The Treasury

Budget 2024 Information Release

September 2024

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Post Election Preparedness: Implementing a social investment approach

Summary

This paper does not attempt to set out detailed advice on specific aspects of implementing a social investment approach, but rather to cover the field of broadly what we would expect the Treasury to need to advise on. This sets out some key elements and assumptions required for implementation to develop a coherent view of how the pieces need to fit together, so that we can quickly respond to the Minister's needs without our advice being piecemeal. There are four sections.

Setting the direction

The first conversation with an incoming Minister will need to be about what their objectives are for social investment and the scope of expenditure they want to include. This will help prioritise effort for further advice, set the pace and determine what levers need to be applied.

Funding and finance settings

Advising on funding settings for implementation will be a key role for the Treasury. Assuming the Government wishes to take a multi-dimensional approach, this will need to include:

- **Getting into baselines**: Setting expectations for key existing areas of agency expenditure to apply an investment approach. This will be complemented by spending reviews where they cover agencies with areas of expenditure amenable to an investment approach.
- **Budget process**: Evolving the approach over time from an initially narrow top-down focus to including more organisations and areas of expenditure with enhanced evaluation and evidence requirements.
- **New funding models**: Considering new funding and commissioning approaches to better support collective impact investment that works across agency silos.
- **Social impact bonds**: Under some conditions, there are benefits to alternative financing mechanisms to support social investment. For bonds to be successful, there will need to be substantial consultation with both providers and the market, and a flexible approach to structure and risk allocation that fits specific circumstances.

A proposed operating model

We propose a relatively decentralised approach to implementation based on clear roles and accountabilities for different aspects of the system. The proposed roles have been discussed with SWA and other Central Agencies and there is general agreement, though still a lot of detail to work through depending on the scale of different aspects. This approach supports efficiency by utilising existing capability and avoiding duplication. Some aspects of the operating model are scalable and can be expanded

over time, which will help manage upfront cost and ensure value-for-money when investment is made.

Timeline for implementation

We have developed a proposed multi-year timeline based on a series of assumptions that can be adapted based on initial discussions. This attempts to balance the need to make early progress and signal direction alongside the constraints of capability and the complexity of some of the proposals.

Next steps

- We should seek initial discussions with advisors of the incoming Government to get a steer on what advice is wanted upfront from the Treasury, SWA and other Central Agencies, and the desired pace of implementation.
- From there we would likely prepare some A3s or slides to support an initial conversation with the MOF focused on objectives, scope and implications for Budget 24.
- We should then follow up with Treasury Reports on more detailed aspects. As there is a potentially large volume of advice required to fully cover social investment, we should work with advisors and secondees on the phasing of this to focus on decisions that must be made early.

Setting the direction for social investment

Investment strategy

Key points and recommendations:

- The first decision required is to identify the outcomes you want to achieve through a social investment approach. This will determine priority groups and focus areas of expenditure, and which levers are most appropriate.

Social investment is about improving the lives of New Zealanders by applying rigorous and evidence-based investment practices to social services. Key features of the Social Investment Approach include:

- Setting clear and measurable outcomes and goals.
- Using data and information to identify:
  - the drivers of the outcomes; and
  - the groups of pdeeople impacted by the outcomes.
- Using evidence of what works for which groups. Using feedback loops to make continually better decisions at all levels.
- Purchasing for outcomes, funding the most effective services (government or NGOs), encouraging innovation, and creating incentives and accountability.

A key early decision for Ministers is setting the strategic direction for the Social Investment Approach by **identifying the outcomes** you want to focus on and setting the goals. The outcomes sought by the Social Investment Approach could include:

- Reducing **fiscal cost** to government, by reducing the drivers of demand
- Addressing **social outcomes**, such as:
  - Long-term benefit receipt
  - Poor health
  - Low educational attainment.

Once the outcomes have been identified, there is a need to assemble the **evidence on the drivers** of outcomes. Some drivers will be **structural (systemic)** in nature, impacting a large and diverse number of people, for example:

- **New Zealand Superannuation** represents a significant fiscal expenditure to government at $21.6b pa, with almost 900,000 recipients, and
- **attendance rates** have been falling in schools over time, across all income deciles)[1].

Thematic Spending Reviews (rather than a Social Investment Approach) may be a more appropriate policy approach where the drivers of outcomes are structural in nature and impacting large numbers of people.

A Social Investment Approach is most suitable where evidence suggests that the drivers involve a **relatively small number of people**. The drivers of outcomes for the small target group may be multidimensional, complex, and interacting (depending on

[1] Though notably it is worse in low-decile schools.

the evidence). The goal may be to address the aggregate fiscal or social costs associated with the small group (e.g. violent offenders). Or the goal may be to address particular social outcomes that impact disproportionately on the small group (e.g. children with parents in prison). The target groups should be identified based on **clear evidence linking the outcome to the cohort of people.** This is important for the specificity and sensitivity of the targeting[2]. *Te Tai Waiora* provides some evidence for possible starting points for focus outcomes:

- **Multiple disadvantage**: about 5% to 10% of the population are experiencing poor outcomes in at least four areas, such as such as poor mental health, or low skills, or unaffordable housing.
- **Declining trends**: growing numbers of children are reaching age 15 without even basic levels of literacy and numeracy; teenagers and young adults have rapidly increasing levels of psychological distress; our rental housing is among the least affordable in the OECD.
- **Low life satisfaction**: segmentation analysis suggests mental health, low income, low trust in institutions and problems with neighbourhood crime are some of the factors that explain low life satisfaction.

The ability to take an evidence-based approach to the drivers of fiscal costs and social outcomes will **develop over time** as we learn more from evaluations, the system adapts, and culture shifts. For Budget 2024, we would recommend new spending be focussed on manifesto commitments which are amenable to a social investment approach and existing priority outcomes for the Government. It is important that these interventions be modest in scale now, to allow space to identify other, higher priority groups in the medium-term as the evidence base improves.

There are trade-offs between addressing urgent, presenting social issues where bad outcomes are occurring now and early intervention approaches which may take years or decades to produce the ultimate desired outcomes. In addition, the earlier intervention occurs, the more difficult it will be to target population groups likely to experience poor outcomes. You may wish to consider balancing the timing and targeting of interventions in setting objectives.

Setting targets

Key points and recommendations:

- The Treasury can play an important supporting role to PSC and DPMC in advice on suitable Better Public Services targets, including for social investment.
- There are a range of potential perverse outcomes to mitigate and we would want to work with Central Agencies to provide further advice once objectives have been set.

[2] i.e., avoiding false negatives (people who need help but miss out) and false positives (people who are given interventions but who are not the most in need).

We expect DPMC and PSC to lead in the development of Better Public Services targets covering key Government priorities across the public sector, including social investment. The Treasury's role is likely to be:

- providing advice on the possible areas and ways of measuring a possible target
- providing joint advice on the process for establishing and monitoring targets
- providing advice on how targets relate to the Budget process; in particular the Wellbeing Objectives required under the Public Finance Act
- providing advice on how targets fit in the overall public accountability performance reporting system, and
- supporting the ongoing monitoring of the targets.

Targets can be used to:

- Clearly signal Government priorities (as such they should be limited in number)
- motivate public servants by creating a sense of purpose around a worthwhile objective
- create a sense of urgency to address a problem (targets are less effective in improving good performance), and
- create a shared sense of purpose, especially when a collaborative approach is needed to achieve the objective.

However, targets when not designed well can lead to:

- a narrowing of focus resulting in "hitting the target but missing the point" (for example; teaching to test, focusing on getting those close to the line across the line, focusing on quantity over quality), and
- gaming through the manipulation of data and actions in order to be seen as achieving the target.

Accordingly we would recommend the Treasury work with Central Agencies to provide further advice on targets for social investment once objectives and key focus areas of expenditure have been decided, alongside advice on broader targets for the public sector.

Measuring results

Key points and recommendations: • A range of improvements to measurement processes and techniques will be required. • The Treasury can help drive improvements through requirements of the Budget process and Spending Reviews.

The impacts of Social Investment policies must be measured to ensure they align with their intended objectives and deliver the anticipated outcomes. Different processes and techniques can be used, and their suitability depends on the specific policy being evaluated. They can be roughly grouped into three categories: monitoring, impact evaluation, and microsimulation models (including actuarial models).

Figure 1: Measurement approaches to support social investment

Monitoring	Impact Evaluation	Modelling
Tracks the policy implementation and outcomes. **Includes:** • Data collection on project activities, processes, outputs, and outcomes. • Use of indicators for progress tracking. **Pros:** Allows for timely adjustments, ensures that implementation is aligned with design, enhanced efficiency. **Cons:** Outcomes, not impact on outcomes.	Comprehensive assessment that attempts to establish a causal relationship between the program and its outcomes. **Includes:** • Evaluation methodologies (e.g., RCTs, quasi-experimental). • Integration of quantitative and qualitative data. **Pros:** Insights on intervention effectiveness and future policy decisions. **Cons:** Not timely	System level valuations of lifetime costs and/or social outcomes **Includes:** • Actuarial modelling of system level valuations of lifetime costs. • Microsimulation models to estimate the impacts of different scenarios on various outcomes. • Identifying at-risk populations • **Pros:** Aggregate impacts of system level changes, comparing scenarios, identifying high-risk groups. • **Cons:** Models can be a "black-box".

Figure 2: Application of different measurement approaches

Example:

An intervention that aims to transition individuals from government benefits into employment

Monitoring:

Track expenditure/budget, program participation, and benefit exit rates (i.e., was the programme implemented as designed).

Impact Evaluation:

Examine if participants were more likely to be in employment after a specific period than if they had not participated in the programme.

Modelling:

Actuarial models would not look at this programme in isolation but could estimate the lifetime costs of individuals currently receiving government benefits and attempt to isolate the impact of aggregate policy reforms.

Setting evidence and evaluation standards
Evaluation capability across government agencies is varied. [33]

Treasury's Role in improving measurement
Treasury can play a role in implementing a Social Investment approach by elevating measurement standards through the Budget cycle. This role can promote the consideration of long-term societal concerns, the assessment of funding proposals, the continuous monitoring of initiatives, and the enhancement of cost-effectiveness evaluation tools (e.g., CBAx). However, as discussed below, any improvements to measurement standards will have to be implemented incrementally, considering capability and capacity constraints. There are four key aspects:

- **Setting Budget Strategy**: At the start of the budget process, one of the primary challenges is to ensure that long-term issues receive as much consideration as short-term, politically significant matters. In a social investment approach, it is essential to take a forward-looking view and prioritise investments that will yield long-term societal benefits.
- **Ex Ante Evaluation of Funding Proposals:** The Budget process involves the evaluation of funding proposals to determine which initiatives should receive financial support. In the context of social investment, it's crucial to assess the potential impact and relative cost-effectiveness of proposed programs. Treasury could apply agreed standards for the quality of evidence supporting Social Investment initiatives. This may also involve the use of cost-benefit analysis to assess and compare expected impacts on outcomes across different initiatives.
- **Ex Post Monitoring of Funded Proposals:** Once initiatives are funded, it is critical to monitor their progress and assess whether they are achieving their intended outcomes. The Budget process should incorporate mechanisms for ongoing evaluation and feedback loops that allow for course corrections. In addition to standard requirements of the Public Finance Act, the Treasury has developed the capability to monitor expenditure and performance measures for a limited number of specific initiatives below the appropriation level. This was developed for monitoring the Climate Emergency Response Fund (also the North Island Weather Events and Green Bonds) but could be reprioritised to focus on other priority areas of expenditure.
- **Strengthening Monitoring and Evaluation:** The Social investment approach aims to enhance the monitoring and evaluation of initiatives to ensure they deliver meaningful outcomes. The Budget process must encourage the development of incentives and capabilities to evaluate and continuously improve the effectiveness of expenditure across the entire budget, rather than just focusing on marginal changes.

Institutional settings

We expect the Minister for Social Investment and Minister of Finance to lead on social investment. This would be complemented by including some key social sector Ministers where there is expected to be a significant focus on social investment within their portfolios. We would recommend keeping the group small (i.e. three to four Ministers total) in order to drive implementation with clear expectations. As the group of Ministers and associated agencies grows, the focus will become more dispersed and coordination will require more resourcing, which risks slowing down implementation.

We would expect the Cabinet Social Wellbeing Committee (or its successor) to be the key group supporting the authorising environment for social investment Ministers. Other Cabinet Committees may have an interest in some aspects of the work, particularly how it is supported by reprioritisation or relates to Budget strategy.

There is also a potential role for Select Committees in providing scrutiny of agency progress against any objectives or targets that have been set as part of implementing social investment. The Review of Standing Orders 2023 included substantial changes to the scrutiny process, and there is potential for this to apply an additional layer of independent assessment of accountability for delivery.

Funding and finance settings to implement social investment

Funding and finance settings are a key mechanism for implementing social investment. We recommend a multi-pronged approach to address multiple Government objectives efficiently, and to progressively address capability constraints. There are four broad levers to drive implementation:

- Getting better value from baselines
- The Budget process
- New funding models
- New finance models.

Getting better value from baselines

Key points and recommendations: • Increasing the use of evidence to drive reprioritisation within agency baselines has potential benefits for both outcomes and fiscal strategy. • At the agency level: implement an investment approach for target areas of expenditure to improve the evidence base and support agency reprioritisation. • At the central level: use spending reviews as a check on the quality of agency processes, and to release funds for reallocation through Budget.

Implementing your broader fiscal strategy will require substantial reprioritisation. In general, social investment will not produce large-scale savings quickly to meet short-term fiscal objectives and there are other tools for achieving these objectives [XXXX paper on Implementing Your Fiscal Strategy refers]. However, applying a social investment approach has the potential to drive reprioritisation to improve outcomes in specific areas and/or to support innovative approaches that require looking beyond agency silos. An effectiveness-based approach to reprioritisation of baselines requires answering two key questions:

- Does sufficient evidence exist to assess the value-for-money of baseline expenditure?
- Is expenditure higher or lower value-for-money than other expenditure in the agency or other agencies?

Some areas of agency expenditure are amenable to putting in place systems of setting investment objectives, portfolio approaches to services, and strong evaluation programmes to drive reprioritisation within a portfolio. In addition, ongoing programmes of spending reviews may release funds to be added to Budget allowances and reallocated. However, without a sufficient evidence base, even resource-intensive spending reviews will struggle to assess the impact of savings options, which will make it difficult release funds without creating significant risks. Using an investment approach to improve the value of baseline expenditure should therefore be implemented at two levels in order to have the best chance of success:

- **At the agency level**: Identifying target areas of expenditure within selected agencies to improve the evidence base. While there are pockets of good evaluation and investment practice, there is significant potential for improvement. Target areas could be selected on the basis of particular outcomes you want to improve or where there are questions about current value-for-money.

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It is important that the focus for whether funds are returned to the centre is on whether adequate processes are in place to assess the value for money of expenditure, and whether agencies are acting on that evidence, **not** on whether there is evidence of poor value-for-money within a given portfolio. Focusing on the latter will quickly disincentivise agencies from undertaking any evaluation or ensuring evaluation is good quality.

Alongside structures to drive reprioritisation, we will need to set expectations for how improvement is to be driven for different areas of expenditure. This will need to be tailored to the nature of the services and what evaluations say about what is driving variation in effectiveness. For example, when there is greater variation within programmes than there is between them, we will get greater improvements in value-for-money by improving the quality of delivery and targeting than by stopping programmes to invest in marginally more effective ones.

Table 1: Approaches to improving outcomes in response to different evidence

	What evaluation is telling us	**What action we should expect to see**
What works:	Variation between different programmes in a portfolio seeking the same outcomes.	Divest/reprioritise from ineffective programmes into more effective ones.
Who works:	Variation between different providers of the same or similar programmes to the same cohorts.	Leverage competitive tension (including between govt/non-govt providers). Exit contracts with low-performers.
How it works:	Variation in results within programmes regardless of the provider.	Set standards, drive improvement in professional practice.
When it works:	Not yet evidence to determine whether a programme is effective or not.	Use time-limited funding and conditional drawdowns of contingencies to hold agencies to account for evaluation results.

In addition to what the evidence is saying, the approach to continuous improvement for these target areas of baseline expenditure will need to take into account some practical considerations:

- **Provider capacity**: Where alternatives are limited, there will be a need to work with providers to improve results rather than just exit contracts.
- **Provider relationships**: Too much tension in contracting may distract from a focus on what is needed to improve impact.
- **Balancing the portfolio**: In some areas and for some cohorts, it may be difficult to get results and/or we have little knowledge of what works. There needs to be some tolerance for failure in order to ensure innovation continues, and to avoid an excessive focus on easy wins.

Overall, we should expect some expenditure in the target areas to be ineffective. What matters is whether there is an explanation as to why the ineffective expenditure remains, and a coherent plan to drive improvement. This is important to getting the right incentives in place to drive improved evaluation

Budget process

Key points and recommendations:

- While the Budget process is a strong lever, it has the drawback of only applying to 'new' funding.
- Timelines for Budget 2024 are tight, and you are unlikely to get quality proposals with open bidding. A top-down process, focussed on a subset of your manifesto commitments which are amenable to a social investment approach, is likely to get the best results.
- Following Budget 2024, we recommend you work with Budget Ministers, the Treasury, and the Social Wellbeing Agency to identify the key outcomes you want to focus on as you continue to implement a social investment approach. The identification of these outcomes and subsequent development of initiatives to achieve them requires substantial lead time.
- [33]
- [33]

Managing social investment within allowances

In recent years, there has been a marked increase in the number of thematic funds created and managed outside allowances (for example, the Climate Emergency Response Fund and the COVID-19 Response and Recovery Fund). These funds link priorities with funding decisions and are useful for ringfencing funding for investments which may otherwise be deferred or crowded out by short-term pressures. However, such funds undermine the Fiscal Management Approach which relies on allowances as the primary tool for ensuring fiscal control and emphasises the importance of trade-offs to ensure that initiatives with the highest value for money are funded. In general, experience internationally is that most forms of hypothecation lead to increased Government expenditure due to this reduction in the salience of trade-offs. We therefore recommend that in general such funds are managed within the allowance framework. If there is to be a separate social investment fund established, we recommend that it be kept small, with a clear scope and performance objectives that are defined by its underlying rationale (for example, targeting areas poorly-served by agency silos and where devolving decisions improves effectiveness).

Social Investment and Budget 2024 Design
We understand you wish to incorporate a social investment approach into the Budget process. There are several ways to implement this:

- Through tagging initiatives as 'social investment' specific and introducing additional evidential requirements for these select initiatives (*Treasury recommended option*)
- As a separate track within the Budget process
- As a tagged contingency, to be drawn down by a commissioning agency when appropriate proposals have been identified
- A lump sum appropriated upfront with devolved management (i.e. a 'Social Investment Fund', discussed in the following section of this paper)

There is much greater timing pressure on Budget 2024 compared to a non-election year Budget process. Because the process will be more condensed, it is important to ensure the Budget is streamlined, and the informational requirements for initiatives are not overly complex. Adding a separate 'social investment' track requires early triage of initiatives which may not be possible at this stage given limited data availability and information on amenability to approach, especially given tight timeframes and limited public sector capability.

We would instead recommend a top-down approach in which you work with Budget Ministers, the Treasury, and the Social Wellbeing Agency to identify which of your manifesto commitments are suitable candidates for social investment, based on the outcomes and objectives you want to prioritise. Additional evidential requirements could be required for these initiatives (particularly ex-post monitoring arrangements), rather than imposing additional requirements on all Budget initiatives.

Implementation of a social investment approach will have to be start small and incrementally progress, given the time constraints for Budget 2024 and limited availability of a suitable evidence base to support proposed interventions. Past Budget exercises indicate that asking more from agencies does not necessarily lead to better quality submissions, particularly where there are capacity and capability issues at play. Instead, increasing requirements needs to be accompanied by targeted supports to build the quality of analysis[3] (e.g., workshops on how to conduct effective cost benefit analysis, improved monitoring and reporting to build an evidence base etc.). As capability and evidence builds, we can make better use of feedback loops to inform funding decisions and raise evidential requirements to a wider set of initiatives.

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Bringing third parties into the Budget process

We understand there may be interest in opening the Budget process to entities outside Government, such as iwi organisations and NGOs. There is a particular case for this for complex services, where costs and benefits may be split across portfolios, making it less likely that promising initiatives will be elevated by a sponsor agency if all the benefits fall on another agency. The main considerations for this are practical:

- **Capacity**: The Treasury could not assess the volume of bids that are likely to result from a totally open Budget process. This could be mitigated by using an invite-only process based on recommendations from the Social Investment Panel (or Ministers).
- **Capability**: Some providers may have good ideas for services but not the capability to translate these into investment-ready proposals that meet Treasury's requirements. This could be addressed by officials working with invited entities in the lead-up to Budget.

Putting these mitigations in place would make it possible, however we would expect there to still be significant resourcing implications for Treasury which could affect delivery of other priorities.

Driving improvement through Budget 2025

From Budget 2025, we recommend applying extra evidential/information requirements for social investment initiatives across the Budget (for example CBAx analysis, monitoring and reporting). All social investment initiatives should have:

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[3] A good example of where this two-pronged approach has been effective is the 2023 gender budgeting exercise. A small number of submitted initiatives were subject to additional informational requirements. Agencies were supported by the Ministry for Women to complete this additional analysis.

- A clear articulation of the outcomes sought (fiscal, economic), the nature of the problem (structural, micro) and appropriate delivery channel
- Evidence linking the target population to the desired outcomes, and
- The ability to apply a measurement framework to provide evidence as to whether funding is successful.

There are then two types of initiative to consider, for which there should be slightly different requirements:

- High confidence investments: Evidence that a programme is effective for the target population and can produce a positive ROI, or
- High-risk, high-reward investments: Innovative proposals with a strong evaluation plan and clear offramps associated with monitoring of implementation.

Strengthening Evidential Returns Over Time – Next Steps

In the long-term we recommend raising evidential requirements broadly rather than specifically for social investments, although when this is implemented will need to take account of rate of growth in capability and evidence bases over time, as agencies respond to the incentives of expectations for baseline expenditure and the Budget process. Treasury can introduce useful feedback loops to provide feedback to agencies about the quality of their submissions, and use this process to track quality over time. The use of Social Impact Bonds also has potential to drive greater discipline in evidence and measurement, and is discussed further in a following section of this paper.

New funding models

> Key points and recommendations:
>
> - In general, we do not recommend the establishment of 'funds' taken outside the Budget process, as the salience of upfront trade-offs will be reduced.
> - However, for areas where services and outcomes are complex, there may be merit in new approaches to funding. This could involve setting up special purpose vehicles or small funds that have a high degree of flexibility over outputs but are subject to strong accountability for outcomes.
> - There are also opportunities to build on existing changes to funding structures that give more flexibility to community-based organisations. However, community organisations are often reluctant to be subject to strong central accountability requirements, and sometimes lack the capability to collect and transmit useful data.

A Social Investment Fund

There are some merits to establishing a separate Social Investment Fund, especially where the interventions are novel, high-risk and high-reward. The Treasury is not resourced to support agencies with the development of evidence-based social investment initiatives; our role instead has instead been to provide second-opinion advice on the reasonableness of others' proposals. Moreover, because of timing constraints, it is unlikely that novel, well-developed social investment initiatives could be identified and funded through Budget 2024. Ministers could therefore set the Fund's goals and parameters and then the Fund's administrators could support the development of suitable initiatives. This could be either:

- A tagged contingency with drawdown conditional on report backs about suitable initiatives that have been identified (Treasury preferred option), or
- a lump sum appropriated upfront.

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Other funding models for delivery by non-government organisations
In addition to (or instead of) establishing a Social Investment Fund, Ministers may wish to consider using existing models of delivery by non-government organisations to address complex needs.

In general, the existing model for social sector funding assumes that suitable organisations exist and have the capability to deliver effective interventions, which does not always hold true. Community organisations have also raised concerns that decisions are too often made centrally, constraining their ability to effectively support people with multiple, overlapping needs; and that funding is too often short-term and rarely sufficient to build capability.

There have been some steps towards a more ‘relational approach’ – for example, the ‘social sector commissioning principles,’ and the proliferation of alternative contracting models, some of which are described below. These alternative models are rarely simply ‘contracting for outcomes,’ but generally involve a degree of joint decision-making, or permit non-government organisations to deliver interventions within specified parameters.

Treasury officials have previously noted that there are some good reasons for some decisions to be made by those closer to the ‘coalface’ (e.g., *Designing a new Collective Operating and Funding Model in the New Zealand Public Sector*, Warren 2021). However, it is already difficult to establish the effectiveness of community investment, and there remains value in Ministers having the information – and the authority – to take strategic decisions on government funding for the social sector.

Particular challenges are:

- Attribution (setting up interventions so they can tell us something persuasive about their effectiveness)
- Timing (benefits are not realised immediately), and
- Capability (the organisation’s ability to carry out the intervention and gather the necessary data to assess its effectiveness).

An appropriate balance between ensuring effectiveness and providing flexibility will require some iteration. However, there are some steps that Ministers could take relatively quickly in this area – for instance, identifying existing models that could take on a larger role.

Table 2: Existing flexible contracting models for potential expansion

Social sector commissioning:	In November 2021, Government agreed to adopt a 'relational approach' to commissioning. Seven 'social sector commissioning principles' were agreed following consultation with communities, community organisations, iwi and government agencies, and an 'Action Plan' was published in October 2022. This shift is meant to apply broadly.
Place-based initiatives (PBIs):	Under the previous National-led Government, three 'place-based initiatives' were established, in which funding was allocated to communities to procure locally targeted interventions. Two of these have continued (in Tairawhiti and South Auckland respectively), and have been broadly effective, albeit at a small scale. The idea is that place-based initiatives will be supported to scale up and build their capacity, after which they would be expected to seek ongoing funding from elsewhere (either new funding or reprioritisation).
Whānau Ora commissioning agencies:	In 2010, the previous National-led Government announced Whānau Ora, a whānau-centred approach to commissioning health and social services with the intention of localising funding decisions. Three commissioning agencies (Te Pūtahitanga o Te Waipounamu, Whānau Ora Commissioning Agency and Pasifika Futures) are contracted to fund and support providers to deliver services based on a set of overarching outcomes.

Table 3: suitability of different funding models for different areas of social investment

Delivery channel	**Confidence in investment**	**Type of services**	**Measuring performance**	
Government delivery of social services	Simple, observable outcomes from known outputs	Suits areas with a 'core' government role (or insufficient non-Government providers), relatively standardised services, large populations. E.g. Administering the welfare system.	Requires specification of expected service levels and monitoring of operational KPIs, with a focus on improving efficiency	
Contracting out	Clear relationships between outputs and outcomes	Suits areas with strong options for service provision and/or a need to tailor the approach. E.g. improving employment and social outcomes.	Contract performance specified on an output and/or outcome basis depending on measurability, with a focus on improving effectiveness	Suits delivery by line agencies
Outcomes-based contracting	Clear outcomes desired but limited knowledge of the outputs required	Potentially suits more complex services, including collective impact models requiring collaboration.	Ideally outcomes-based but attribution can be difficult, so in practice often centred on intermediate outcomes.	
Social investment fund or funds	Clear outcomes desired but limited knowledge of the outputs required	Enables a centralised portfolio approach to investing in a range of services targeted via populations rather than the services provided.	Fund performance assessed against outcomes at the portfolio level. Fund managers monitor individual investments.	Suits collective impact
Commissioning agencies	Complex and/or varied outcomes and outputs needed at the local level	Suits areas where Government has little knowledge of the services that are needed or how to reach particular populations.	Requires specification and ownership of the outcomes at the local level. E.g. Whānau Ora	

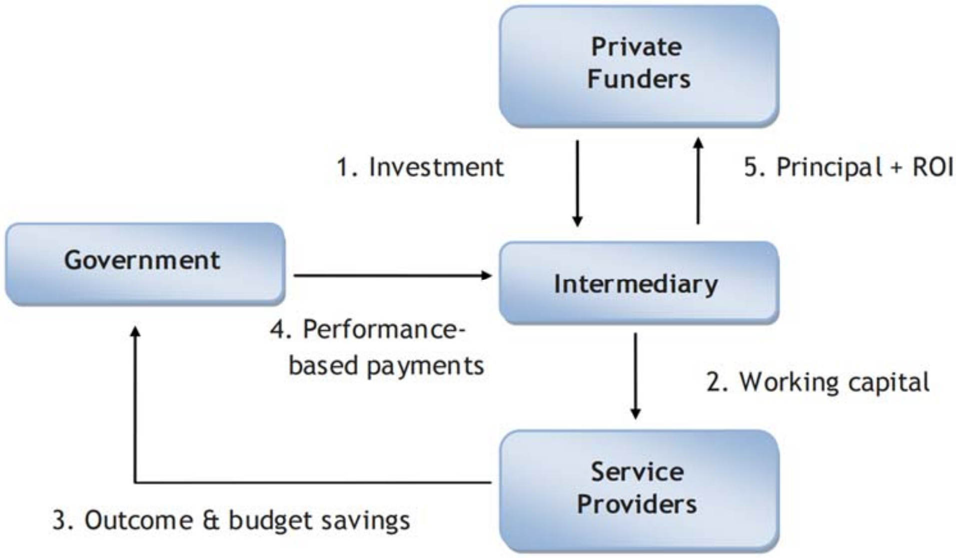
Social impact bonds – alternatives to Government finance

Key points and recommendations • Social Impact Bonds have the potential to drive innovative approaches to social investment, however they are only suitable under specific conditions for providers, markets and Government. • Social Impact Bonds are not an ‘all or nothing’ instrument, and there is a continuum of blended finance structures that could be tailored to specific objectives. • We recommend thorough consultation with both providers and the market to ensure the right conditions are met and the structure is appropriate to set implementation up for success.

A social impact bond involves:

- The government committing to make a payment based on meeting outcome metrics
- A private funder / investor providing up front funding on the expectation of receiving payment from government
- An intermediary which uses this up-front funding to enter into contracts with service providers, and
- Service providers providing services to an identified population.

Figure 3: Roles and relationships in a Social Impact Bond



Source: Social Impact Bonds: A Guide for State and Local Governments, 2013.

This approach to financing has several advantages compared with standard contracting models:

- It provides a strong incentive for all parties to focus on and achieve the intended outcomes.
- It makes use of private financing, reducing the level of up-front government funding required and potentially transferring risk to the investor.

- It can allow for greater flexibility and innovation in how services are provided. Intermediaries and providers can change how services are delivered and coordinated. This is particularly valuable where existing contracting approaches are restrictive for providers.
- Ability to leverage the skills of intermediary organisations. An intermediary may be better placed than existing service commissioners to contract with and coordinated service providers.

Several conditions are needed for an SIB to be viable to all parties, including:

- Clearly defined, timely and quantifiable outcome metrics. Often intermediate outcome metrics are used due to the lag between service delivery and changes in the intended outcome. However, these need to be carefully selected to ensure they are strongly related to the ultimate outcome and don’t create perverse incentives.
- Strong evidence that the programme or service can improve outcomes. Without strong evidence, private investors may not be willing to take on the risk of the programme failing to deliver. While this can be a barrier to using a SIB, it also has a positive selection effect, filtering out programmes and providers that investors are not confident in.
- Strong evidence that, if effective, the programme will result in fiscal savings to the government. While a programme may be effective at improving outcomes, it needs to provide greater value-for-money than existing services to cover the additional fixed cost of establishing an SIB.
- Investor interest, understanding and capability. This will be a particular challenge initially due to the relatively thin capital markets and limited experience with SIBs in New Zealand.

SIBs exist at one end of a spectrum of funding and financing tools. Where a SIB may not be feasible (e.g. due to limited investor appetite to take on risk), alternative options are available, including:

- Contracts directly with providers with outcomes-based payments. These can be useful when there is no need for an intermediary (e.g. there is no need to coordinate multiple services).
- Blended finance options. These are similar to SIBs but the government provides up front funding for a share of the programme’s operating costs, in addition to payment based on outcomes. This retains an outcome-based incentive but reduces the level of risk taken on by the investor.

Establishing a SIB can require high upfront costs, specialist capability and can take significant time to set up. For example, while the New Zealand social bonds procurement pilot was launched in late 2013, the first social bond was not agreed until 2017.

To ensure a SIB is viable for all parties, we suggest a staged engagement approach before establishing an SIB. At each stage, there is an opportunity to consider a SIB is the best approach or whether alternative contract or funding models would be more appropriate:

- **Engagement with providers**: This will help understand the level of capability among providers, the challenges they face with existing contracting models and whether a SIB be effective in that area. While a SIB may be useful in some areas, in other areas there may be other interventions that can support providers faster and more effectively than an SIB.
- **Defining the outcome metric**: For payments to be based on an outcome metric, it must be measurable, timely, reliable and strongly related with the ultimate intended outcome of the programme. There also needs to be a clear plan for how this outcome will be measured as the programme is delivered (e.g. using existing administrative data sources or additional data collection) and how an appropriate counterfactual will be defined (e.g. a control / comparison group or historical baseline data). Where there is no outcome metric that satisfies these requirements, other contracting approaches would be more appropriate.
- **Rigorous cost-benefit analysis**: Before the government or investors are willing to provide funding, all parties need to have confidence that the programme can improve outcomes at a lower cost than existing services.
- **Engagement with investors**: Given the thin capital market in New Zealand and limited experience with SIBs, a range of options should be developed, such as bonds of different sizes and different levels of blended finance. If investor appetite is limited or investors require such a large return that the SIB no longer makes fiscal sense to the government, direct outcome-based contracting approaches can be used as an alternative.

A Proposed operating model for implementing social investment

Aligning System Roles

The incoming Government has suggested a model under which the Social Investment Agency provides a system-wide leadership role in implementing the investment approach. We support this approach but note there are core - and potentially overlapping - functions of Treasury and line agencies. Alignment is needed to manage resources across the system, drive efficiency, and prevent duplication.

Role of Treasury

The role of the Treasury could be centred around its existing core functions and capabilities. There would be some marginal impact on capacity that would have to be managed in line with other Government priorities:

- Promote/require use of evidence through Budget processes (e.g. set standards that promote evidence and evaluation).
- [33]
- Advise on establishing the range of funding settings for different social investment programmes (across the spectrum of contracting for services, commissioning entities, funds and Social Impact Bonds).
- Undertake spending reviews that include assessing agency evidence bases against standards set by the cross-agency expert group on evidence standards convened by SWA.
- (Potentially) monitor expenditure and performance for significant initiatives and/or a social investment fund.
- (Potentially) support the development of capability in the use of Social Impact Bonds.

Role of SWA

SWA could have a significantly expanded role building on existing strengths in analysis and evidence. All roles except administering a fund are in line with existing capabilities and are relatively scalable (for example, a 'what works' centre could range from a few FTE aggregating work done by agencies to a full-scale research hub). Administering a fund would require several new capabilities in procurement, legal, contracting and relationship management:

- Provide data/analytics central function to understand from IDI and other sources of data and evidence who and where needs support.
- Establish a 'what works' centre for social sector (incl. synthesising evidence, bridge to academia).
- Convene a cross-agency/academia expert group to set standards for impact measurement, and provide assurance and advice to agencies doing evaluations.
- Determine and support agencies' requirements for infrastructure and tools (e.g. data and analytics assessment and support).

- Provide full secretariat for governance groups (incl. strategic advice).
- Identify priority areas for baseline spending reviews (joint work with Treasury and agencies, with Treasury setting overall timelines and agencies undertaking the work).
- [33]

Role of Social Agencies

Social agencies will have varying levels of capability and capacity to implement social investment. New expectations are in line with what could be considered core roles, but would likely require reprioritisation, which may be challenging in cases where they are already undertaking reprioritisation to manage cost pressures and decreasing baselines.

- Implement investment approach methods/principles, as appropriate to agency.
- Promote evidence-based practice consistent with guidance and oversight from cross agency expert group convened by SWA (e.g., build capability to interpret and use evidence at the front line, mandate and support evaluation and measurement in contracts – at least 5% of grant).
- Build monitoring, evaluation and impact measurement into all stages of programmes – from programme design to tracking outcomes beyond programme participation.
- Directly purchase and fund service providers, building on and aligning with social sector commissioning work programme.
- Complete reviews of baseline spending, consistent with timing and process set by Treasury.
- Submit funding bids consistent with standards set by SWA (social investment fund) and Treasury (Budget).

Setting SWA up for Success

It is critical that system wide resources and capability, especially SWA's, are sufficient to meet Government's expectations. This means being clear about which functions are needed and can be delivered in the near-term, which might be built over time, and which already exist – but may need modifications. A 2018 analysis related to the factors associated with success and failure of various New Zealand public research institutions is informative.[4]

The analysis distinguishes between two types of organisations – those that engage directly in social research with its in-house staff and those that have a primary or major function of commissioning outside researchers to carry out specified social research projects. Our understanding is that SWA is intended to perform both functions, though it may be preferable to focus on the central/coordinating/commissioning role in the near-term.

Success factors for social research institutions, as detailed in the report, include

[4] Whom-the-bell-tolls-030418-WEB2.pdf (swa.govt.nz)

competent professional staff, good management, and adequate resourcing and critical mass for the size of the task they faced. In addition to these baseline factors, successful institutions also displayed:

1. a clearly defined field of research
2. well identified research priorities - Closely related to the first factor is the need to produce research which meets the needs of its clients, either the government directly or the public sector agency commissioning the research or providing the grants
3. a stable long term funding model, at least for baseline funding
4. effective relations with the departmental policy and social service delivery agencies

Failures identified in the analysis included:

1. Attempting to cover too many different areas of social research
2. Not providing the type of information and advice wanted by the government of the day, or providing information or advice at odds with their policy direction
3. Lack of an adequate long term base funding arrangement

Ministers should be clear of the role of SWA relative to other entities, give as much direction as possible on the focus areas, and provide sufficient funding for involved parties to fulfill their intended role. It will take time to develop, understand, and build confidence in the system, therefor we recommend starting modestly and building over time [more to come based on SWA's self-assessment].

A proposed operating model for implementing social investment

Incoming Government

- Set governance arrangements and ensure adequate resourcing
- Decide respective roles for budget process, Social Impact Fund, and Social Impact Bonds as funding and financing mechanisms
- Decide role of Better Public Service-style targets and set specific targets
- Identify desired outcomes and priority populations

Overarching Framework

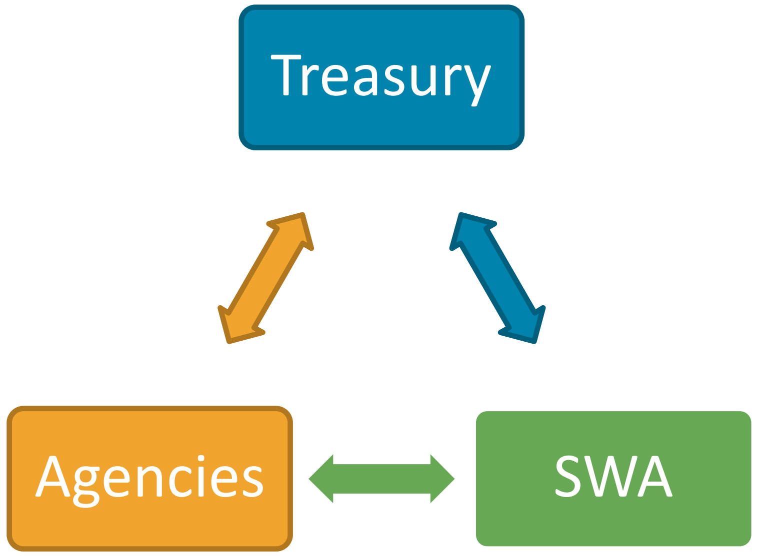
- We suggest a decentralised approach, with three key entities: the Social Wellbeing Agency (SWA), Treasury, and agencies that deliver social services
- This enables agencies to build on existing data and analytics infrastructure, with SWA taking a role in direction setting and supporting smaller agencies with less capability

Treasury

- Promote/require use of evidence through budget processes (e.g. set standards that promote evidence and evaluation)
- Convene a social investment panel to assess investment choices (including advising government on whether to support new initiatives or continue pilot programmes consistent with identified priority populations and targets). This could advise on budget choices, as well as on a future pipeline of investments
- Advise on establishing the range of funding settings for different social investment programmes (across the spectrum of contracting for services, commissioning entities, funds and Social Impact Bonds)
- Undertake spending reviews that include assessing agency evidence bases against standards set by the cross-agency expert group on evidence standards convened by SWA
- (Potentially) monitor expenditure and performance for significant initiatives and/or a social investment fund
- (Potentially) support the development of capability in the use of Social Impact Bonds

Agencies Delivering Social Services

- Implement investment approach methods/principles, as appropriate to agency
- Promote evidence-based practice consistent with guidance and oversight from cross agency expert group convened by SWA (eg, build capability to interpret and use evidence at the front line, mandate and support evaluation and measurement in contracts – at least 5% of grant)
- Build monitoring, evaluation and impact measurement into all stages of programmes – from programme design to tracking outcomes beyond programme participation.
- Directly purchase and fund service providers, building on and aligning with social sector commissioning work programme
- Complete reviews of baseline spending, consistent with timing and process set by Treasury.
- Submit funding bids consistent with standards set by SWA (social investment fund) and Treasury (budget)



Central Social Investment Agency (e.g. SWA, SIA)

- Provide data/analytics central function to understand from IDI and other sources of data and evidence who and where needs support
- Establish a 'what works' centre for social sector (incl. synthesising evidence, bridge to academia)
- Convene a cross-agency/academia expert group to set standards for impact measurement, and provide assurance and advice to agencies doing evaluations
- Determine and support agencies' requirements for infrastructure and tools (e.g. data and analytics assessment and support)
- Provide full secretariat for governance groups (incl. strategic advice)
- Administer cross-system Social Investment Fund (incl joint work with Treasury on any Social Impact Bonds)
- Identify priority areas for baseline spending reviews (joint work with Treasury and agencies, with Treasury setting overall timelines and agencies undertaking the work)

Role of Other Entities

- ***Public Service Commission***: Advise on streamlined governance and coordination structure; consolidate and report on outcomes and targets relevant to Government's social investment objectives
- ***Department of Prime Minister and Cabinet***: Promote use of evidence through Cabinet processes, align work of Implementation Unit and Child Wellbeing and Poverty Reduction Group
- ***StatsNZ****:* Manage cross-agency data infrastructure; facilitate access and sharing; oversee compliance with ethics, governance, stewardship standards; collect statistics and outcome measurements relevant to Government's social investment objectives; leadership on Māori rights and interests; bridge to academia on IDI use
- ***Population Agencies****:* Support the provision of evidence from range of different sources (e.g. to complement evidence from IDI) and work across system to provide advice on how to implement, monitor and evaluate culturally-specific adaptations within social investment framework
- ***Chief Science Advisors***: Provide high quality, independent scientific advice; actively link government and academia
- ***Consultants and academics***: Meet market need, validate approach/rigor of evidence. Possible participation in cross-agency working group
- ***Service providers*****:** Signal capacity/constraints and community needs; provide data for evaluation purposes and respond to evidence to create feedback loops
- ***Private sector****:* Signal areas of interest for investment; contribute to investment pipeline work

What can be delivered when?

The following timeline assumes:

- There is a desire to include at least some social investment elements in Budget 24 as a signalling exercise, despite the compressed timeframes.
- A Social Investment Fund is to be established, and Ministers are satisfied that the benefits outweigh the impact on the Fiscal Management Approach.
- Ministers agree on the respective roles of Treasury and SWA in setting and enforcing standards through spending reviews and the Budget process.

[33]