5. The 'new responsibility model' for New Zealand public-sector CEOs[1]

The Hon. Bill English

I approach the topic of public-sector change from a finance minister's perspective, speculating on how we might embrace further reform over the next 10 years. It is a review that comes from a number of years observing this important topic, starting with my experience as a junior Treasury official when Roger Douglas was New Zealand's Minister of Finance, developing when I entered Parliament in 1990 when the government I was part of was undertaking a program of dramatic reform, and, most recently, continuing over a number of years spent in opposition, where I had time to ponder and reflect on the lessons learned.

One of the advantages of bringing a finance minister's perspective to the topic of substantive reform and policy change is that it helps answer one basic question: why would anyone in the community choose to do what we in government want them to do? Essentially, the only reason they will agree to do what we want them to do is because we have the money and they require it. There is no shortage of public-policy talk that is attractive and articulate, but if you cannot find a reason why people should want to do it then it simply does not happen. Public services do not need to do anything in particular—that is the nature of the business.

Over the next 10 years we are going to see a revolution in public management. Governments around the world are striving to tackle the enormous fallout from the present global recession. Australia is in a somewhat unique position of being under less pressure than any government in the developed world to think hard about its public services. As for New Zealand, our fiscal and economic outlook lies somewhere between the relatively benign outlook for Australia and the extremely grim outlook for countries such as the United Kingdom and the United States with respect to their public finances. This is our challenge.

New Zealand's economic challenges

The economic context provides an important backdrop to my views of public-sector management. Consider first New Zealand's current economic challenges and how they contrast with Australia's. When comparing the Australian and New Zealand economies over the past 15–20 years—with the exception of the

1 This chapter is an edited version of a speech given by the Hon. Bill English MP to the 2010 ANZSOG Annual Conference in Melbourne.

Australian resources boom and the trade effect that brings—many similarities can be found. If you put aside the resources boom, you would find that Australia, like New Zealand, has experienced unbalanced growth. In New Zealand, at least, this growth has been sluggish, and too much of it has been driven by excessive debt, over-consumption and fast increases in government spending.

The New Zealand economy has become lopsided in two ways, and both need to be addressed for a rebalancing to occur. First, our trade sector has been in recession for five years, with no new jobs created in the export sector for a decade. Second, we need to address our rapid increase in external liabilities. Australia owes the rest of the world about 60 per cent of gross domestic product (GDP); New Zealand owes 90 per cent, with ours forecast to rise over the next five years. Both countries need to correct that imbalance; we simply cannot keep returning to global financial markets and asking them to lend us money. The Australian banks, which essentially finance New Zealand's external liabilities, have repeatedly told me that this is going to get more difficult and more expensive, not easier.

In an attempt to rebalance our economy, the New Zealand Government is currently embarking on a wide-ranging program of reform after a decade of stalling and inaction. To do this, we will be demanding more accountability and effectiveness from the public sector. The main reform we have made so far has been changes to our tax system. From 1 October 2010, we will be dropping income taxes considerably, with the top tax rate falling to 33 cents, the marginal tax rate on the average wage becoming 17.5 per cent and company tax becoming 28 cents. Tax on savings accounts will also be reduced. To pay for these changes, the New Zealand Government is increasing the goods and services tax (GST) from 12.5 per cent to 15 per cent, increasing the effective tax rates on property investment and closing a range of domestic and foreign loopholes. These changes are designed to rebalance the economy and increase our international competitiveness and have so far been received with a surprising level of bipartisanship. This is largely because of the policymaking process we followed, which I will discuss shortly.

As a result of New Zealand's recent sluggish economic performance, our fiscal position has dramatically reversed in the past four or five years. After 15 years of surpluses, we are now facing at least another five or six years until we resume surpluses. Even then we need surpluses of approximately 2 per cent of GDP to meet the obligations of the New Zealand Super Fund, a large sovereign wealth fund designed to offset the future costs of superannuation. Consequently, in the professional lives of most of our present-day civil service leaders there will not be a time when we have the easy money we had in the past 10 years. In other words, there will not be a time in the professional lives of our civil service when the government is free to simply increase the price it pays for public services.

To address this dire situation, we have set some tight fiscal constraints. Over the next four years there will be a 4.8 per cent real increase in government spending, or 1.2 per cent per year. This is difficult to compare with the Australian Federal Government's 2 per cent real increase per year, except that we know it is lower, partly because in New Zealand we cover all federal and state (provincial) activities under one roof. So far we have reprioritised nearly $4 billion of spending over the next three or four years from low-value and ineffective services to higher-value, frontline and more effective services. These are, however, the quick wins from a previous decade of loose management of government spending and rapid growth in government spending, particularly since 2005.

The 1.2 per cent goal will be hugely challenging, and New Zealand's public service has only recently started to understand what that might mean after a decade of 6 and 7 per cent compound annual increases. That said, whatever we do will look mild compared with the radical experimentation happening in the United Kingdom and the United States, where they are adding 10 or 12 per cent per year of GDP to their stock debt and, in some cases, shutting down entire public services. What will the community look like without public services? We will find out.

The outlook for the New Zealand public sector

Looking ahead, how are we going to live with these tight fiscal constraints? How are we going to deliver more (as the public is demanding) for less (as our finance markets are demanding)? To answer these questions, we will be looking for new ideas and directions and, frankly, I do not think they are to be found in Australia and New Zealand. That said, New Zealand will be looking at the best Australia can come up with and, similarly, we hope Australia will look to us. Around the world we will see a revolution in public service management. The prevailing literature and new public management approaches are conditioned by at least a decade of generous year-on-year increases in funding, and developed a complacency that 15 years ago was not found in our public services but has since re-emerged.

The large economic shifts that have recently occurred, particularly in the United Kingdom, the United States and Europe, mean that these governments will spend the next 20 years trying to first stop the massive increase of deficits they are currently running, and next work out how to pay back the significant public debt they have accrued. I do not believe we fully understand that while the economies of these countries will soon pick up, their public finances will be a mess for decades to come. These deficit economies face the prospect of cost-crunching innovations and dramatic downsizing of their public sectors.

The optimism of the past decade that smart people using the massive resources of government can transform society will depart these countries. That thinking has not only run out of money in most places now, but also actually achieved little that was genuinely transformational while it prevailed. New, more revolutionary experiments will have far less aspirational goals. We will have to determine which public services and income-support measures really matter—not just which ones people like, but ones that really matter. We will have to work out how to deliver those services for much less money.

At the same time another set of experiments will be undertaken. Those countries that are substantially in surplus—in our region, largely the Asian 'command' economies—are going to be developing internal demand, growth and private consumption and, therefore, demand for public services that currently do not exist in their own countries. As a result, I expect New Zealand and Australia will find themselves selling their frameworks for better management, better accountability and transparency to these emerging economies that are developing their range of public services.

Fiscal constraint and the 'responsibility model' for CEOs

In light of this, what are we doing in New Zealand, given that we have more fiscal pressure than Australia and do not have the benefit of a commodity boom to cushion the otherwise underperformance of our economy? The answer is what we call the 'responsibility model': a five-year plan centred on chief executives that incorporates some of the factors we believe will drive further change. As an incoming government in late 2008, we had a choice of ripping out 'savings' from the budget and embarking on a large-scale restructuring plan. We are not, however, doing that. We have left existing structures largely in place while establishing very clear fiscal constraints over the next four years. To do this, we are pushing the responsibility for managing resources onto our public-sector chief executives; it is not up to the Treasury or the Minister of Finance to ensure that we live within those constraints; it is up to the leadership of the separate sectors of government. We are consciously stress testing our existing, fairly devolved model of public-sector management.

There are two reasons why we are working with the existing system. One is simply that our election campaign was conducted just prior to the onset of the global financial crisis. Within days of us launching a major tax package with significant revenue costs, Lehman Brothers bank went down, the Australian Government announced its deposit guarantees, and the world suddenly changed. Despite these upheavals, we decided to stick with our original plans, having earlier specifically ruled out large-scale structural change in the public services.

The second reason we have chosen to stick with the existing models is that New Zealand's experience through the 1980s and 1990s has taught a number of people—including myself—that long-term effective change is driven by people who clearly understand the parameters they are working within and have the tools they need to implement change. That is why we are making chief executives of departments the fulcrum of change.

This 'responsibility model' requires ministers and chief executives to clarify exactly what results they want. We are using the basic tools of ministerial and chief executive accountability, and thus spend a good deal of time ensuring that discussion between the Prime Minister and his ministers exactly reflects these expectations over the next two or three years.

We believe strongly in an alignment of political and administrative expectations. The process of ensuring the Prime Minister and ministers are clear about their expectations and performance is something we value strongly. It is a process that takes time to build momentum; a culture of caution and risk management in our public sector has become deeply embedded in the decade. As ministers, we must keep demonstrating political support for change and reinforcing the mandate that chief executives can use tools and make changes without fear of political consequences. After two years, they are starting to believe us. We reinforce this message with regular oversight of the 10 different public entities that make up 80 per cent of government expenditure. Much work has been required using these very basic tools simply to slow the growth in government spending.

Continued cooperation with Australia is also critical to delivering quality services within tight fiscal restraints. Australian businesses own $45 billion worth of assets in New Zealand, so we are working with the Australian Government on everything from insolvency law through to businesspeople being able to get through customs more easily. We are developing institutions for intellectual cooperation and we have comprehensive access to Australian politicians and officials, granting us specific knowledge and relevant expertise when we want to lift that knowledge and use it. There is a much bigger body of independent policy analysis in Australia than in New Zealand, so it is practical for us to draw on the Australian experience, rather than do it all ourselves. For example, in a difficult policy area such as competition law it would be a good idea to appoint cross-membership on our competition regulators.

The challenges to further public-sector reform

There are, of course, many challenges associated with the 'responsibility model', but for experienced civil servants they will all be predictable. The first is that if we cannot generate early momentum, the public sector will doubt its politicians can stick to self-imposed spending constraints and so will hope and wait for a return to the status quo. Some in our public service are still trying to wait it out, but this approach will not work. To be blunt, hope is not a strategy for a professional civil servant. It has been tried often and has occasionally worked, but it will not succeed over the next few years because the global recession and difficulties of public finance are not going to change. In New Zealand, at least, there is strong demand from the public to see the civil service doing what they have had to do themselves: be careful with their spending and make sure they have clear priorities in their businesses or their household. There is thus popular support for our approach.

Second, in a devolved system such as ours, it takes time and effort to achieve the right balance between the collective and individual interests among ministers. I have learned the hard way that the public service will avoid doing something if ministers are ambivalent about it getting done. Even if one minister clearly wants to do it, if the others are lukewarm then that provides an excuse for stalling. In New Zealand, we spend a great deal of time getting the collective interests of ministers aligned—a significant challenge in a centre-right government in which ministers tend to come from self-employed and business backgrounds. In our system, they have considerable ministerial freedom to do or not do things. But once ministerial cohesion is achieved, that sends a clear and compelling message to the public service.

To assist with this endeavour, hard-wired accountability is essential. The complexity of the ministry at one end and the centrifugal forces of agencies trying to stay in the game at the other are not going to hold. We must develop different hard-wired models. Ideally that starts with ministers and it means that we probably need to rethink how cabinets work in order to achieve greater ministerial alignment (and reduce 'static'). Ministers need to work together to ensure the collaborative and cooperative delivery of services takes place. The New Zealand cabinet recently took 18 months to agree on a small program aimed at integrating social services at the local level. Principally, this was because, as Finance Minister, I refused to agree to it until we had a model of hard-wired accountability—not just another committee. Other ministers refused to agree for other reasons, but after 18 months we finally worked out how to integrate these services efficiently. It was a hugely instructive exercise for ministers because they are starting to realise that there is a problem out there and that problem often begins with us. At present the only powerful tool for achieving closer alignment is that ministers are ultimately accountable to the Prime Minister, who has the power to sack them. But modern cabinets require more than this punitive sanction to make them work effectively.

Our third and perhaps most important challenge is whether our public-management system permits or encourages the kinds of solutions that are now required. In the past 20 years there have been many attempts at 'joined-up' or 'collaborative' government. But solutions such as shared services, joint procurement, and joint decision making across a sector do not fit naturally into the parliamentary appropriation process, or into the traditional structures of the public service—an institution whose hierarchal accountability has not altered for many years. Most of these attempts at collaborative government, at least in New Zealand, have failed ultimately because the processes of 'joining up' are actually very inefficient. They take enormous amounts of time and effort and do not always result in better accountability. Usually, frustration prevails and all parties return to their original modus operandi.

Consequently, it is a challenge for public servants to develop strong 'internal governments' to run joint processes. In New Zealand, we are expecting them to do this without strong direction from a highly centralised process. To facilitate this, we have supported a handful of collective processes such as joint procurement and, beginning soon, administrative and support services benchmarking shared services in the health sector. We are, thus, focused on the issues associated with administrative change because we are pursuing a program of organic change. Additionally, we have also set up an internal infrastructure unit to create better capital management.

In each of these examples, our chief executives have the choice of picking up these tools or not; they are not compelled to use them. Initially progress has been slow, but the momentum is now picking up as chief executives begin to realise that when they forecast their costs against their revenues they find a significant negative gap. This financial pressure can promote the case for change; CEOs' revenues are flat, their costs are rising and over the next four years that gap will grow every month that they sit on their hands. This message is starting to have an impact.

Allowing voluntary participation in these collective initiatives maintains a healthy tension between central agencies and other policy entrepreneurs, while providing a great way of showing public-sector managers the value of spending time and effort collaborating. Essentially, if executives are not willing to enter into collaborative endeavours (and sit through the interminable meetings this usually involves) then they should not have to, but if this is the case, they must find another way to improve delivery. If they want to use new media to achieve better communication they can. We believe that voluntary participation is critical to ensuring public servants make genuine progress, rather than just ticking the box on reporting to the minister. Nevertheless, the internal governance of back-office processes is merely a first step. Admittedly, we are yet to fully achieve this, but we will.

The next major step is to determine the outcomes we want in the wider community and structure accountability and governance in the public sector around those outcomes. Yet, such an approach conflicts with our traditional model of parliamentary accountability. The fact is though, the traditional model of parliamentary accountability might account for the money, but it has singularly failed over the past 20 years to account for results. In New Zealand, for example, we have been through a long process of trying to upgrade the scrutiny of our select committees. But from a minister's perspective, it is not a fearsome forum, largely because of the huge information imbalance between opposition MPs and ministers.

Accordingly, we need to resolve the tension between accountability for results and accountability for the money. An example is the criminal justice system, which we in New Zealand are trying to make less costly and more affordable. New Zealand has one of the highest imprisonment rates in the world, but locking people away is expensive. Consequently, at a time when funding is tight, we have to find new ways to foot the bill for tougher sentences for serious criminals—something the public is demanding. One response is to examine carefully the prosecution and imprisonment rates for less serious offenders to determine what patterns are forming. So, four years ago our justice-sector agencies in New Zealand began to work together to better understand what happens in the justice pipeline—who is arrested and why, how they come to the attention of the police, how they move through the courts, how they end up in prison and what does it all cost. This has generated some initial operational solutions for a more effective and a more just and humane system.

We can get some benefits within the current justice system, but one recurring problem is that we have a series of agencies with their own statutory powers. The police are different to the courts, which are different to the corrections services, which are different to the probation people, who are different to the non-governmental organisations. Each of these organisations has a strong culture that is typically hierarchical and rigid. Having analysed the ways the justice pipeline works, the fundamental next step is not to again recite the appalling statistics about which groups are more likely to end up in prison, which has been the stuff of public policy in this area for too long, but rather to develop a governance regime that is going to allow us to drive the outcomes that we want—namely, reduced prisoner numbers.

For the existing public service, providing this type of advice is much more difficult than performing business as normal within their part of the justice pipeline, because we are asking them to fundamentally alter their relationships of power, funding and authority. They will do this only if we can develop a strong enough constituency in the public who demand fewer people in prison, for example, or less youth offending. But at the moment we do not have a suitable structure; instead, it is an amalgam of chief executives and police commissioners all trying to work their way in a similar direction. If we are really going to drive reform, so we can head off the current demand for another 3000 new prison beds in New Zealand, we are going to need a new governance structure. Our public service has not thought nearly hard enough about how it will change the accountability regimes to drive the outcomes we need with less money to spend.

In the sector of criminal justice in New Zealand, we will not meet public expectations within current fiscal constraints with the current institutional arrangements in place. We simply cannot do it. It does not add up. To do this our public service must focus strongly on how to cut through multiple layers of authority, risk management and minister management and actually put people in charge of outcomes.

This issue is not unique to the justice sector; it is far more pervasive. In New Zealand, we are currently undertaking a broad front of reform in the areas of workers’ compensation, long-term welfare, social services, social housing and defence. In almost every case the key issue is not policy analysis but rather governance. Our public service finds itself on the edge of a revolution with almost none of the tools that it most needs in order to negotiate the next 10 years.

Using open policy development to anchor reform

The logic of my argument is that the entire policymaking process is going to be subject to intense pressures for change. It needs to be more efficient and have better incentives and it needs an injection of energy because the world is changing fast. The model of a large standing policy capacity available just in case the government needs it is the product of a time when money was easy. It is no longer applicable. As an incoming government, we found ourselves needing to use a different model in order to get clarity and results. We have been trying a different policy approach. Instead of relying exclusively on the public service, we have used a combination of officials, academics and private-sector experts. As an example, consider the process we have used for our tax changes.

If you imagine the political risks in putting up a GST, which we did, how then did we find ourselves in a position where we are yet to lose our heads over it? The answer is that we used a combination of expertise to enlighten a public service that had previously been too sealed off from the rest of the world. We succeeded, in other words, by using a very open process of making policy.

At the start of 2009, we decided to look at the tax system and not to do it behind closed doors. We created a ‘tax working group’ led by Victoria University in

Wellington and comprising academics, private-sector experts and officials—but not headed by an official or by a politician. We did not prescribe what they may or may not look at; we gave them very broad parameters. The key instruction we gave them was that every week or two they had to publish their work. This they did, publishing working papers, deliberations and minutes on the Internet, covering the wide range of topics on tax reform that reflected their very wide brief.

This real-time publication generated a high degree of media interest and diminished the role of the politicians to nothing more than keeping an open mind. To illustrate this, when the media, upon reading the first publication, asked the Prime Minister which dreadful things he had in store, his response was firm: 'Well, we're not ruling anything out.' This was probably the most critical moment in our policymaking process thus far in this term, as it subsequently enabled a high level of public discussion among the media, commentators and bloggers. In the end, after determining the problems and short-listing the potential solutions, it actually generated a consensus about which response the government would make, so that by the time we announced our solution—an increase in the GST—there was no backlash, as the many thousands of people who had participated in the public discussion could understand the reasons for it and expected it.

The government is increasingly using this kind of open policy development. Recently, we published the latest report of the 'welfare working group', which has been looking at our long-term welfare problems, including issues surrounding welfare beneficiaries and social housing. The group, which includes no officials, will next meet with the social-housing sector, and after their findings are published, we will make some decisions. Even though the social-welfare sector traditionally votes overwhelmingly against the National Party, they are giving us rich and positive engagement because they can see that we are taking the issue seriously and are listening to what they are saying. Indeed, what most people at the coalface have to say is very sensible—once they forget which party you are from. They are usually extremely frustrated by their inability to meet the needs that they see as immediate.

The only specific demand we made of the welfare working group was to ask them to determine what the problems were and what kind of changes we might need to make—ranging from how the relevant institutional arrangements interface with government through to how those affected fit into their broader communities. We put together a very challenging group of people who covered the full range of ideological views.

With this form of open policy development, the barrier for entry into the process is now zero. Anyone can access nuanced policy analysis within an hour on any topic you can think of in a way that when I was a junior official took two or three people in a team several months to assemble through a literature review. The barriers to entry are very low because access to stores of knowledge is now virtually costless. But what is more important than the knowledge is the feedback loop, and this is something the public sector is going to have to learn quickly, because if we do not get into feedback loops then those loops will just go around us. Governments coming into power will, as we did, create a loop outside, because there is nothing like the experience of opposition to teach you about this. Having spent three terms in opposition, by the time we came to power we had assembled more than 100 specific undertakings, a multi-billion-dollar tax-cut package, and a detailed first 100-day plan. We did all this with three policy advisors.

The key point here is that we do not need a big policy infrastructure to generate credible policy. The public service—certainly in New Zealand—will find that as the fiscal constraints begin to bite, it will be competing with good-quality, cheaper options for policy advice. Of course, good policy advice is underpinned by those ethics that are at the core of the public service—the professionalism, the institutional knowledge and the inherent continuity—but not at any cost. That is going to be the challenge of the next five years or so. We have learned from our experience that an externalised process with immediate, real-time feedback loops can generate high levels of energy in a policy process. Fast learning by politicians and officials provides a strong focus, and ultimately builds political support as much by the way you do the policy as by the results themselves.

Conclusion

In conclusion, the past decade was largely one of complacency. An excess of cash and confidence was ascribed to the public sector, not just in New Zealand but in most developed countries. The results of this largesse of cash and confidence are not overly impressive. Government is bigger but core social problems remain intractable; voters are sceptical that their cash was well used. The benign economic conditions of that decade will not occur again in our professional lifetime. But has the way we think about public services and public policy changed as much as the world has in the past two years? The answer is no, not yet. Our thinking will have to change.

In New Zealand, we have chosen a path of considered and consistent change over time, rather than rapid restructuring. We have engaged with the leadership of the public service because we believe they have the capability and the sense of mission to make the changes that will be required. I am confident that if we use the tools available plus a wider range of resources alongside the public service then New Zealand will succeed in this new era. There is also a moral dimension to this: we have a large obligation to the next generation. Remember, there will be fewer of them coming into the workforce as we leave it. The cost of inertia and inaction—at least in the New Zealand economy—will be a double burden for a society with not only an ageing population to support but also large public debt as a legacy of the past couple of years. We owe it to those young people to pay our own way, to pay our own bills as we go, rather than leave them with two lots of bills that they might believe they do not deserve. And because we owe it to them to pay our own way, we need to innovate, take risks and push the boundaries. The clock is ticking.