Accident Compensation Corporation, Earthquake Commission, Housing New Zealand Corporation, New Zealand Qualifications Authority, New Zealand Trade and Enterprise, New Zealand Transport Agency, and Tertiary Education Commission	Yes	Yes	Yes
All District Health Boards (20)	-	Yes	Yes
All other Crown agents (21) Callaghan Innovation, Careers New Zealand, Civil Aviation Authority of New Zealand, Education New Zealand, Energy Efficiency and Conservation Authority, Environmental Protection Authority, Health Promotion Agency, Health Quality and Safety Commission, Health Research Council of New Zealand, Maritime New Zealand, New Zealand Antarctic Institute, New Zealand Blood Service, New Zealand Fire Service Commission, New Zealand Tourism Board, New Zealand Transport Agency, New Zealand Walking Access Commission, Pharmaceutical Management Agency, Real Estate Agents Authority, Social Workers Registration Board, Sport and Recreation New Zealand, WorkSafe New Zealand	Yes (**)	Yes	-
Autonomous Crown Entities (ACEs) (18) Arts Council of New Zealand Toi Aotearoa, Broadcasting Commission, Families Commission, Government Superannuation Fund Authority, Guardians of New Zealand Superannuation, Museum of New Zealand Te Papa Tongarewa, New Zealand Artificial Limb Service, New Zealand Film Commission, New Zealand Historic Places Trust (Pouhere Taonga), New Zealand Lotteries Commission, New Zealand Symphony Orchestra, New Zealand Teachers Council, Public Trust, Retirement Commissioner, Standards Council, Te Reo Whakapuaki Iirangi (Maori Broadcasting Funding Agency), Te Taura Whiri I Te Reo Māori (Māori Language Commission), Testing Laboratory Registration Council	-	Yes	-
Independent Crown Entities (ICEs) (17) Broadcasting Standards Authority, Children's Commissioner, Commerce Commission, Drug Free Sport New Zealand, Electoral Commission, Electricity Authority, External Reporting Board, Financial Markets Authority, Health and Disability Commissioner, Human Rights Commission, Independent Police Conduct Authority, Law Commission, New Zealand Productivity Commission, Office of Film and Literature Classification, Privacy Commissioner, Takeovers Panel, Transport Accident Investigation Commission	-	Yes	-

	Property	Procurement	ICT
Crown entity companies (11) <i>Crown Research Institutes (CRIs):</i> AgResearch Limited, Institute of Environmental Science and Research Limited, Institute of Geological and Nuclear Sciences Limited, Landcare Research New Zealand Limited, National Institute of Water and Atmospheric Research Limited, New Zealand Forest Research Institute Limited, New Zealand Institute for Plant and Food Research Limited <i>Other companies:</i> Crown Irrigation Investments Limited, New Zealand Venture Investment Fund Limited, Radio New Zealand Limited. Television New Zealand Limited	-	Yes	-
PFA Schedule 4A companies (8) Crown Asset Management Limited, Crown Fibre Holdings Limited, Fairway Resolution Limited, Health Benefits Limited, Network for Learning Limited, The Research and Education Advanced Network New Zealand Limited, Southern Response Earthquake Services Limited, Tamaki Redevelopment Company Limited	-	Yes	-
School Boards of Trustees	-	-	-

(*) 7 specific Crown agents with the common characteristic of sizeable ICT business transactions and investment

(**) Except for the NZ Blood Service, which is excluded from the Property direction.

A regularly updated list of State Sector organisations is at www.ssc.govt.nz/state_sector_organisations.

Explanatory material on directions to extend functional leadership requirements (for Select Committee)

Introduction

- 1 Extending functional leadership mandates beyond core Public Service departments is desirable to secure economies of scale, improve operational efficiency, build capability and improve service delivery. These purposes are consistent with the purposes for which a section 107 direction under the Crown Entities Act 2004 (the Act) may be used.

Consultation process and themes

- 2 The State Services Commissioner wrote to all the entities covered by the proposed directions to advise them of the proposals and invite their responses. The monitoring departments for each of the affected entities were also written to and invited to respond.
- 3 A range of briefing sessions, individual meetings and phone discussions took place, including:
 - a meeting of the chairs and chief executives of Crown agents covered by all 3 directions, hosted by the State Services Commissioner
 - a meeting of the chairs of the District Health Boards (DHBs), covered by the ICT and Procurement directions, attended by representatives from the State Services Commission and functional leaders
 - 7 briefing sessions held by the Procurement functional lead officials (including sessions in Auckland and Christchurch), and six individual meetings with agencies
 - a teleconference session between GCIO officials and the National Health IT Board, and four meetings with individual Crown agents
 - three briefing sessions for Crown agents covered by the Property directions.
- 4 In addition, there were numerous follow-up discussions and phone calls (particularly for Procurement, given the much greater number of entities involved).
- 5 Written submissions were received from 36 Crown entities, 1 Public Finance Act Schedule 4A company, and three monitoring departments. Both written submissions and oral feedback were considered as part of the consultation.
- 6 Key themes from the submissions will be outlined (from the Cabinet paper).

Background material on the individual directions

Procurement direction

Issue to be addressed by the Procurement direction

- 7 The Government Rules of Sourcing (the Rules) support the aim of Procurement functional leadership to improve procurement performance across the State sector. They do this by placing a stronger focus on upfront planning, robust buyer-supplier engagement, encouraging innovation, and better, more transparent processes.
- 8 The Rules reflect internationally recognised minimum standards of good procurement practice, but currently apply only to Public Service departments, New Zealand Police and New Zealand Defence Force. This has resulted in inconsistent procurement practices across government agencies, and opportunities to improve the way that government agencies do business with suppliers are being missed.

Which entities the Procurement direction is to be applied to

- 9 The Procurement direction is to be applied to about 100 entities, including:
 - all statutory Crown entities (ie all Crown agents, Autonomous Crown entities, and Independent Crown entities)
 - all Crown entity companies (including Crown Research Institutes and other Crown entity companies)
 - all Public Finance Act schedule 4A companies (which are treated as Crown entities for the purpose of section 107 directions).

The current list of State sector organisations is available at www.ssc.govt.nz/state_sector_organisations.

- 10 Every Crown entity has to give effect to a section 107 direction, except that Crown Research Institutes only have to have regard for such directions.

Costs and benefits of the Procurement direction, and how costs will be funded

- 11 The proposed direction will double the amount of procurement expenditure covered by the good practice standards set out in the Rules, from approximately \$10 billion to \$20 billion per annum.
- 12 As agencies are already expected to follow the Auditor-General's procurement guidance, the Rules should not impose any substantial additional costs on them, although some agencies may need to invest some additional resources for a transitional period to update policies and procedures, train staff etc. The cost of this will depend on each entity's level of alignment to the Rules. Where agencies are already well aligned, there should be limited, if any, additional costs associated with compliance.
- 13 There are significant direct financial benefits to agencies from the application of the Rules, in addition to benefits across government. Benefits to agencies include reduced prices from the aggregation of government spend and reduced

transaction costs from not having to duplicate tender processes for products made available under an all-of-government contract. These savings should become evident as entities transition from current contracts. There are also sustainable benefits from consistent application of good practice, including the contribution of procurement to the growth of New Zealand businesses leading to increased exports, which are difficult to quantify.

- 14 Within the Rules are requirements to purchase from all-of-government contracts (which represent only 2% of procurement expenditure across government). Forecast savings from these contracts is approximately \$350m over the life of the contracts. The mandatory requirement will provide some greater certainty to these forecast savings. It is estimated that an additional \$5-10m savings per annum would come from Crown entities that are currently not purchasing from these contracts voluntarily.
- 15 The all-of-government contracts cover common-use goods and services that most government agencies need to operate. Many agencies have already recognised that the value of the all-of-government approach to these categories goes well beyond the actual cost savings and includes the benefit of reduced procurement effort. This can be particularly important for smaller agencies that have limited in-house procurement expertise.
- 16 The all-of-government contracts are established on the basis of an administration levy (not exceeding 1.5% of the purchase price) which covers the cost of establishing and managing the contracts. Savings are retained by the agency, and can be applied by the agency to other activities such as front line services.

Feedback from consultation specific to the Procurement direction

- 17 Feedback from consultation on the Procurement direction was diverse, reflecting the wide range of entities covered by the direction.
- 18 Several entities were highly supportive of the proposed direction, and noted close alignment between their internal procurement practices and the Rules. Implementation issues included the need for entities to have sufficient time to adjust their internal change management processes, such as internal communications and staff training. They also requested clarification of some Rules. Other specific concerns included threshold levels for applying the Rules, and concerns over legal risk and liability.

Changes to the Procurement direction as a result of consultation

- 19 Changes made as a result of consultation include:
 - The date for the direction to take effect is specified as 1 February 2015 (to allow time for entities to adjust their internal processes, and for the Functional Leader to develop tools and processes to support entities in applying the direction and make minor adjustments to the Rules for clarification.
 - Clarification that ministers approve amendments to the Rules.
 - Removal of a requirement for entities to co-operate fully with the Functional Leader in any monitoring of compliance in order to be clear that the aim is

to focus on good procurement practice, not to increase risk to entities or to focus on compliance.

Amended Procurement direction

20 Text will be added from the Cabinet paper.

ICT direction

Issue to be addressed by the ICT direction

- 21 Government has charged the Government Chief Information Officer (GCIO) with leading government ICT to provide system-wide assurance, enable integrated digital service delivery, and deliver sustainable business savings of \$100 million per year by 2017. At present, the ICT Strategy and Action Plan, including mandated ICT assurance requirements, applies only to Public Service departments, and 4 non Public Service departments (NZ Defence Force, NZ Police, NZ Security Intelligence Service and the Parliamentary Counsel Office).
- 22 Including a set of Crown agents with significant ICT business transactions and investment enables the benefits of integrated digital service delivery to be spread more widely across the State Services, provides more support for and visibility over ICT assurance, and contributes to the sustainable business savings that can be achieved.
- 23 The requirements sit alongside other existing administrative rules and expectations. For example, the directions do not change the decision rights or asset management or reporting standards expressed in Cabinet office circulars like CO(10)02 and CO(11)06.

Which entities the ICT direction is to be applied to

- 24 The ICT direction applies to all DHBs and seven Crown agents with sizeable ICT business transactions and investment: Accident Compensation Corporation, Earthquake Commission, Housing New Zealand Corporation, New Zealand Qualifications Authority, New Zealand Trade and Enterprise, New Zealand Transport Agency, and Tertiary Education Commission (27 entities at present)

Costs and benefits of the ICT direction, and how costs will be funded

- 25 There are likely to be some initial transition costs for Crown entities associated with integration of mandated common ICT capabilities. However, some Crown entities are already using common capabilities such as RealMe or Infrastructure-as-a-Service, and have made those decisions voluntarily because the cost, functionality, and uplift in delivery of services make the common capabilities more attractive than what was previously in place. Through increased participation, agencies have experienced increased savings per annum. There may also be increased costs to the Treasury (eg, the Portfolio Performance Management function) from the expanded scope for ICT and other areas of functional leadership resulting from the directions.
- 26 The vast majority of the financial savings from the ICT functional leadership mandate are 'cost avoidance'. For example, common ICT capabilities such as

IaaS and Desktop-as-a Service (DaaS) deliver benefits through cost avoidance. These benefits are achieved as agencies avoid having to fund a large refresh of assets because they have reached the end of their useful lives, or are no longer supported. Under the DaaS contract, for instance, agencies will not have to fund upgrades such as the Windows XP to Windows 7 upgrade, which many government agencies are currently facing. This means that cash flows are maintained at manageable levels and bottlenecks are avoided.

- 27 Funding for the GCIO is largely from Crown funding, with some user-pays for services. Under the current funding model, savings realised from the extension of ICT functional leadership would be retained by individual Crown entities.

Implementation issues, and how they will be addressed

- 28 Concerns raised included duplication of processes, adding to the compliance burden. The GCIO is working with the Treasury's Portfolio Programme Management team and the National Health IT Board (NHITB) to streamline their work with already existing processes rather than creating duplication. The NHITB will act as the GCIO's agent within the health sector.
- 29 A number of entities also raised the need for clarity around timeframes for ICT common capabilities, including when they would be available, and when uptake is expected. The amended direction includes that the entities will be consulted before new common capabilities are agreed, and that they will be implemented "within timeframes negotiated with the GCIO". Most entities asked about opt-out processes from common capabilities. That has also been explicitly included in the direction.

Changes to the ICT direction as a result of consultation

- 30 Changes to the ICT direction proposed for consultation include:
- Most of the direction will take effect on the date it comes into force under section 109 of the Crown Entities Act, except that the ICT assurance requirements will only apply to DHBs from 1 July 2015.
 - Explanatory information has been added, eg, that the timing for introduction of common ICT capabilities is, where relevant, subject to negotiation with the GCIO. This responds to uncertainty about required timing for implementation.
 - Clarifies that any new mandatory ICT common capabilities will need to be contemplated by the *Government ICT Strategy and Action Plan to 2017*, decisions to mandate them by the GCIO and Head of State Services in relation to departments (pursuant to the power conferred on them by Cabinet, CAB Min (12) 34/4C refers) will apply automatically to the relevant Crown entities under the direction (thereby removing any separate exercise of discretion), and decisions on exemptions will ultimately, where required, be escalated to ministers.
 - Insulates the direction from challenge under section 113 because there is now an exception which applies to the substance of the direction that states "except to the extent that any requirement in this clause 1 would be inconsistent with section 113 of the Crown Entities Act 2004".

- Future proofs the requirements around assurance and security panels by removing the specific names of current panels.

Amended ICT direction

31 Text will be added from the Cabinet paper.

Property direction

Issue to be addressed by the Property direction

- 32 The functional leadership approach for property recognises opportunities for benefits from a cross-departmental approach to property strategy, procurement, standards and processes. The mandate agreed by Cabinet [CAB Min (12) 35/4B] requires the Property Management Centre of Expertise (PMCoE) to achieve capability, effectiveness and efficiency improvements across Public Service departments and four non Public Service departments. In addition, responsible Ministers for each Crown agent (except DHBs) have been invited to convey their expectations that Crown agents comply with the mandate.
- 33 While the majority of Crown agents currently act in accordance with the Property Functional Leader's mandate, this does not guarantee future cooperation. Relying on voluntary cooperation represents a delivery risk to forecast potential savings if cooperation decreases.

Which entities the Property direction is to be applied to

- 34 The entity is to be applied to all Crown agents, except for DHBs and the NZ Blood Service (26 entities at present).

Costs and benefits of the Property direction, and how costs will be funded

- 35 Since 2013, the majority of Crown agents have already been applying the Property functional leadership requirements on a voluntary basis. The Property direction will therefore not add to current Crown agent costs in most cases. The costs arise mainly from the requirement to produce Property plans (which many agents do anyway), and from compliance with good practice standards and principles.
- 36 Benefits from the direction rise from enabling achieving greater capability, effectiveness and efficiency improvements in relation to office accommodation, public interface and service delivery space. The Property Functional Leader estimates that the Crown agents account for around 9.6% of the leasehold component of total forecast benefits between years 2015/16 and 2024/25.
- 37 The PMCoE receives Crown funding to provide guidance, support and monitoring in respect of property management within the public sector, but operates a cost-recovery model to cover all of its costs. The majority of savings remain with the agencies covered by the Property direction as provided for in the cost-recovery model (currently a minimum of 95% savings remain with the agencies).

Issues raised in Property consultation

- 38 Five submissions simply expressed positive support for the direction. The main other feedback sought clarification on the requirements and their scope, including making them standalone without cross-references to other Cabinet minutes or documents. Questions were also raised about the processes for resolving any disputes about the application of the requirement.

Changes to the Property direction as a result of consultation

- 39 Changes to the Property direction in response to consultation are outlined below.
- Changes were largely to clarify the requirements and make them unambiguous.
 - Clarification that the Functional Leader will have regard to the Crown agent's operational requirements in their property plan when approving it.
 - Making it clear that operational areas and areas under the direct control of a Crown agent's investment function are excluded.
 - The NZ Blood Service is now excluded from the direction on the same basis DHB's are (all office space is going to be within operational sites).
 - An explicit requirement that Crown agents must implement the average workplace density of 12-16 square metres at the soonest practicable opportunity (instead of a cross-reference to a Cabinet minute with this requirement).
 - Reworded a requirement to state that Crown agents will adopt and use the IWMS approved by the functional leader (rather than calling it by name "Archibus" because the provider could conceivably change).

Amended Property direction

40 Text will be added from the Cabinet paper.

Monitoring and review

41 The Functional Leaders will report on whether the directions are achieving the intended objectives, and on any lessons learned, as part of their regular reporting to responsible Ministers and to Cabinet.

Appropriateness of direction to apply whole of government approach, as against alternatives

42 Appendix 2 of the Cabinet paper SEC (13) 70 (released on SSC's website at www.ssc.govt.nz/whole-of-govt-directions-dec2013) covers this matter and will be provided to the committee.

Statutory process

43 In accordance with the Act, if after consultation the Minister of State Services and the Minister of Finance give a direction to support a whole of government approach they must, as soon as practicable:

- notify the entities to which the direction will apply that the directions has been given and will come into force subject to section 109 of the Act ('House of Representatives may resolve to disapply a direction under section 107)
- present the direction under section 107 to the House of Representatives.

44 A direction comes into force 15 sitting days after it is presented to the House of Representatives, unless the House resolves, in that period, to disapply it under section 109 of the Act. Such a direction is referred to the Finance and Expenditure Committee which either examines it itself, or refers it to another select committee.

45 As soon as practicable after a direction comes into force under section 109, the Ministers of State Services and Finance must ensure that it is published in the *Gazette* and on the Internet. If the direction does not come into force, the Ministers must notify the entities to which the direction would have applied that the direction has been disappplied and will not come into force.