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Introduction

The subjects dealt with in this report cover some of the more diverse parts of the Audit Office's interest in how public money is spent. Four of the articles touch (directly or indirectly) on some of the largest areas of annual Government spending – health, education, and information technology. The fifth article – on “impact evaluation” – potentially touches all areas of Government spending.

Health Sector

As we foreshadowed in our *Fourth Report for 1999*,¹ this report contains articles on:

- A further review of the financial condition of Hospital and Health Services (HHSs) (pages 9-24). On the whole, the financial condition of HHSs improved markedly in 1998-99.
- Capital purchasing by HHSs (pages 25-42). Generally, the practices and procedures applied to the selection of purchases that we examined were of a good standard. However, we observed room for improvement in some areas.
- The project to change from a manual to an electronic system of processing claims for pharmaceutical service subsidies and dispensing fees (pages 43-68). The original aim to have full electronic claiming in place by 30 June 1999 was not achieved, and is still to be achieved. The new system was to be run from a single processing centre in Wellington, but the Government has just announced that the Wanganui processing centre is to remain in operation.

Large Information Technology Projects

The fourth article (on pages 69-78) is a summary of the key messages from a detailed report that we will publish shortly on the subject of *Governance and Oversight of Large Information Technology Projects*. As has been widely publicised, some recent IT projects have involved spending large amounts

¹ Parliamentary paper B.29[99d], page 7.

of public money without producing a successful outcome. It is time to take a look at ways of minimising history's propensity to repeat itself.

Education Sector

The fifth article (on pages 79-98) discusses what we see as difficulties – for both school boards of trustees (school boards) and the Audit Office – with the accountability requirements of the Public Finance Act 1989 and the Education Act 1989 and suggests some changes.

School boards are the most numerous type of Crown entity. The number fluctuates as schools open or close or private schools integrate into the State system. At 31 December 1998 there were 2,669, and by 30 June 1999 there were 2,664.

Collectively, school boards spend a significant proportion of the money voted annually by Parliament for education. Thus it is appropriate that, as Crown entities, school boards are subject to the accountability requirements specified by Part V of the Public Finance Act. However, other (not necessarily consistent) accountability requirements are imposed by the Education Act.

Impact Evaluation

The sixth article (on pages 99-140) deals with a subject that is (or, if it is not, should be) at the heart of any serious consideration of the worth of public spending:

- Is proposed spending on new policies likely to produce the results expected?
- Is spending on existing policies producing the results expected?
- Is spending on existing policies producing any unexpected or undesired results?

Of course, the subject is considerably more complex than may be perceived from those three simple questions. Nevertheless, we believe that it is a matter that both the Government and Parliament should address in the interests of ensuring that public money is spent on policies whose real effects are known (at least with a reasonable degree of certainty).

Introduction

- 1.001 In this article we analyse and comment on the financial condition of Hospital and Health Services (HHSs)¹ based on the information in their audited financial statements for the five years 1994-95 to 1998-99.
- 1.002 In 1997 and 1998² we reported on our analysis of the financial condition of Crown Health Enterprises over the three financial years from 1 July 1994 to 30 June 1997. That analysis highlighted significant losses, resulting in erosion of the equity base and the need for additional financial support from taxpayers.
- 1.003 Our analysis and comment is confined to financial condition because that (at present) is the limit of the Audit Office's mandate. However, as we said in both 1997 and 1998, financial measures alone are not a suitable basis for judging the "success" of HHSs. Appropriate attention needs to be given to establishing a suitable mix of financial and non-financial measures and standards that are publicly reported against.

Changes Affecting Hospital and Health Services

- 1.004 With effect from 1 July 1998 three significant changes have affected HHSs:
- a revised statutory requirement that HHSs operate in a "business-like and effective manner" and "on a not-for-profit basis", instead of as "successful and efficient businesses";
 - introduction of the "Deficit Switch"; and
 - introduction of a capital charge.

1 New Zealand Blood Service Limited (NZBS) was established as an HHS on 1 July 1998. We have not included data for NZBS in our analysis because of the range of services NZBS provides and the fact that its primary relationship is with other HHSs and health service providers rather than with the Health Funding Authority.

2 *First Report for 1997*, parliamentary paper B.29[97a], pages 121-140; *Second Report for 1998*, parliamentary paper B.29[98b], pages 11-36.

“Deficit Switch”

- 1.005 In 1998 we reported that capital contributions from the Crown were not, in some cases, being used to expand the Crown’s investment in HHSs. Rather, the contributions were being used to provide working capital because of previous operating deficits.³ To address this problem the Government agreed to what was called the “Deficit Switch”. The switch amounted to a transfer from Vote Crown Health Enterprises to Vote Health of the appropriations for what had been effectively a deferred payment for health services already delivered, rather than [genuine new capital] for the development of capital assets.⁴
- 1.006 To give practical effect to the switch:
- the Health Funding Authority (HFA) was required to redress price imbalances and volume requirements; and
 - for 1998-99 \$129.5 million was transferred from Vote Health Service Providers (formerly Vote Crown Health Enterprises) to Vote Health so that the HHSs could be funded to a level that appropriately covered the real and reasonable costs of the services they were contracted to provide.
- 1.007 The objective of those measures was to more appropriately reflect the price of health services and thereby halt the trend of annual operating deficits that HHSs had recorded up until 1998. An idea of the extent to which that objective was achieved in 1998-99 can be gained from Figure 1.1 on page 15. It was also intended that future capital contributions would be for financing capital projects and not for funding shortfalls in the cost of service delivery.

³ *Second Report for 1998*, paragraph 1.025.

⁴ *Ibid.*, paragraph 1.026.

Capital Charge

- 1.008 From 1 July 1998 all HHSs have been required to pay a capital charge to the Crown based on their actual shareholder's funds. The intention of the capital charge is to make explicit the true costs of the taxpayers' investment in the HHSs and, by requiring that those costs be recognised, encourage effective and efficient management of HHS assets and liabilities.
- 1.009 For 1998-99 HHSs were separately funded out of Vote Health Service Providers for the capital charge. For 1999-2000 the separate funding is being continued out of Vote Health. This separate funding is an interim arrangement for these two years. It is expected that, at some future date, the cost of the capital charge will be incorporated in the HHSs' pricing structure for their services.
- 1.010 The capital charge funding for each HHS is calculated on the basis of shareholder's funds at the beginning of the 1998-99 financial year, adjusted for the planned net operating result after tax for the year and any estimated asset revaluations. The HHSs pay the capital charge to the Crown monthly calculated at 11% of the month's balance of shareholder's funds. Thus the funding provided does not necessarily equal the charge paid.
- 1.011 In accordance with generally accepted accounting practice, the funding from the HFA is included as revenue in the HHSs' Statement of Financial Performance. However, the payment of the capital charge to the Crown is regarded as a distribution to the shareholder and as such is recorded "below the line". Thus, the effect of the capital charge transactions is to increase revenue and beneficially affect the net operating result, with a corresponding diminution in shareholder's funds.
- 1.012 For the reasons stated in paragraphs 1.010 and 1.011, readers should be aware that transactions relating to the capital charge are reflected in our data for 1998-99 and comparisons between that year and previous years need to be read accordingly.

Overall Picture of Financial Condition

1.013 The financial condition of the HHSs is a function of their financial position and performance over time. In order to provide a concise and (we hope) informative picture of HHS financial condition we have compiled two sets of data⁵:

- Table 1.1 on page 21 shows selected financial statistics on an aggregate basis for HHSs for the five years 1994-95 to 1998-99.
- Table 1.2 on pages 22-23 shows the same financial statistics for each individual HHS for 1998-99 – the latest financial year we have audited.

1.014 Key aspects of the trends in the aggregate financial condition of HHSs over the five years are:

- net operating deficits in all years, but a significant reduction in the deficit for 1998-99;
- as a result –
 - a major turn round in the erosion of the equity base caused by operating deficits; and
 - much reduced reliance on capital contributions from the Crown in 1998-99;
- shareholder's funds have nevertheless declined over the period, and would have been considerably lower without the capital contributions from the Crown.

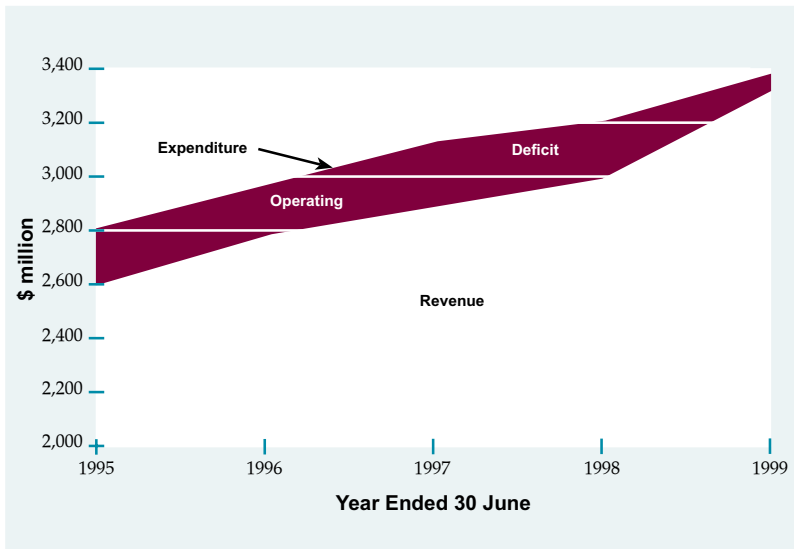
1.015 We comment on these trends in the following paragraphs.

⁵ The source of the data is the audited annual financial statements of the HHSs. Consequently, figures used are all in current dollars as reported in those statements.

Operating Results

1.016 The aggregate annual operating results over the five years 1994-95 to 1998-99 are presented graphically in Figure 1.1 below.

Figure 1.1
Aggregate Operating Results
1994-95 to 1998-99



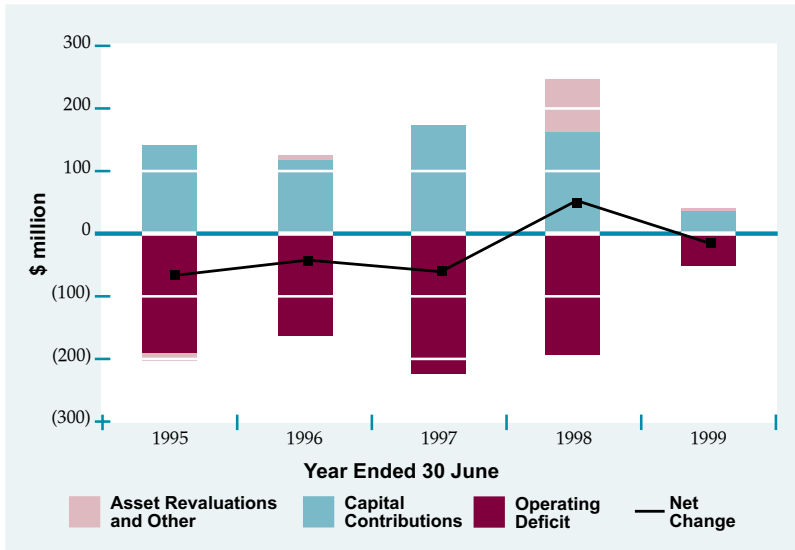
1.017 While revenue rose steadily over the five years expenditure also rose, although the rate of increase in expenditure declined in the last two years. Expenditure always exceeded revenue but the gap narrowed appreciably in 1998-99.



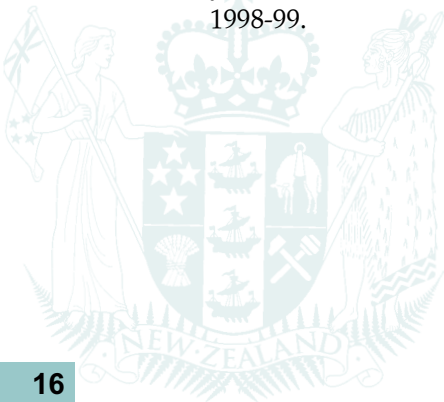
Changes in Shareholder's Funds

1.018 The changes in shareholder's funds each year for the five years to 1998-99 are shown graphically in Figure 1.2 below.

Figure 1.2
Changes in Shareholder's Funds
1994-95 to 1998-99

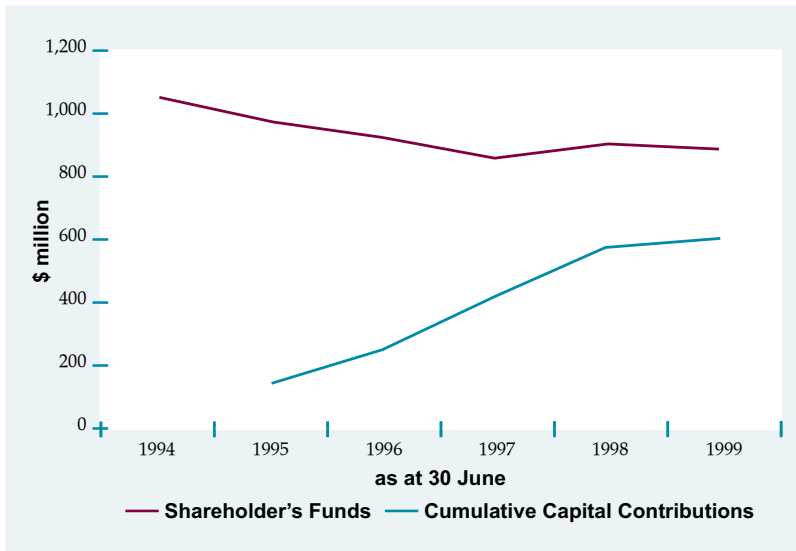


1.019 The two features that stand out are the amounts of capital contributions from the Crown – as positive contributions to changes in shareholder's funds – and the amounts of operating deficits that have the opposite effect. In both cases the amounts were substantial in the four years from 1994-95 to 1997-98 but dropped dramatically in 1998-99.



1.020 The relationship between the amounts of shareholder's funds at the end of each of the five years and the cumulative effect on those amounts of the Crown's capital contributions is illustrated in Figure 1.3 below. The picture is clear: but for the additional capital provided by the Crown the amount of shareholder's funds would have dropped over the five years to about 27% of what it stood at on 1 July 1994.

Figure 1.3
Shareholder's Funds and Cumulative Capital Contributions 1994-95 to 1998-99



Composition of Shareholder's Funds

1.021 The composition of shareholder's funds at the end of each of the five years is shown in Figure 1.4 on page 18.

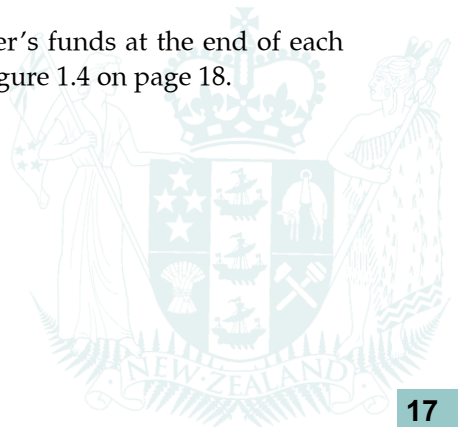
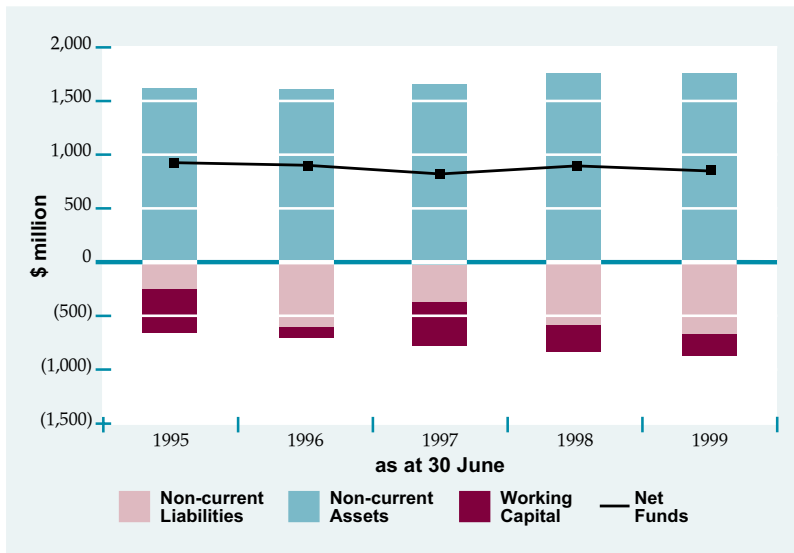


Figure 1.4
Composition of Shareholder's Funds
1994-95 to 1998-99



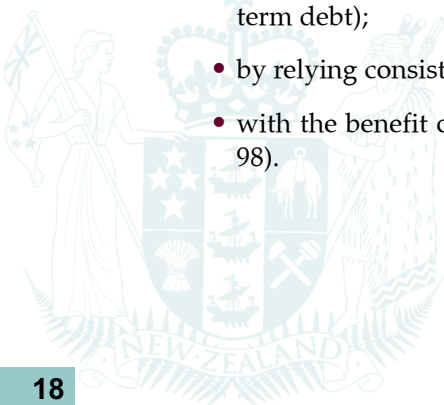
Note – “Working Capital” is calculated as the difference between current assets and current liabilities. “Current” means realisable within one year of the reporting date. Current liabilities therefore include that portion of term debt due to mature within the year.

“Non-current Assets” are assets (such as land, buildings, and plant) that are not expected to be realised in cash or sold or consumed within one year of the reporting date.

“Non-current Liabilities” are liabilities (such as term debts) that are not expected to be settled or extinguished within one year of the reporting date.

1.022 The “asset base” – in the form of land, buildings, plant, etc. – has been maintained over the five years. On the other hand, maintenance of the asset base has happened:

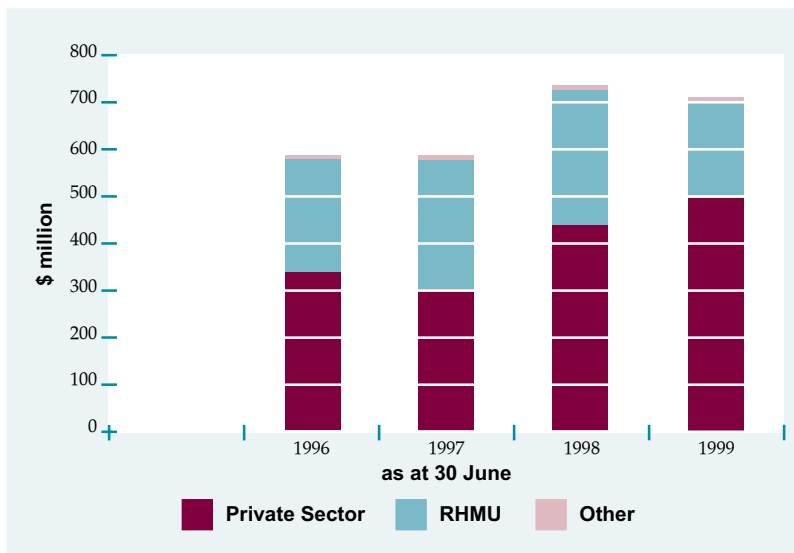
- at the expense of increased non-current liabilities (mainly term debt);
- by relying consistently on negative working capital; and
- with the benefit of asset revaluations (especially in 1997-98).



Term Debt

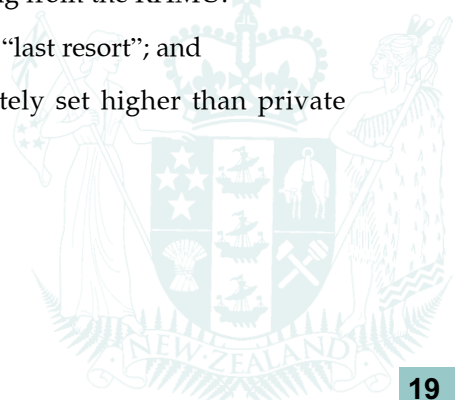
1.023 The sources of term debt – both current and non-current – at the end of each of the five years are shown graphically in Figure 1.5 below.

Figure 1.5
Sources of Term Debt
1995-96 to 1998-99



1.024 The principal feature shown by Figure 1.5 is that borrowing from the RHMU has remained a significant proportion of term debt that, overall, has increased. By 1999, RHMU debt still represented 29% of all term debt, notwithstanding that borrowing from the RHMU:

- is intended to be a matter of “last resort”; and
- is at interest rates deliberately set higher than private sector term debt rates.



Conclusion on Overall Financial Condition

1.025 The preceding analysis highlights the improved financial condition of HHSs since the “Deficit Switch” initiated in 1998-99 and the HFA’s redress of price imbalances and volume requirements. The financial performance of HHSs in that year was in marked contrast to the preceding four years. Those years were characterised by large operating deficits and reliance on the Crown providing a continuing flow of additional capital.

1.026 A number of factors could be involved in the improvement. These include:

- a more appropriate price paid for contracted services by the HFA, so that HHSs are closer to being funded for the costs they incur;
- additional Crown capital being used to improve buildings and facilities rather than fund day-to-day operations; and
- better matching of service delivery to contracted revenue, which may include delivery of fewer unfunded services.

1.027 We also believe that Parliament is now being given a clearer representation of the true cost of health and disability support services through the switching of appropriations from Vote Health Service Providers to Vote Health.



Table 1.1 – Aggregate Financial Statistics 1994–95 to 1998–99

	1994-95 \$000	1995-96 \$000	1996-97 \$000	1997-98 \$000	1998-99 \$000
Expenditure	2,800,168	2,952,254	3,130,096	3,205,241	(1)3,384,804
Revenue	2,601,768	2,783,567	2,902,025	3,007,661	(2)3,330,468
Net Operating Result	(198,400)	(168,687)	(228,071)	(197,580)	(54,336)
Movements in Equity					
Capital Contributions	135,351	113,276	168,436	157,726	32,819
Asset Revaluations	2,555	6,884	(124)	83,919	5,376
Other	(13,414)	(1,638)	(48)	2,907	(565)
Opening Shareholder's Funds	124,492	118,522	168,264	244,552	37,630
Net Change for the Year	1,045,609	971,701	921,536	861,729	908,701
Closing Shareholder's Funds	(73,908)	(50,165)	(59,807)	46,972	(16,706)
971,701	921,536	861,729	908,701	891,995	
Composition of Shareholder's Funds –					
Working Capital	(398,618)	(56,275)	(412,257)	(232,671)	(217,342)
Non-current Assets	1,622,472	1,604,616	1,649,621	1,735,707	1,763,083
Non-current Liabilities	(252,153)	(626,805)	(375,635)	(594,335)	(653,746)
971,701	921,536	861,729	908,701	891,995	
Term Debt –					
Private Sector	(3)	331,266	294,529	440,868	493,401
RHMU	(3)	254,261	280,068	285,248	204,573
Other	(3)	4,845	10,995	10,433	9,679
(3)	590,372	585,592	736,549	707,653	

Note: a + b = c

Notes - (1) includes the cost of the capital charge.

(2) includes the funding received to meet the cost of the capital charge.

(3) We did not compile these figures when we first reported in 1997.

THE FINANCIAL CONDITION OF HOSPITAL AND HEALTH SERVICES

Table 1.2
Individual Financial Statistics 1998-99
(All amounts in \$000)

Hospital and Health Service	Operations			Movements in Equity		
	Expenditure (1)	Revenue (2)	Net Operating Result	Capital Contributions	Asset Revaluations	Other
Northland Health	100,670	104,008	3,338	-	-	-
Waitemata Health	206,256	203,615	(2,641)	-	3,922	-
Auckland Healthcare	562,321	556,832	(5,489)	-	-	-
Counties Manukau	255,215	255,463	248	-	-	17
Health Waikato	302,348	302,384	36	-	-	-
Lakeland Health	66,889	67,090	201	-	-	-
Western Bay Health (3)	49,238	49,268	30	-	-	(14,189)
Pacific Health (3)	77,850	78,143	293	-	-	14,189
Tairāwhiti Healthcare	48,405	44,035	(4,370)	2,500	-	-
Taranaki Healthcare	83,985	79,608	(4,377)	3,000	21	-
Health Care Hawkes Bay	121,421	113,228	(8,193)	5,500	-	-
MidCentral Health	165,603	165,776	173	2,000	-	-
Good Health Wanganui	69,514	69,582	68	-	-	(40)
Wairarapa Health	32,839	30,480	(2,359)	2,300	-	-
Hutt Valley Health	94,719	94,870	151	-	-	-
Capital Coast Health	266,032	244,270	(21,762)	10,000	323	(608)
Nelson-Marlborough Health	106,904	105,995	(909)	1,619	-	-
Coast Healthcare	44,883	40,803	(4,080)	1,400	-	-
Canterbury Health	296,818	298,490	1,672	-	-	-
Healthlink South	117,595	116,743	(852)	4,500	-	66
Health South Canterbury	47,034	44,880	(2,154)	-	-	-
Healthcare Otago	188,341	188,388	47	-	-	-
Southern Health	79,924	76,517	(3,407)	-	1,110	-
Totals	3,384,804	3,330,468	(54,336)	32,819	5,376	(565)

(1) Expenditure includes the cost of the capital charge (see paragraph 1.011).

(2) Revenue includes the funding received to meet the cost of the capital charge (see paragraph 1.011).

(3) Western Bay Health amalgamated with East Bay Health on 1 February 1999 and became Pacific Health.

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Changes in Shareholder's Funds			Composition of Closing Shareholder's Funds			Sources of Term Debt (5)		
Opening Shareholder's Funds	Net Change for Year (4)	Closing Shareholder's Funds	Working Capital	Non-current Assets	Non-current Liabilities	Private Sector	RHMU	Other
39,376	3,338	42,714	5,155	46,599	9,040	7,000	-	-
83,530	1,281	84,811	(4,832)	148,537	58,894	58,500	-	1,346
88,210	(5,489)	82,721	(48,786)	179,419	47,912	35,353	-	144
68,809	265	69,074	(26,994)	128,495	32,427	36,853	-	-
99,578	37	99,615	(8,903)	189,749	81,231	82,434	-	-
9,639	201	9,840	(4,250)	24,457	10,367	1,714	8,579	22
14,159	(14,159)	-						
8,206	14,482	22,688	(1,877)	46,695	22,130	2,000	14,984	4,140
14,715	(1,870)	12,845	464	26,633	14,252	5,000	8,543	3
20,396	(1,356)	19,040	(8,229)	42,613	15,344	15,000	-	30
37,068	(2,693)	34,375	(5,700)	83,276	43,201	-	40,508	2,080
31,072	2,173	33,245	(17,308)	60,173	9,620	22,700	-	-
24,813	28	24,841	136	42,114	17,409	-	17,000	-
7,672	(59)	7,613	(899)	16,394	7,882	-	7,150	406
36,395	151	36,546	(2,313)	65,216	26,357	-	23,545	100
77,179	(12,047)	65,132	(45,353)	193,929	83,444	89,664	30,167	83
22,818	710	23,528	1,217	45,321	23,010	-	17,461	90
10,504	(2,680)	7,824	(2,568)	20,561	10,169	900	8,866	355
117,769	1,672	119,441	(12,414)	193,838	61,983	57,915	-	589
19,297	3,714	23,011	(27,459)	50,861	391	8,632	8,123	-
10,826	(2,154)	8,672	(11,091)	21,329	1,566	861	10,541	-
39,110	47	39,157	8,246	91,270	60,359	59,575	-	158
27,559	(2,297)	25,262	(3,584)	45,604	16,758	9,300	9,106	133
908,701	(16,706)	891,995	(217,342)	1,763,083	653,746	493,401	204,573	9,679

(4) This is the sum of Net Operating Result and Movements in Equity.

(5) Current and non-current.

Summary

- 2.001 Hospital and Health Services (HHSs) make large capital purchases, some recent examples of which have come in for questioning about the way that they were handled. Therefore, we decided to undertake a general review of HHSs' capital purchasing policies and practices.
- 2.002 Generally, we found good practice at the 11 HHSs where we carried out our review of 14 capital purchases. However, we also identified several areas where the HHS needed to improve its purchasing policies and practices.
- 2.003 Although these shortcomings did not necessarily significantly affect the outcome of the purchases we reviewed, the processes needed to be tightened so that the HHS could demonstrate that:
- it is achieving value for money when purchasing; and
 - its processes are seen to be fair.
- 2.004 The positive things we noted from our review were that:
- In all but one case the HHS had documented purchasing policies and practices. The one exception was an HHS that had been established for only a year, and which has since developed purchasing policies and practices.
 - The HHSs had a sound basis for the decision to purchase and (in all but two cases) they managed their overall capital expenditure in accordance with strategic priorities and business plans.
 - In all but two purchases the HHS Board was involved at an early stage of the purchase process, was given adequate information, and sought appropriate advice on technical matters.
 - For all 14 purchases a purchase specification was prepared – four by the HHS itself and 10 by an external consultant. In preparing the four specifications themselves the HHSs had sought specialist advice, consulted with users (where relevant), and had the specification independently reviewed (in all but one case).

- The HHSs tendered all 14 purchases. The majority were closed rather than open tenders. However, for the closed tenders the HHS's method of selecting the supplier was demonstrably fair.

2.005 The shortcomings we noted were that:

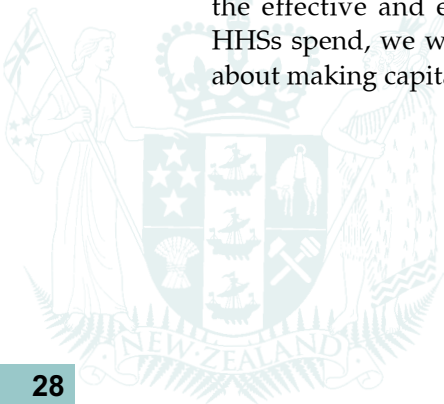
- The documented purchasing policies and practices of five of the HHSs did not meet our criteria. None of the five had documented practices for tender evaluation or pre-determined tender rules.
- These shortcomings were reflected in the individual purchases that we reviewed. For six purchases the HHS did not have predetermined tender rules and for four the HHS did not have pre-set evaluation criteria. In two of those four cases, the HHS evaluated tenders against the specification set out in the Request for Proposal or Business Case, and in the other two the HHS had some criteria that were not communicated to the tenderers

What Has Happened?

2.006 Since we undertook our review the Minister of Health has instructed all government departments and agencies associated with health to ensure that they follow good practices when spending public money. The over-riding consideration is to be accountability for spending taxpayers' money by a process that is transparent.

What Are We Doing?

2.007 Because proper purchasing procedures are important to the effective and efficient use of the public money that HHSs spend, we will maintain our watch on how they go about making capital purchases.



Why We Looked at Capital Purchasing

- 2.008 HHSs spent \$229 million on capital purchases in the year ended 30 June 1998. This is a significant sum of money. In addition, over the last two years questions have been asked in Parliament about purchasing in the health sector. (We reported in September 1999 on the purchase by Capital Coast Health Limited of a new computerised information system.¹)
- 2.009 We looked at HHS purchasing policies and practices as part of our audit for the year ended 30 June 1998. The results of this preliminary review suggested that a more detailed review would be worthwhile. We therefore conducted an in-depth review as part of the audit for the year ended 30 June 1999 to establish whether HHSs:
- had documented purchasing policies and practices of an adequate quality; and
 - were applying those policies and practices.

What We Looked At

How Did We Choose the Capital Purchases that We Reviewed?

- 2.010 We identified 44 capital purchases – comprising building projects worth over \$1 million and information technology (IT) projects worth over \$500,000 – that HHSs had approved since July 1997. We selected these two categories on the basis that:
- large sums of money are tied up in building projects; and
 - IT projects (which are widely undertaken by HHSs) need to be properly specified to ensure their success.

¹ *Fourth Report for 1999, parliamentary paper B.29[99d], pages 11–45.*

- 2.011 From the 44 purchases we selected a sample 14 for the purposes of our review. This sample was representative of HHSs and the two project types. Our selection process placed greater weight on the high-value projects, resulting in the sample comprising 46% of the total value of contracts approved (i.e. \$133.9 million out of \$288.7 million).
- 2.012 The sample of 14 consisted of seven building projects and seven IT projects, by 11 of the 23 HHSs.

How We Performed Our Review

- 2.013 We applied the criteria set out in our *Good Practice for Purchasing by Government Departments*.² We produced the *Good Practice* guide in 1995 after reviewing departmental purchasing policies and practices. We published the guide so that departments could use it as a benchmark when determining their own purchasing arrangements. However, we believe that the guide could be useful to other public sector entities such as HHSs.
- 2.014 In assessing whether the policies and practices used by each HHS for the purchases we selected complied with our guide, we had discussions with appropriate HHS staff and sighted relevant supporting documentation.

What We Measured the HHSs Against

- 2.015 In assessing the quality of the purchasing policies and practices that the 11 HHSs used, we looked to establish whether each HHS had met the following broad criteria:
- documented purchasing policies and practices;
 - a sound rationale for the decision to purchase;
 - appropriate involvement of the Board;
 - a written purchase specification;
 - an appropriate method of purchase;

² ISBN 0 477 02848 9, September 1995.

- a predetermined set of rules for tender;
- sound practices to evaluate tenders; and
- an effective project management system.

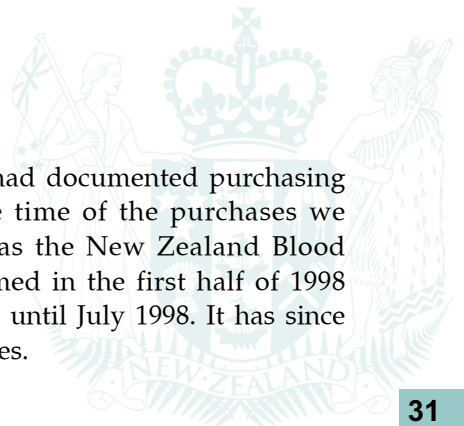
Documented Purchasing Policies and Practices

Our Expectations

- 2.016 We expected that each HHS would have documented purchasing policies and practices to ensure that:
- the greatest value for money is achieved when purchasing; and
 - tenderers are dealt with fairly throughout the purchasing process.
- 2.017 Specifically, we looked for evidence that the HHS had documented purchasing policies and practices that met the guidance in our *Good Practice for Purchasing by Government Departments*.
- 2.018 Both of the objectives stated in paragraph 2.009 are critical to the purchasing process. By not detailing the practices required to meet these objectives HHSs run the risk that:
- an error is made;
 - the “best” supplier may not be selected; and/or
 - the purchasing process may not be able to withstand scrutiny.

Our Findings

- 2.019 All but one of the 11 HHSs had documented purchasing policies and practices at the time of the purchases we reviewed. The exception was the New Zealand Blood Service, which was only formed in the first half of 1998 and was not fully operational until July 1998. It has since developed policies and practices.



2.020 However, of the 10 HHSs that had documented purchasing policies and practices, five did not fully meet the standards in our *Good Practice* guide. All five did not have specified practices for tender evaluation, nor did they have pre-determined tender rules.

Rationale for the Decision to Purchase

Our Expectations

2.021 We expected that each HHS would have a sound basis for the decision to purchase and that it was managing its capital expenditure in accordance with strategic priorities and business plans.

2.022 Specifically, we looked for evidence that the HHS had:

- ensured that the purchase was in line with its long-term strategic objectives;
- established the need to purchase;
- considered the effect of the purchase on clinical and financial viability over time;
- defined and identified the specific incremental benefits directly attributable to the purchase;
- completed a cost-benefit analysis and identified that cost savings or efficiency gains could not be achieved without the purchase; and
- considered all alternative options to the purchase including the “do nothing” option.

Our Findings

2.023 For six of the 14 purchases the HHS had sought funding support from the Crown by way of additional equity, and therefore had to prepare a business case for approval by the shareholding Ministers. The requirements for these business cases are set out in guidelines produced by the Crown Company Monitoring Advisory Unit (CCMAU).³

³ CCMAU: *Guidelines For Hospital and Health Services – Seeking Support for Capital Expenditure*, May 1998.

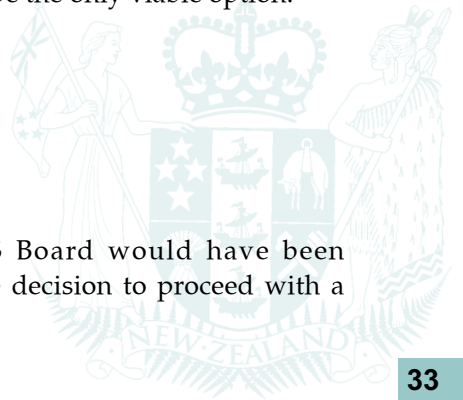
These guidelines require that the decision to purchase is fully justified, alternatives to the purchase are considered, and the costs and benefits of the purchase are assessed.

- 2.024 By the HHS preparing the business case these six purchases met our expectations.
- 2.025 For the remaining eight purchases (six of which were IT projects), the HHS had in each case:
- Established the need for the purchase – in relation to the IT projects this included year 2000 compliance, increasing maintenance costs, and bringing IT systems and control “in house”. Both building projects were needed to meet service delivery requirements.
 - Assessed the effects of the purchase on clinical and financial viability.
 - Established the specific incremental benefits expected from the purchase.
 - Established that the purchase would mean cost savings and increased efficiency.
- 2.026 For seven purchases the HHS had included the purchase in its business plan and established a linkage between the benefits of the purchase and the business plan objectives. One purchase (an IT project) had not been included in the business plan.
- 2.027 The analysis of the options to purchase was done well. All except three HHSs considered the various options – including the “do-nothing” option – and recorded the reasons why each was rejected. The three that did not do the analysis were purchasing IT replacements and they all considered replacement to be the only viable option.

Board Involvement

Our Expectations

- 2.028 We expected that the HHS Board would have been appropriately involved in the decision to proceed with a significant purchase.



2.029 Specifically, we looked for evidence that the Board:

- was involved at an early stage in the purchase process;
- was given adequate information on which to base its decision to proceed with the purchase; and
- received appropriate advice to enable it to understand any technical matters.

Our Findings

2.030 In all but one of the 14 purchases:

- the Board was involved in the purchase from the initial stages;
- the information supplied to Board members when making the decision to proceed with the purchase was of a good quality and included financial and technical reports from internal and external consultants.

2.031 In one case the Board had approved the inclusion of the project in its business plan, but the purchase had proceeded to the point of calling and receiving tenders before the Board approved it. By not approving the purchase until tenders were called the HHS increased the risk that the purchase process may have reached the stage where the Board was committed to proceeding with a purchase that it might not have otherwise made. In addition, the information supplied to the Board did not meet its own policies as there was no formal capital proposal form and there was a lack of user involvement and financial justification.

2.032 The Board had also received technical advice in all but one case, where the HHS was replacing its IT infrastructure. The new infrastructure purchase was the first step to provide the platform for a larger IT project and we understand that the Board received technical advice in relation to the larger project. If the Board does not receive adequate information and advice on technical matters, the risk is increased that the purchase will not necessarily meet the requirements of the HHS.

Written Purchase Specification

Our Expectations

- 2.033 We expected that each HHS would have prepared a clear, comprehensive, and accurate specification of exactly what it wanted to purchase, to ensure that the product purchased would do what it was needed to do.
- 2.034 Specifically, we looked for evidence that:
- the specification focused on the functional requirements of the product (what it is expected to do) and the physical characteristics of the product (for example, technical and operational requirements, performance standards and quality assurance requirements);
 - the HHS had sought appropriate advice if it did not have the necessary technical expertise;
 - the HHS had consulted with operational staff and other users to ensure that the specifications met their needs; and
 - for purchases of a high value or technical complexity, or involving some other element of risk, the HHS had ensured that someone other than the preparer had evaluated the specification.

Our Findings

- 2.035 For all 14 purchases the HHS had prepared a purchase specification.
- 2.036 For 10 of the purchases the HHS used an external consultant (because of the technical and specialised nature of the purchase) to prepare the purchase specification.
- 2.037 In all relevant cases the users' needs were assessed when preparing the specification and, where an external consultant was used, an independent consultant evaluated the specification. (If someone other than the preparer does not review the specification, the risk that it has not addressed all aspects of the item to be purchased is increased. Unless the specification is correct the item purchased will not necessarily meet the needs of the organisation.)

2.038 The remaining four purchase specifications (which involved the purchase of IT equipment) were prepared in-house. For all four purchases the HHS had consulted with users where relevant, and all but one had the specification reviewed by someone independent of the person preparing it.

An Appropriate Method of Purchase

Our Expectations

2.039 We expected that each HHS would have used a purchase method – open tender, closed tender, or selective purchase – that it could demonstrate was the most appropriate to the circumstances.

2.040 Specifically, we looked for evidence that:

- The preferred method of purchase was an open tender⁴ because it –
 - establishes the most competitive price and terms available;
 - explores or tests the market for alternative solutions; and
 - fulfils a public duty of fairness and equity between suppliers.
- If a closed tender⁵ was conducted, the identification of suppliers was well founded, thorough and demonstrably fair.
- If a selective purchase⁶ was made, the HHS had carefully considered and justified the reasons for using it, bearing in mind that –

4 Where all potential suppliers (subject to any practical limitation of reaching them all by advertising) are given the opportunity to tender.

5 Where invitations to tender are issued to a predetermined list of suppliers. This method has advantages when only a limited number of firms are believed to have the capability and when confidentiality is important, and it is not as costly as it limits the number of responses. The biggest disadvantage is that a better source of supply may be missed.

6 A purchase made from a supplier without having invited competing tenders from any other supplier.

- the most competitive price and terms may not be obtained;
- the best source of supply may not be found; and
- potential suppliers, whether known or unknown, will not be given an equal chance to compete for the business.

Our Findings

2.041 The methods of purchase used were:

Open Tender	3
Closed Tender	10
Part Closed Tender/Part Selective Purchase	1
Total	14

2.042 Where the HHS used the closed tender method of purchase, potential suppliers were identified with the assistance of external consultants, project managers or in-house technical staff.

2.043 The one instance of partial selective purchase was for installation of computer and telephone cabling. Selective purchase was used because the installer was already the preferred supplier of communication systems for the site redevelopment and was the main provider in New Zealand.

2.044 Overall, we consider the methods were demonstrably fair – except in one case where the lack of documented evidence meant that we were not able to form an opinion. This lack of evidence increases the risk that the HHS would not be able to establish that its selection process was fair should it be challenged.



Predetermined Tender Rules

Our Expectations

- 2.045 We expected that each HHS would have conducted the tender in accordance with a predetermined set of rules, and advised tenderers what the tender rules would be and how they were to be applied.
- 2.046 Specifically, we looked for evidence that there were tender rules governing:
- the conditions of tender;
 - acceptance of tenders;
 - late tenders;
 - tender evaluation criteria;
 - due diligence enquiry; and
 - post-tender negotiations.

Our Findings

- 2.047 For the 14 purchases:
- In five cases the HHS conducted the tender in accordance with a predetermined set of rules.
 - In three cases the HHS had no predetermined rules but the tender was conducted in conjunction with an external consultant or project manager and standard industry rules of tender were adopted. In these cases we accept that the purchases met our criteria.
 - In the other six cases the HHS had no predetermined rules.
- 2.048 Not having predetermined tender rules increases the likelihood of uncertainty between the HHS and potential suppliers as to what rules are to be applied to a particular purchase. The absence of rules also increases the risk that an individual tenderer might feel treated unequally or unfairly compared with other tenderers, and publicly disputes the tender process.

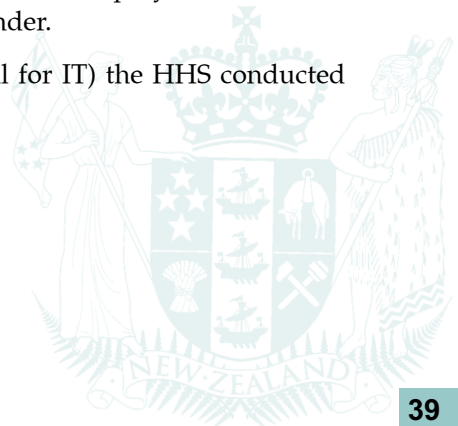
Tender Evaluation Practice

Our Expectations

- 2.049 We expected that each HHS would have established a sound set of practices by which it could evaluate tenders on a consistent and defensible basis.
- 2.050 Specifically, we looked for evidence that the HHS had:
- decided how the tenders would be evaluated before calling them;
 - included in the tender documents reasonable particulars of what evaluation criteria were to be applied;
 - used a range of appropriately skilled people to evaluate the tenders; and
 - adequately documented the evaluations so as to demonstrate that it gave proper consideration to, and had reached a sustainable decision on, each tender.

Our Findings

- 2.051 We encountered a variety of approaches to tender evaluation. The approaches can, however, be grouped into two broad categories:
- those used where the HHS conducted the tender itself; and
 - those used where the HHS, because of the specialised technical nature of the purchase, employed an external consultant to conduct the tender.
- 2.052 For six of the 14 purchases (all for IT) the HHS conducted the tender itself.



- 2.053 For two of these six purchases the HHS fully met our expectations by having pre-set evaluation criteria. For two other purchases the HHS did not have pre-set evaluation criteria but used an alternative such as the specification for purchase set out in the Request for Proposal or Business Case. For the remaining two purchases the HHS had some criteria but they were not communicated to the tenderers.
- 2.054 Teams of evaluators were used for all six purchases. In four cases the teams contained people with technical and commercial knowledge – one team comprised nine users covering all professional groups and business processes within the HHS. In the other two cases the team members were solely from an IT background. However, in one of those two the final sign-off for the project was the responsibility of the Chief Financial Officer.
- 2.055 The evaluations were documented and provided evidence of how tenderers were differentiated.
- 2.056 For the eight purchases (one IT and seven building) where the HHS employed a project manager to conduct the tender on its behalf:
- The evaluation criteria used were industry standards or the purchase specification (in most instances this was the building specifications). Once compliance with the building specifications had been established and the cost was within an allowable range, the contract was awarded to the lowest cost tenderer.
 - The project manager evaluated the tenders.
 - The project manager retained the evaluation documentation. The HHS received a summary of the tender process, the evaluation results, and a recommendation as to the successful tenderer.

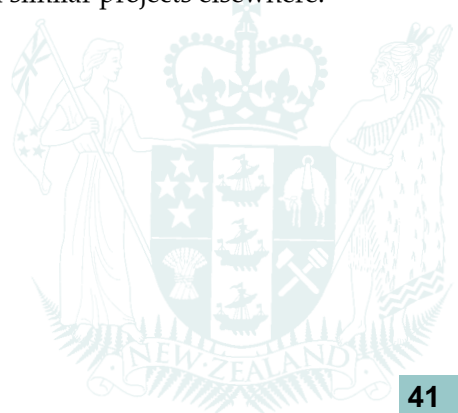
Project Management

Our Expectations

- 2.057 We expected that the HHS would manage each purchase project to ensure that it was completed:
- according to the specifications;
 - within budget; and
 - on time.
- 2.058 Specifically, we looked for evidence that each project:
- was managed by a qualified person;
 - had a detailed implementation plan which allowed for “go/no go” break points or “off ramps”;
 - had a reporting regime in place to monitor progress, cost and compliance with the specification; and
 - had a post implementation review.

Our Findings

- 2.059 A project manager was appointed to oversee each project. External consultants were appointed to manage five out of the seven building projects (because of the specialised nature of the purchases). All had previous experience managing similar projects. For the other two building projects the HHS appointed a suitably qualified internal staff member to be the project manager, both of whom had considerable experience in similar projects elsewhere.



- 2.060 Of the seven IT projects:
- In four cases an HHS staff member (the IT manager) was appointed to manage the project on the basis of their knowledge and experience in the industry.
 - In the other three cases human resource and consulting firms appointed an external project manager after a selection process. All three were appointed on the basis of their qualifications, knowledge and experience within the industry relevant to the project specifications.
- 2.061 Only one project did not have a detailed implementation plan – however, the HHS did monitor the costs of the project against budget. For the other 13 a robust programme for reporting progress against the plan was employed.
- 2.062 Eight of the implementation plans provided for a “go/no go” break point to identify where the project might have deviated significantly from the plan and (if necessary) allow for a decision to be made whether to proceed and (if so) on what basis. Where the plan did not provide for a break point, in one case the HHS thought the time involved was too short and in three cases the HHS thought that close monitoring would have revealed the need for the project to be reviewed if necessary.
- 2.063 At the time of our review only two projects had been completed. For one the HHS had completed a post-implementation review, and for the other the HHS told us that it would be completing a review shortly.



Background

- 3.001 We have reviewed the efforts of Health Benefits Limited (HBL) and the Health Funding Authority (HFA) to introduce a system of electronic claiming of pharmaceutical service subsidies and dispensing fees by community pharmacists. We undertook the review in light of our past findings of some deficiencies in the manual system for claiming the subsidies.¹
- 3.002 HBL is wholly owned by the HFA. Among other activities, HBL processes subsidy claims from community pharmacists for medicines that they have dispensed and that the Government has agreed to subsidise. Subsidised medicines are detailed in the *Pharmaceutical Schedule* maintained by Pharmaceutical Management Agency Limited (Pharmac), another wholly owned subsidiary of the HFA.
- 3.003 The HFA contracts with pharmacists for them to purchase medicines, on receipt of prescriptions dispense the medicines to patients, and then claim the patient's pharmaceutical service subsidy and the dispensing fee from HBL. Payments to pharmacists are made from the Wanganui Office of HBL (HBL Wanganui). The HFA has a service level agreement with HBL for the performance of this work.

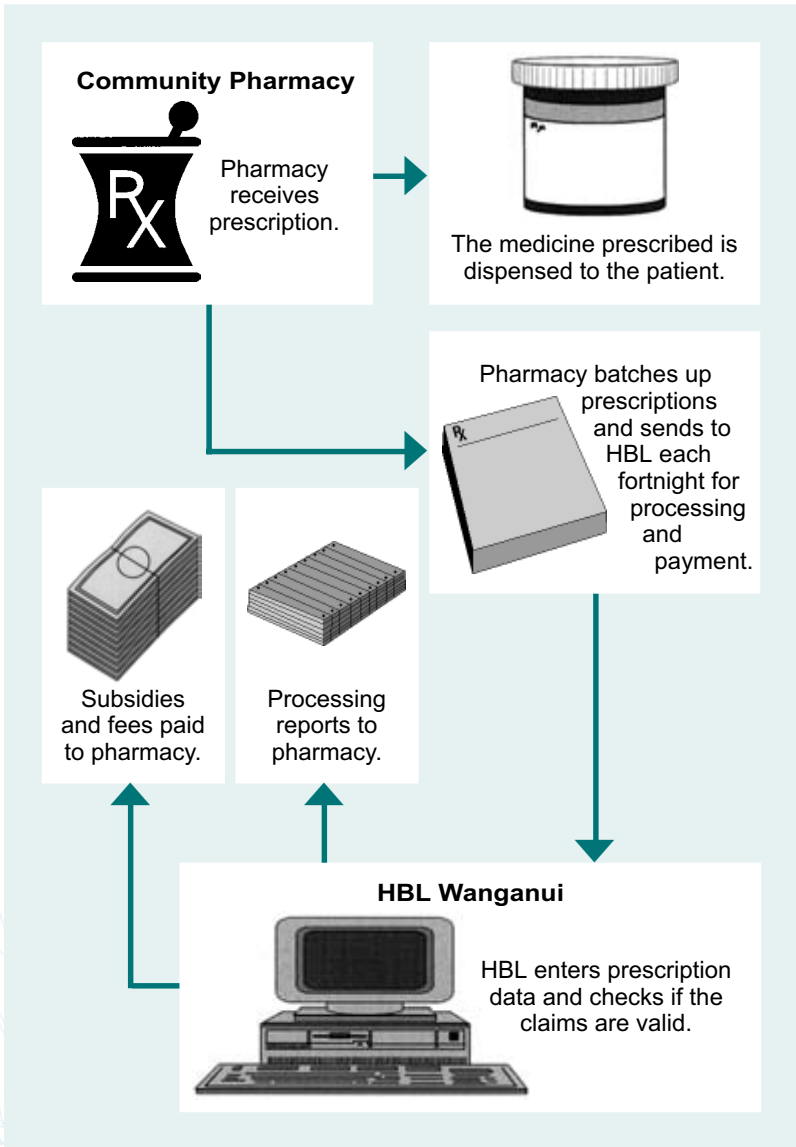
The Process of Subsidy Claiming

- 3.004 Each year, HBL Wanganui has to process claims for payment for about 35 million pharmaceutical items from about 1,000 community pharmacies. Manual systems are the main way of processing claims. They are time-consuming and laborious and occupy most of the approximately 200 people employed at HBL Wanganui.
- 3.005 As depicted in Figure 3.1 on the next page, each fortnight pharmacies send in the prescriptions from which medicines have been dispensed to patients. The staff at HBL Wanganui

¹ *Fourth Report for 1997*, parliamentary paper B.29[97d], pages 61-75; *Fourth Report for 1999*, parliamentary paper B.29[99d], pages 86-92.

have to read each prescription and manually enter the details into a computer system. The computer system checks the details and calculates the value of each item (as detailed in the *Pharmaceutical Schedule*) and the amount to be paid to the pharmacist.

Figure 3.1
Wanganui Centre Processing Flow Diagram



Electronic Claiming

- 3.006 A table of key dates and events appears on pages 48-49.
- 3.007 HBL has, for several years, been proposing to implement a system of electronic claiming. Its Directors' annual report for the year ended 30 June 1996 noted that:

HBL has signalled major changes in its operating structure and methods arising from a need to introduce electronic claiming by service providers such as doctors and pharmacists. It is clear that electronic claiming is essential if the requirements of stakeholders are to be met.

- 3.008 The system of electronic claiming that was initially developed by HBL involves pharmacists entering the details of prescriptions dispensed into a pharmacy-based computer system and sending the information on disk to HBL Wanganui. There, the information from the disk is loaded into the HBL computer system and processed. Significant savings in cost and time were expected from changing to electronic claiming.

Introducing Electronic Claiming

- 3.009 HBL planned on having all pharmacists claiming electronically by June 1999. Use of electronic claiming was to result in the closure of HBL Wanganui and a saving of several million dollars each year in processing costs. HBL did not achieve either objective and this report reviews the reasons why.
- 3.010 The introduction of electronic claiming by community pharmacists has been affected by a number of factors. We have identified three distinct phases in the change from manual to electronic claiming:
- Development and successful application by over 300 pharmacists of a basic electronic claiming system, described as the “1.5 system”.
 - The HFA contracting with pharmacists in November 1998 to adopt a more comprehensive system – identified as the “2.7 system”². This system has not yet been fully

² HBL describes the latest version of this system as the “2.28 system” (see paragraph 3.062).

ELECTRONIC CLAIMING OF PHARMACEUTICAL SERVICE SUBSIDIES AND FEES

THREE

Table of Key Dates and Events

RHAS				HEALTH BENEFITS LIMITED
THA	<ul style="list-style-type: none"> RHAs introduce monthly dispensing. North Health decides to withdraw from using HBL's manual payment system and establish its own. North Health plans for a new payment system to be the forerunner of the 2.7 system. Transitional Health Authority established on 1 April. THA decides that the new North Health payment system is to be used by HBL. 	1995	<ul style="list-style-type: none"> Advisory Task Force established to implement electronic claiming. Advisory Task Force work given more impetus. North Health gives notice of withdrawing from using HBL payment system. HBL annual report signals need for electronic claiming. 	
HFA	<ul style="list-style-type: none"> Health Funding Authority takes over from THA on 1 January. HFA contracts with pharmacists to adopt the 2.7 system - November. 	1996	<ul style="list-style-type: none"> HBL develops the 1.5 system. HBL takes over from North Health development of the new national payment system. August - new national payment system goes live. 1998-99 Business Plan published setting targets for electronic claiming. 1 December - memo to Wanganui Centre staff about changes to processing claims. 31 December - target of 49% of claims to be made electronically. 	
		1997		
		1998		

ELECTRONIC CLAIMING OF PHARMACEUTICAL SERVICE SUBSIDIES AND FEES

B.29[00a]



THREE

implemented. The project was stalled at the outset by poor project definition and because of a failure to effectively co-ordinate and manage the work of the various parties, all of whom are essential to the success of the project. HBL initially attempted this co-ordination function but was unable to achieve it. In reality, as will be discussed later, the co-ordination of all the parties could be managed only by the HFA.

- The realisation by the HFA that it needed to drive the project and co-ordinate the various parties. This change of attitude by the HFA, together with improved project management and the employment by HBL of staff with appropriate skills for a project of this complexity, has resulted in progress being made with the project.

The 1.5 System

- 3.011 HBL Wanganui developed the 1.5 system in late-1997. It represented a logical step in the change to electronic claiming. The plan was to have most pharmacists claiming under the 1.5 system by 30 June 1999.
- 3.012 HBL's 1998-99 Business Plan projected that 99% of subsidy claims would be made electronically by 30 June 1999, with intermediate milestones of 49% by 31 December 1998 and 70% by 31 March 1999. The consequent expectation was that by June 1999 HBL Wanganui would be reduced in size.
- 3.013 However, by March 1999 only about 33% of pharmacists were using the 1.5 system to claim electronically. HBL was therefore behind in its targets for introducing the 1.5 system. In part this appears to have been because HBL management had begun to realise there were drawbacks to the system.
- 3.014 Both pharmacists and HBL felt frustrated by features of implementing or operating the 1.5 system. For example, pharmacists had to undergo a long and intensive "accreditation" process that involved HBL re-entering the prescription information to check the accuracy of the pharmacists' work. Pharmacists still had to send the original prescriptions to HBL Wanganui and bundle them in a certain order that pharmacists found time-consuming.

- 3.015 Therefore, not everyone was satisfied with the 1.5 system. In March 1999, a joint HBL and New Zealand Pharmacy Guild newsletter to pharmacists stated that *the system requires manual input and intervention by HBL and is not showing the savings in time for [the] pharmacy originally envisaged.*
- 3.016 After the newsletter was issued the rate at which pharmacists were changing to electronic claiming fell away. From April to July 1999, only a further 16 pharmacists changed to the 1.5 system. As discussed below, a major reason for HBL's declining interest in the 1.5 system was the development of the new 2.7 system.

The 2.7 System for Electronic Claiming

Main Features of the 2.7 System

- 3.017 The 2.7 system was proposed as a major advance on the 1.5 system. The 2.7 system would allow medicines to be priced in the pharmacy by reference to an electronic version of the *Pharmaceutical Schedule*. Pharmacists would be able to submit to HBL a claim for the subsidised value of the prescriptions dispensed, together with a disk of the prescription information. HBL would check and pay the claim, using the 2.7 pharmacy payment system. The pricing component of this system is a product licensed to the HFA for this purpose.
- 3.018 HBL estimated that the 2.7 system would increase productivity by 2,000%. By comparison, HBL had estimated that the 1.5 system would increase productivity by 190%.
- 3.019 The successful introduction and continued operation of the 2.7 system depends on a number of other parties configuring their systems to match.

Origins of the 2.7 System

- 3.020 The four regional health authorities that were the predecessors of the HFA were each responsible for the purchase of health services. However, HBL processed pharmacists' claims for all four of them.

- 3.021 During 1996-97 one authority, North Health, withdrew from the service provided by HBL and established its own payment system in conjunction with an outside contractor. North Health also planned what was to become the 2.7 system, which would allow pharmacists to submit fully priced claims for the prescriptions that had been dispensed.
- 3.022 The Transitional Health Authority (the immediate predecessor to the HFA) decided that HBL would use the new system being developed by North Health to replace its existing system, arrangements for the use of which were to cease in mid-1998.
- 3.023 In January 1998, HBL took over from North Health staff the development of a replacement national pharmacist payment system. The system went live in August 1998. This new system was also intended as the basis for the 2.7 version of the electronic claiming system. HBL assumed responsibility for testing and implementing the 2.7 system and planned to have most pharmacists claiming under this system by 30 June 1999.

Basis for the 2.7 System

- 3.024 In November 1998, the HFA signed contracts with pharmacists in the North Island and some in the South Island that would require them to submit their claims to HBL for payment using the 2.7 system. This was to take effect by 30 June 1999. (The HFA has since concluded a similar contract with southern region pharmacists to submit claims electronically.)
- 3.025 Although responsibility for the project to implement pharmacy electronic claiming was passed to HBL, in reality it was in no position to require the other parties to adhere to the timetable for implementation. The reason is that HBL's only formal link is with the HFA and pharmacists have their own individual contractual relationship with the HFA.
- 3.026 The successful implementation and operation of pharmacy electronic claiming depends very much on the co-operation of the other parties that have a key role in the system. They are illustrated in Figure 3.2 opposite and discussed in the following paragraphs.

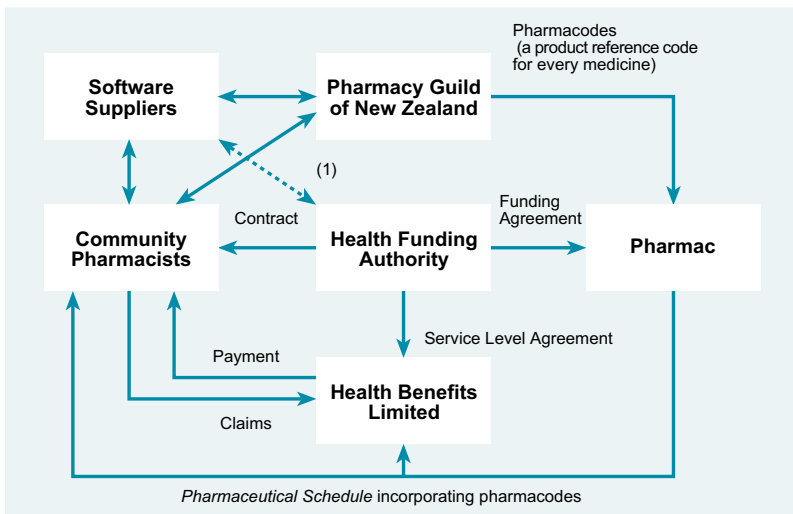
Health Funding Authority

3.027 The HFA contracts directly with pharmacists and with its subsidiaries HBL and Pharmac. The HFA has other contractual responsibilities relevant to the 2.7 project including, for example, responsibility for preparing a procedures manual to accompany electronic claiming and reaching agreement with the Pharmacy Guild for the efficient and accurate provision of “pharmacodes”.³ The HFA has no direct contractual relationship with the Pharmacy Guild, nor (normally) with the software suppliers (see paragraphs 3.070-3.071), but these organisations are an integral part of the process.

Pharmaceutical Management Limited

3.028 Pharmac is responsible for producing the *Pharmaceutical Schedule*. An up-to-date and accurate schedule is essential to the success of the 2.7 system. For electronic claiming to work, the paper-based schedule has to be converted successfully to an electronic form.

Figure 3.2
Parties Involved in the Processing and Payment of Pharmaceutical Benefits



(1) The Health Funding Authority has agreed a contract with one software supplier.

3 Every medicine has such a code and the provision of these codes to Pharmac is essential for an accurate electronic schedule.

- 3.029 The paper version of the *Schedule* is the official source document and, until recently, Pharmac was neither funded to nor required by the HFA to produce an electronic version. Pharmac initially developed the electronic *Schedule* as an internal resource, which was not always adequately maintained.
- 3.030 HBL began using this electronic version as a basis for its payment operations, rather than maintaining its own separate version. HBL took responsibility for checking the electronic version, but found it to contain inaccuracies. Pharmac has recently been provided with funding from the HFA and has agreed to produce an accurate and reliable electronic version of the *Schedule*.

Software Suppliers

- 3.031 Three suppliers provide the software used by pharmacies. The suppliers have to ensure that the software incorporates an electronic version of the *Pharmacy Schedule*. Typically, the suppliers take their instructions from their clients – the pharmacists – or the pharmacists’ representative – the Pharmacy Guild. (Recent decisions by one supplier mean that there will now be only two software systems offering a format that will be suitable for electronic claiming.)

New Zealand Pharmacy Guild

- 3.032 The Pharmacy Guild represents the interests of pharmacists and works with the HFA, Pharmac and HBL on all issues relating to the efficient delivery of prescribed medicines to patients. The Guild also works with software suppliers to ensure that pharmacy software incorporates a “fit for purpose” *Pharmaceutical Schedule*. The Guild has taken a close interest in the electronic claiming project and has undertaken benchmark prescription testing to ensure that systems perform as expected.

A Single Processing Site

- 3.033 HBL originally operated from four sites:
- Wanganui, employing approximately 200 people;
 - Christchurch, employing 100 people to process claims from medical practitioners and other health professionals;
 - Auckland, employing 20 people; and
 - its Head Office in Wellington, employing 15 people.
- 3.034 The change to electronic claiming for all of HBL's payment systems meant that HBL would need fewer staff in the future. HBL had originally planned – as stated in its 1998-99 Business Plan – to move all processing to one site in 2000-2001.
- 3.035 However, in November 1998 HBL issued a revised business plan which indicated that the move to a single site would take place in 1998-99. The move was expected to reduce the annual labour costs associated with the processing of pharmaceutical subsidy claims by \$3.2 million. Both the move and the savings were dependent on implementing electronic claiming for all pharmacists.
- 3.036 On 1 December 1998 HBL issued a memorandum to all staff at the Wanganui centre, telling them that:
- the operating functions would be moved to a single site;
 - the location of this site was still to be decided; but
 - by 30 June 1999 most of the 1,000 pharmacies would be claiming electronically.
- 3.037 HBL told us that there was a consultation process with staff on whether there should be a single site and the location of any such site.
- 3.038 In February 1999 HBL issued a further memorandum that named Wellington as the location of the single site. The result would be staff reductions at Wanganui beginning in March 1999 and continuing through to June 1999. By the end of June it was expected that only about 20 staff would be engaged on the processing of pharmaceutical subsidy claims and the site would, in effect, be largely closed as a processing centre.

Implementing the 2.7 System

- 3.039 The 2.7 system has not yet been fully implemented and the Wanganui centre continues to carry out manual processing. The main reason for the failure to implement the system by 30 June 1999, and therefore to meet the revised 1998-99 Business Plan targets, are described in the following paragraphs. They detail a (concerning) lack of project management by HBL and incorrect reporting at the early stages of the project. Achieving the revised targets was also inhibited by the decision to discourage pharmacists from adopting the 1.5 system and encouraging them to wait for the 2.7 system.
- 3.040 HBL knew in November 1998 that the 2.7 system was the preferred method for electronic claiming. All pharmacists were to be on this system by 30 June 1999, and HBL had predicated its move to a single site on implementation of the 2.7 system. Nevertheless, we could find no project plan prepared in 1998 for implementing the system.
- 3.041 An internal HBL Wellington paper dated 19 December 1998 noted that there had been almost no progress on implementing the 2.7 system. (For example, no dates had been set for testing it.) Concern was also raised that the system may not be compatible with some existing HBL systems. A further internal paper, dated 24 February 1999, noted that a draft plan was being developed for ensuring that pharmacy software was compatible with the 2.7 data requirements, but that *we are well behind in meeting any objective*.
- 3.042 The first recorded project management meeting notes that we found are from an HBL meeting of 12 January 1999. A project plan for implementing the 2.7 system was tabled at this meeting, and showed that the system would be ready for pilot testing on 1 March 1999. The meeting noted in its action plan that, as an interim step, HBL would continue with its programme to convert the remaining eligible pharmacies to electronic claiming using the 1.5 system.

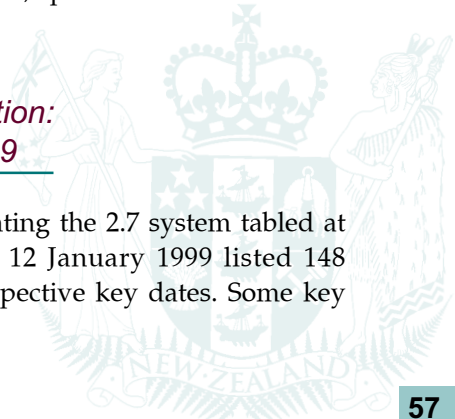
3.043 The project plan for the 2.7 system highlighted a number of risks and how these would be managed, including:

Risk	Management Plan
Software vendors are not making changes and are slow in rolling out their products.	While we do not control this risk we are maintaining a close relationship with the vendors. Weekly contact is planned so early action can be taken on issues.
Lack of agreement by Pharmac, the Pharmacy Guild and the HFA on changes to the Pharmaceutical Schedule to make it programmable.	This is another risk that HBL does not control but is managing closely. Weekly meetings between Pharmac, the Pharmacy Guild and HBL are planned to progress the Schedule.
Implementation of 2.7 delayed beyond April 1999.	2.7 implementation is delayed, the process improvements for manual processing and 1.5 will be vigorously continued.

3.044 However, while these risks were identified, we could find no record that that they had been systematically addressed in the way indicated in the management plan. For example, as noted in paragraph 3.041, by 24 February 1999 HBL still had no system in place for checking to ensure that pharmacy software was compatible with the 2.7 system. With hindsight, it is difficult to see how HBL could have managed these risks given that it had no contractual relationship with all these parties, apart from its service level agreement with the HFA.

***Reporting on Implementation:
December 1998-April 1999***

3.045 The project plan for implementing the 2.7 system tabled at the internal HBL meeting of 12 January 1999 listed 148 necessary tasks, with their respective key dates. Some key dates included:



- testing of modem-based claims capture system, complete by 29 January 1999.
- testing of electronic *Pharmaceutical Schedule*, complete by 3 February 1999.
- pilot testing of software, to commence 1 March 1999.
- “roll-out” of the 2.7 system, to commence 9 March 1999 and scheduled to take 22 days.

3.046 However, we could find no reports of any kind on the progress in completing these tasks. In our assessment, this lack of reporting may have been because few (if any) of the 148 tasks were actually completed. The project seems to have suffered a breakdown in its management. The system was not ready for pilot testing on 1 March 1999 and (as discussed later) it was to be many months before the project reached this stage.

3.047 That the project was in trouble at this early stage was not the picture that HBL management reported to the HBL Board. HBL management provides monthly reports to its Board and we reviewed the nature of the reporting on the 2.7 system.

3.048 A report to the Board dated 9 December 1998 noted that the 2.7 system would be pilot tested in March 1999. At its January 1999 meeting, the Board asked for an update on the introduction of the 2.7 system. It is clear from a review of correspondence between Board members that they were concerned that HBL must meet the targets set to achieve electronic claiming.

3.049 There was also concern among Board members that HBL management could become distracted by the move to a single site at the expense of concentrating on the need to implement electronic claiming. Unless the 2.7 system was introduced, the move to a single site was not feasible.

3.050 In response to a request from the Board, a paper was presented to the February Board meeting stating that electronic claiming under the 2.7 system would start from 1 March 1999. The report said –

The strategy is to test each of the pharmacy systems through the last two weeks of February and thereafter to start with a limited number of pharmacies live claiming (approx.10-20). We will use pharmacies to actively test our systems with volume over a two week period and on the basis of our capability, manage a roll out rate of 50 (approx) every two weeks for the first two 6 weeks and then ramp it up to 100 per week (all going well).

- 3.051 Reference was made to another paper, also presented to the February Board meeting, which contained more detail on the project. That paper, dated 11 February 1999, set out the risks associated with the change to the 2.7 system and how these would be controlled. The dependency on other parties such as software suppliers, Pharmac, and the Pharmacy Guild was noted.
- 3.052 It was proposed to deal with these risks by regular meetings with all parties and ensuring that everyone was keeping to the agreed timetable. If the implementation of the 2.7 system was delayed beyond April 1999, more effort would be made to put pharmacists onto the 1.5 system.
- 3.053 Based on this information from management, the Board minutes for the February 1999 meeting concluded that *the change in the electronic claims process from 1.5 to 2.7 is proceeding and that the 2.7 process is being developed satisfactorily and implemented in the Wellington office.* Given the assurances provided to the Board by HBL management, it would have been difficult for the Board to have reached a different conclusion.
- 3.054 The HBL Board was again informed at its March 1999 meeting, in a paper dated 15 March 1999, that if implementation of the 2.7 system was delayed beyond April 1999, HBL would seek to put more pharmacists onto the 1.5 system. However, in the same month HBL had, in a newsletter to pharmacists, effectively discouraged pharmacists from switching to the 1.5 system.
- 3.055 The project plan submitted to the Board for the 2.7 system indicated that the 2.7 system was to be piloted at three sites, starting on 1 March 1999 and ending on 12 March. The plan also indicated that the 2.7 system would be made available to those pharmacists claiming under the 1.5 system over a 24-day period from 16 March to 14 April.

However, by March little progress had been made in implementing the 2.7 system. The Board was incorrectly informed that the project was still on track when very little work had in fact been completed.

- 3.056 In its quarterly reports to the HFA, what HBL management said about the state of the 2.7 project was also not correct. In its service level agreement with the HFA, HBL is required to report on any significant developments and achievement of agreed targets.
- 3.057 In its report to the HFA in February 1999 covering the quarter October-December 1998, HBL assured the HFA that . . . *the intention is to start electronic claiming using 2.7 from 1 April 1999. The issue holding us back at the moment is to be resolved in the next week.*
- 3.058 The HFA had a number of concerns with that quarterly report and wrote to HBL on 9 March 1999 expressing *extreme concern* with a number of issues, including the failure to meet agreed targets for electronic claiming. The HBL reply, dated 18 March 1999, stated that it still expected to meet the deadline of 30 June 1999 for most pharmacists to be claiming under the 2.7 system. Given the lack of progress with the 2.7 system and the failure to complete the testing of the system, HBL should have known that there was almost no possibility that by 30 June most pharmacists would be claiming under the 2.7 system.
- 3.059 We have also reviewed HBL's quarterly report for the period January-March 1999, which was prepared in April and sent to the HFA under a covering letter dated 1 May 1999. The report noted that HBL was behind in progress towards implementing electronic claiming, but said it was still expected to have 90% of pharmacy claims processed through the 2.7 system by late-July 1999. By the time this report was sent to the HFA it was clear that there was no chance of having most pharmacists claiming electronically by 30 June 1999.

A Fresh Start

- 3.060 In late-March 1999 HBL hired a new project manager, who carried out a strategic review of the project and produced a report dated 14 May 1999. While the report focused on the options for implementing electronic claiming, it also highlighted that the business plan targets would not be met and (consequently) the expected savings in processing would not be realised.
- 3.061 This report was presented to the May 1999 meeting of the HBL Board. It appears that this was the first time that the Board had been fully informed as to the true status of the project, and the lack of progress that had been made since December 1998.
- 3.062 A new data specification was developed and agreed to by the HFA, HBL, Pharmac, and the Pharmacy Guild on 11 June 1999. This data specification (which re-named the system 2.28) included a number of key changes and modifications to the 2.7 specification, allowing a fully electronic and automated claiming system.
- 3.063 Recognising that only the HFA could effectively co-ordinate and manage the various parties involved in this project, the HFA now took the lead in managing stakeholder relationships and in overseeing the project. The HFA appointed one of its staff as the overall project manager and appointed the General Manager of Pharmac as project sponsor. The latter is also the chairperson of the Steering Group.
- 3.064 Clear terms of reference for the project were written. Fundamental management elements of the project were to:
- establish a steering group of officials from HFA, HBL, and Pharmac;
 - establish a formal stakeholders' group comprising those officials plus the Pharmacy Guild; and
 - confirm who was responsible and accountable for each function.

- 3.065 This greater involvement of the HFA in the project also reflected its recognition that there had been a number of situations where the accountabilities between HBL and the HFA were not clear. For example, it was never clear who in the HFA was responsible for making decisions on the implementation of electronic claiming. A number of HFA staff tended to be involved, some of whom had inadequate knowledge or authority to properly represent the HFA's views.
- 3.066 The HFA sought to remedy this problem by ensuring that it had a single point of contact and that this person was of appropriate seniority, with a business focus and a good understanding of the business needs, priorities and financial implications of the project.
- 3.067 HBL also adopted a more rigorous approach to reporting to the HBL Board and improved the documentation of meetings and decisions made.

The Current Situation

- 3.068 In the period April to August 1999, the HFA and HBL devoted time and effort to meeting with all the various parties involved in electronic claiming and ensuring that there was participation in developing the processes and systems. The project steering group holds fortnightly teleconferences. There are regular (also fortnightly) meetings of the stakeholders to check on progress in implementing the new system and to discuss and resolve issues as they arise.
- 3.069 The key date of 4 October 1999 for the system to have been tested and be ready to receive claims was met. We were informed that planning is proceeding on the basis that those pharmacists currently submitting claims under the 1.5 system will be ready to submit claims under the 2.7 system in March 2000.
- 3.070 Following the successful testing of HBL's part of the 2.7 system the HFA decided that, to make further progress, it needed to contract with the two suppliers of pharmacy software. The objective was to ensure that the suppliers

- would meet implementation milestones and conform to the required quality standards for installation and operation of the 2.7 system in pharmacies.
- 3.071 Only one of the two software suppliers agreed a contract with the HFA. In accordance with the contract this supplier:
- first successfully tested the system on a trial batch of pharmaceutical items; and
 - has now piloted the system in eight pharmacies during January and February 2000.
- 3.072 So far the pilot testing has been successful. If the results of the testing for the second claim period demonstrate successful implementation of the system the stakeholder group will decide on whether the system is ready for nation-wide use.
- 3.073 The other software supplier will continue developing its system to meet the same contractual conditions as the first supplier.
- 3.074 As we were finalising the text of this article the Government announced that the Wanganui centre would continue to carry out claims processing.

Consequences of Not Implementing the 2.7 System by 30 June 1999

- 3.075 Not implementing the 2.7 system, and thus not eliminating manual processing at the Wanganui centre, by 30 June 1999 has had a financial cost. It now seems that achievement of the estimated annual savings of \$3.2 million (see paragraph 3.035) will not eventuate until 2000-2001. Both the HFA and HBL had prepared their budgets on the basis that these savings would be achieved in 1999-2000.
- 3.076 Significant improvements have been made to the manual processing systems at HBL Wanganui, and HBL has said that it has the capacity to continue with manual claiming. However, we note that it takes up to three months to train new processing staff. If significant numbers of key

processing staff were to leave, HBL could face real problems in coping with the volume of manual claims until more pharmacists are able to claim electronically.

Risks to be Managed

3.077 In completing implementation of the 2.7 system there are four main areas of risk that will need close attention.

Co-ordinating the Parties

3.078 The 2.7 system involves many parties, all of whom have to agree and synchronise their actions to ensure that the system is successfully implemented. The need for this co-ordination of activities will continue after the system has been implemented. To reduce any future risk of lack of proper co-ordination, the current fortnightly meetings of the key parties need to be continued.

Progress Reporting

3.079 The Board of HBL now receives regular and detailed reports on the state of the project. However, to reduce any future risk of the Board being given incorrect information on the state of a key project, the Board needs to insist on receiving regular reports on all projects. These reports – which should feature as a fixed item on Board agendas – need to show actual progress compared to planned progress, with detailed explanations given of any delays.

Loss of Experienced Staff

3.080 The announcement of the closure of HBL Wanganui led to staff seeking employment opportunities elsewhere. The closure has not yet happened, but the priority for many staff will now be to find other work. The need to continue in the meantime with manual processing, together with reduced staff levels and in an environment where staff now know the centre will definitely close, exposes HBL to the risk of again falling behind in processing claims from pharmacists.

3.081 Notwithstanding the improvements to the manual processing systems at HBL Wanganui, until significant numbers of pharmacists are switched to the 2.7 system there is a continuing risk of another backlog of work building up. Should there be significant delays in implementing the 2.7 system, HBL will need a contingency plan to ensure that payments to pharmacists continue to be handled in a timely manner.

New System Risks

3.082 The 2.7 system is a substantial improvement on existing processing systems. However, it presents new risks in terms of accurate data and audit requirements. These risks will need particularly close attention.

Summary and Conclusions

3.083 During 1998, HBL embarked on a programme of convincing pharmacists to take up a form of electronic claiming known as the 1.5 system. By March 1999, about 300 pharmacists were claiming under this system.

3.084 However, in the latter part of 1998, HBL and the HFA became convinced that a new system known as 2.7 was much superior. The 2.7 system allowed pharmacists to electronically submit fully priced claims for the medicines dispensed. The HFA contracted North Island and some South Island pharmacists to claim under the 2.7 system, once it was operating.

3.085 In 1998, HBL saw significant efficiencies in basing all its processing operations at one site. The original HBL plan was to move to a single site in 2000-2001, by which time all of its electronic claiming systems would be in place. HBL decided to bring forward this consolidation and in February 1999 announced that the Wanganui centre would be closed by 30 June 1999. A key factor permitting the closure of Wanganui was implementation of the 2.7 system.

3.086 However, the announcement of the closure of the Wanganui centre was made without the 2.7 system being fully developed and tested to ensure that it worked.

- 3.087 In the initial stages of the project to implement the 2.7 system unrealistic target dates were given. The dates were not met and HBL management incorrectly reporting the status of the project compounded the problem.
- 3.088 HBL has over-promised and under-delivered on the pharmacy electronic claiming project. However, it was never for HBL to promise that it alone could deliver the implementation of the project. Had there been a clear definition of the project at the outset – and a comprehensive system specification available to pharmacy software suppliers – there would have been a realisation that HBL, as a service provider to the HFA, lacked the authority and mandate to successfully co-ordinate the various parties. This was a task for the HFA.
- 3.089 There are now tight controls over the management of this project, including a system of reporting against key events.
- 3.090 The system has now been successfully piloted in a small number of pharmacies.

Lessons to be Learned

- 3.091 There are several lessons to be learned from what has happened with the project to implement electronic claiming.
- Where other parties have a key role in ensuring the success of a project, they need to be involved in the project at the outset and (where possible) formal links established with them. Their involvement – and the information made available to them – needs to be at a level where they can have confidence that the project will succeed.
 - The introduction of complex projects, such as pharmacy electronic claiming, needs to be well managed from the beginning, otherwise it is very difficult to make up lost ground. To prevent bad starts on such projects in the

future, there needs to be clear and early specification of system requirements, and strict monitoring of the project plan, the progress achieved, and the reasons for any delays.

- Where one party has an overall responsibility for implementing a project, that party must be represented by one appropriately senior person who understands the needs, priorities, and financial implications of the project.
- Particular care needs to be given to project responsibility and control during times of significant organisational change.

3.092 The events described in this article offer a useful case-study of object lessons for decision makers in considering future similar projects.



Forthcoming Report

- 4.001 In the next month we will be publishing a detailed report on the governance and oversight of large information technology (IT) projects in the public sector. This article summarises the key messages from the detailed report.
- 4.002 Recent, highly publicised difficulties with public sector IT projects – such as the National Library and Police INCIS projects – have focused public and political attention on them. Problems have included failure to deliver what was required and major time and cost overruns.
- 4.003 Difficulties with IT projects are not new, or confined to the public sector or (indeed) to New Zealand. Much has been written about the need for sound project management, and the principles of effective project management are well known. Yet the difficulties with IT projects continue. Lessons learned are not shared, and the same mistakes recur from project to project and from entity to entity.
- 4.004 We did not think it would be useful to revisit the issues of project management in detail. Instead, we decided to examine the problem from the angle of governance and oversight – the top levels of IT projects.
- 4.005 The public sector is a far more open and transparent environment than the private sector, and the chains of authority and decision-making are longer. While private sector chief executives might only have their board of directors to account to, public sector chief executives must consider:
- the monitoring role of central agencies;
 - their own Ministers; and
 - potential Parliamentary and public interest.
- 4.006 The detailed report will refer to all aspects of large IT projects in the public sector. But it concentrates on, and its most important findings are for, chief executives, Ministers, and members of Parliament in their Select Committee roles – the top of the governance and oversight

chain. The report will be written for central government, but its principles will be applicable to the whole Crown sector and (at least partially) to local government and the private sector as well.

- 4.007 The principles in the detailed report will distil current wisdom about large IT projects. While we expect most of the principles to stand the test of time, both principles and processes must be constantly refreshed in a rapidly changing environment. Key players must remain alert to changes that might challenge or complicate the principles.
- 4.008 For example, current work to spread information across agencies and sectors, for policy and other purposes, complicates the roles and accountabilities for development and management of systems. Such changes do not invalidate the principles – they merely make them harder to apply.

Key Messages

- 4.009 The detailed report will discuss:
- basic governance structures for IT projects;
 - how IT projects actually happen; and
 - reasons for success and failure.
- 4.010 Each section of the report will raise issues for consideration, summarised in a set of questions which we believe that chief executives, Ministers, and Select Committee members should ask with respect to any large IT projects they are involved with.
- 4.011 Our key messages for each of these three groups are set out in the following paragraphs.



Key Messages for Chief Executives

- 4.012 Chief executives play a linchpin role in the success of major IT projects. Often, these projects are cornerstones of the entity's business plans, including change and development strategies. The chief executive therefore has a major interest in the project's success. However, the chief executive is critically dependent on the quality of the people directly involved in the project, and on continuity in the department's business purpose and strategies over the long implementation time of the project.
- 4.013 The risk that a large IT project will divert key resources from normal operations – to the detriment of the day-to-day delivery of core services – needs to be carefully managed.

Project Management

- 4.014 The chief executive may well act as sponsor for a large IT project – particularly a project with significant business implications. Nevertheless, the chief executive must guard against being either too close to the project to assess purpose and progress objectively, or too remote to be aware of significant changes in status or risk.
- 4.015 The project manager for a significant IT project should have:
- a suitable track record;
 - the confidence of organisational sponsors and central agencies; and
 - suitably designed incentives to see the job through successfully.
- 4.016 The larger and more complex a project is, the more likely it is that a co-operative relationship with a competent lead supplier may be more effective than an arm's-length relationship based on tight output specifications.
- 4.017 In any event, the chief executive (or a senior business manager) of the lead supplier needs a forum within which to communicate with the departmental sponsor, as the supplier also has a significant stake – financially and for its reputation – in the successful outcome of the project. A project steering committee may provide this.

The Contract

- 4.018 The project contract should protect the interests of the Crown while establishing a proper legal environment for a relationship with the supplier that will stand for the duration of both the project and any subsequent support contract.

Quality Assurance

- 4.019 Independent quality assurance processes need to be established for most significant projects. The processes should concentrate, and report clearly to the chief executive, on possible or planned scope changes and how project risk is being managed.

Implications of Legislative Change

- 4.020 The Minister and the relevant Select Committee should be made aware of:
- the impact that any planned legislative changes would have on a project; and
 - whether these changes are being sponsored by the chief executive's department or by another department or entity.

Key Messages for Responsible Ministers

- 4.021 Responsible Ministers are accountable to Parliament for the performance of their departments and, hence, for the departments' performance in managing projects. Ministers are heavily dependent on both central agencies and the departments themselves for information about the likely benefits, progress, and risks associated with projects being proposed or undertaken.

The Business Case

- 4.022 The Minister should expect the business case for a new project to clearly state, in measurable terms, what it will do for the department and for taxpayers – i.e., the intended business outcomes of the project. The risks identified in the business case should be relevant, based on the experience of competent advisers, reasonable (i.e. not understated), and show an understanding of the range of uncertainties in the project.
- 4.023 The business case should also include provision for sufficient funding to support competent, independent, quality assurance. The quality assurers should report to the project steering committee and the chief executive, and the assurers' unedited reports should be available to the Minister and central agencies.

Funding

- 4.024 Appropriations for funding will often be made either at a bulk level or so early in a project's life that cost and time estimates are very uncertain. Such contingencies and uncertainties should be clearly spelt out in the business case and, if not initially appropriated for, acknowledged and tracked for potential future supplementary appropriations.

Monitoring

- 4.025 Central agencies have clearly defined roles in monitoring the development of business cases and the progress of projects. The Minister should expect sound advice from them on these matters, based on their applying sufficient, competent resources to the project in question.
- 4.026 Regular project reports to the Minister should be brief, to the point, and factual. Reports should specify progress against the benchmarks established in the initial business case and details of progress for the latest reporting period. Reports should also keep the Minister informed on key risks, changes in key risks, and the effect of those changes on promised project outputs and outcomes.

- 4.027 The chief executive should also give the Minister confidence that the department is in full control of the issues identified in the “Key Messages for Chief Executives”.

Key Messages for Members of Select Committees

- 4.028 Select Committees perform an important oversight function on behalf of Parliament and taxpayers. Through reviews of the *Estimates*, financial reviews, or inquiries, the Committees hold the Executive to account for its plans and actions. They do not have a hands-on management role but, as part of the oversight process, they have a reasonable expectation of being informed of planned major initiatives, and of progress on those initiatives.
- 4.029 Recent difficulties with major projects have diminished the confidence of some Select Committees in Executive performance and accountability for IT projects. Accordingly, the major objective of our tackling the subject has been to help Select Committees carry out their oversight role with more confidence in the outcome.

Central Agency Monitoring

- 4.030 Central agency monitoring roles have been clarified, and their capabilities are being strengthened, in order to improve oversight of departmental IT projects.

Information from Departments

- 4.031 A committee should expect information from the department on plans for, or progress on, large IT projects as part of their *Estimates* or financial review reporting. The information should have the characteristics identified above for reports to the Minister.
- 4.032 If a committee has concerns about project plans, risks, or progress, the most important factors for it to inquire into are those identified above in the key messages to chief executives and Ministers.

Implications of Legislative Change

- 4.033 When evaluating new legislation, a committee should expect advice from the department on the impact that the changes will have on its work in progress and the costs or risks which might be created by the legislative change.

Use of Example and Case Studies

- 4.034 The detailed report will illustrate the themes that have emerged by using:
- the example of an imaginary government department; and
 - actual case studies.
- 4.035 We have created a cameo of an imaginary government department – the Department of History and Ideas (DHI) – which is automating its core business processes to provide Internet access to citizens. The programme is in trouble because the DHI has made all the major mistakes possible. The cameo is not based on an actual case, but built up from events that have actually occurred in a range of public sector entities.
- 4.036 In the detailed report, each episode of the DHI story will look like this:

The Department of History and Ideas (DHI) has been part of the Public Service for almost 100 years. Its role is twofold – to collect and record information on all aspects of New Zealand society relating to human endeavour and to disseminate the material through any medium available to citizens.

Successive governments have cut back its budget but it would be politically damaging to close it down as it is a well-loved resource for advertisers, teachers, sports coaches, writers and crossword puzzle experts. A new Chief Executive was appointed two years ago and charged with the task of preparing the department to be restructured as an SOE. The Chief Executive reports to the Minister of Culture and has an annual vote of \$16 million.

The DHI has had approval to convert all its material into digital format and automate its systems for gathering, codifying, documenting and disseminating the material. Cabinet approved the Historical Modernisation project (HISTMOD) in 1998 with a budget of \$6.5 million and an implementation time of 2½ years.

- 4.037 The detailed report will also use actual case studies of projects that have been successful or provide useful lessons. Each case study will look like this:

Real examples of the theme for each section are taken from the following projects:

Land Transport Safety Authority – Drivers Licence Project

Department of Social Welfare – FOCIS Programme

ASB Bank – major development project

Inland Revenue Department – FIRST Programme

New Zealand Customs Service – Customs Modernisation Programme (CusMod)

Land Information New Zealand – Land*online*

Ministry of Agriculture and Forestry – Service Provision Project, Standard Desktop Project

National Library – NDIS Project



Summary

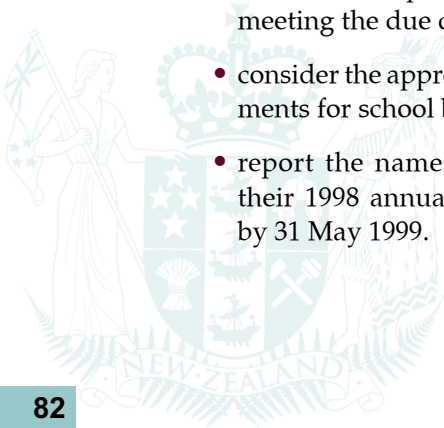
- 5.001 We have reported to the House three times on the accountability and audit of school boards of trustees (school boards) and the related issue of timeliness of reporting.¹
- 5.002 We commented favourably in our *Third Report for 1998* on the timeliness of reporting by school boards, and we do so again in this report. However, we are unable to report any significant improvement in meeting the requirements of the Public Finance Act 1989 for the issue of the audit reports within 30 days of receiving the financial statements.
- 5.003 The two different times for reporting – in the Education Act 1989 and the Public Finance Act – have different incentives associated with them. The consequences of failing to meet the Education Act deadline for school boards to forward their annual report to the Ministry of Education can be considerable. Boards and our auditors are also conscious that external accountability to the Minister of Education and parents – not solely the meeting of audit deadlines – is the essence of the reporting requirement.
- 5.004 Further, the requirement in the Public Finance Act does not take into account the realities of the school board audit or, indeed, of the audit process itself.
- 5.005 Therefore, in our opinion it would be more in keeping with the special circumstances that apply in the schools' sector, and with the accountability intentions, for the requirements of section 43 of the Public Finance Act in respect of school boards to be reviewed.

1 *First Report for 1997*, parliamentary paper B.29[97a], pages 93-105; *Third Report for 1997*, parliamentary paper B.29[97c], pages 81-87; and *Third Report for 1998*, parliamentary paper B.29[98c], pages 25-28.

- 5.006 Instead, and in order to focus on the outcome of timely reports to the stakeholders, it might be more appropriate to require a school board to:
- prepare its annual report, to include its *audited* financial statements, within five months of balance date;
 - make its annual report available to all parents and to the Ministry of Education within five months of balance date; and
 - in the case of parents, make the annual report available to them no less than 20 working days before the annual meeting.
- 5.007 There could be a consequential need to adjust the annual meeting requirements of the board.
- 5.008 We recommend a review of the two accountability requirements for reporting to Parliament on the schools' sector (see paragraph 5.018) to ensure that –
- the most recent financial information can be available; and
 - the appropriate administrative action can actually be carried out.

Purposes of This Article

- 5.009 The purposes of this article are to:
- describe the accountability requirements for school boards in the context of other accountability requirements;
 - describe the performance trends of school boards in meeting the due dates under those requirements;
 - consider the appropriateness of the accountability requirements for school boards; and
 - report the names of school boards that failed to send their 1998 annual report to the Secretary for Education by 31 May 1999.



The Accountability Requirements

Interests of Stakeholders

- 5.010 In most contexts, timely audited financial statements are recognised as an important element of accountability. For example, the board of every company is obliged to prepare an annual report² containing the audited financial statements³.
- 5.011 The focus of reporting by companies is on the accountability of the board of directors to the shareholders. The financial statements and any auditor’s report must be made available to every shareholder every year, before the annual meeting. The pre-eminent interest of a company’s shareholders is in the value of its shares. We would expect the audited financial statements to play an important role in a company’s accountability regime.
- 5.012 School boards have two principal stakeholders to whom they are accountable: the parent community and the Minister of Education. The accountability requirements for a school board in respect of these stakeholders are similar to those for the board of a company to its shareholders – but there are some important differences.
- 5.013 Audited financial statements also provide an important source of assurance to the school board’s two principal stakeholders. This is recognised in the Education Act, where the board is required to report as a Crown entity under the Public Finance Act.

2 Companies Act 1993, section 208 (1).

3 Ibid, section 211(1)(b) and (c). An auditor’s report on the financial statements is not required following a unanimous resolution by shareholders that no auditor be appointed for the year under section 196(2). Every listed company is required to have an auditor.

5.014 In our 1997 report we noted (in particular) the importance of the accountability of school boards to their local communities, and stated that:

In our opinion, audited financial statements should be available for the annual meeting. Otherwise the school community will not have the benefit of independent assurance that the contents of the financial statements are reliable.

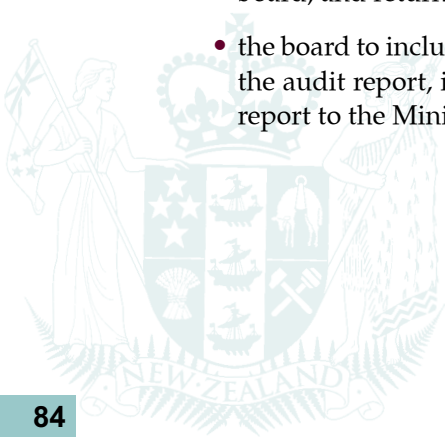
5.015 However, we would expect the school's stakeholders to have an overriding interest in the quality of educational outcomes. The accountability regime in the schools' sector gives greater emphasis to reporting – certainly in school reports to parents, for example – on educational achievement than on financial performance. We discuss the matter of reporting service performance in paragraphs 5.037-5.040.

5.016 The reporting and audit requirements of school boards are compared with those of government departments, other Crown entities, and companies in Figure 5.1 opposite.

Public Finance Act Requirements

5.017 The Public Finance Act requires:

- every school board (as a Crown entity) to prepare annual financial statements in the prescribed form and send them to the auditor within 90 days of the balance date of 31 December;
- the auditor to issue an audit report on the statements within 30 days of receiving the statements from the board, and return the statements to the board; and
- the board to include the audited statements, together with the audit report, in its annual report and send the annual report to the Minister of Education.



*Figure 5.1
Comparative Reporting and Audit Requirements*

Entity	Financial Statements To Auditor	Audit Report Issued	Annual Report To Stakeholders
Government department	Within 60 days of balance date.	Within 30 days of receipt of financial statements.	To Minister who must present it to the House within 6 sitting days of being returned by the auditor.
Crown entity	Within 90 days of balance date.	Within 30 days of receipt of financial statements.	To Minister who must present it to the House within 6 sitting days of being returned by the auditor.
School board	Within 90 days of balance date.	Within 30 days of receipt of financial statements.	To parents by 3rd Tuesday in May. To Ministry by 31 May. ⁴ Schools' sector report of Minister by 30 June. To electorate MP within 1 month of audit report being issued.
Company	Not specified.	Not specified, but with annual report (within 5 months of balance date).	Within 5 months of balance date. ⁵

⁴ The annual report may or may not include audited financial statements.

⁵ The annual report has to be distributed not less than 20 working days before the annual meeting, which must be held within 6 months of the balance date (Companies Act 1993, section 120).

5.018 The Minister in turn has two responsibilities under the Public Finance Act:

- to report to the House by 30 June each year on the performance of the schools' sector in the immediately preceding financial year;⁶ and
- to send to each member of Parliament a copy of the audited financial statements of schools in their electoral district⁷ within a month of the audit report being issued.

Education Act Requirements

5.019 The majority of schools' funding comes from money appropriated by Parliament. Therefore, the State also has a key interest in the schools achieving the administrative and educational objectives specified by the State. This is recognised by the Education Act requiring that:

- each school has a charter that is an undertaking by the school's board to the Minister with respect to the good management of the school and achievement of the objectives approved by the Minister;
- every school board has to report to parents at an annual meeting to be held between 31 March and the third Tuesday in May; and
- every school board must make its annual report available to the Minister of Education at a date specified under section 87 of the Act.

5.020 Reporting on the charter undertaking is an important aspect of the accountability arrangements for school boards. Therefore, the Minister can be expected to have a keen interest in the audited financial statements.

5.021 The Education Act requirement to have the annual report and financial statements available to the annual meeting compares with the Companies Act requirement. However, the important difference is that the Education Act stops short of making it mandatory for *audited* financial statements to be available at the annual meeting.

⁶ Public Finance Act 1989, section 44b.

⁷ Public Finance Act 1989, section 44c.

5.022 The Secretary for Education has fixed 31 May as the date by which the board's annual report (including the audited financial statements) is to be sent to the Ministry. This deadline is consistent with the five months from balance date within which the majority of companies have to prepare their annual report.

Trends in the Timeliness of Meeting Due Dates

5.023 Having reported on the timeliness of reporting by school boards over a five-year period, we are able to identify some particular trends in meeting the reporting and audit deadlines for:

- forwarding [by the board] of financial statements for audit;
- issuing [by the auditor] of the audit report; and
- reporting to the stakeholders.

5.024 The data behind these trends is set out in Tables 5.1 and 5.2 on pages 95-96.

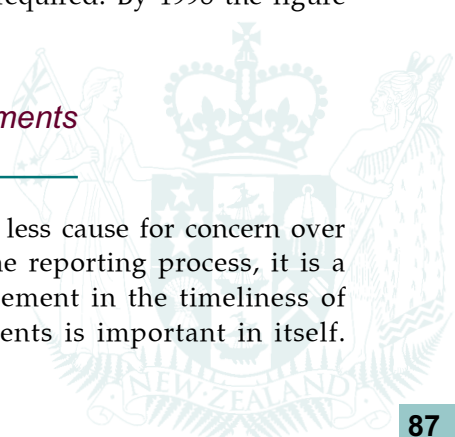
Forwarding of Financial Statements for Audit

5.025 Financial statements are now being forwarded for audit on a more timely basis.

5.026 For 1994 our auditors reported that only 65% of boards sent their financial statements to them within 90 days of the end of the financial year, as required. By 1998 the figure had increased to 83%.

Quality of Financial Statements Forwarded for Audit

5.027 While there is apparently far less cause for concern over timeliness at this stage in the reporting process, it is a moot point whether improvement in the timeliness of forwarding financial statements is important in itself.



The quality of the financial statements received for audit is critical if the outcome of timely and reliable external reporting is the important concern. If the financial statements are of inadequate quality the audit report may be held up, and reporting to the stakeholders may be seriously delayed.

- 5.028 In this respect we note an increasing unwillingness on the part of our auditors to accept clearly substandard financial statements. There may be a case for increased advisory support from the Ministry of Education if school boards are to raise the quality of the financial statements to the level where they are acceptable when first submitted.
- 5.029 We acknowledge that the Ministry has recently increased the number of financial advisers from three to six, and note the Ministry's objective to make on-site visits to schools whose financial statements indicate areas of concern.⁸ We will be interested in the effects of this increased support.

Issuing of Audit Reports

- 5.030 There has been only slight improvement in the timeliness of the issuing of audit reports. We have drawn attention previously to this area as being of most concern.
- 5.031 Only about 30% of audit reports were issued within the statutory deadline each year over the period 1994-1997. For 1998, the proportion of audit reports that were issued within 30 days of the statutory deadline for receipt of the financial statements showed only a slight improvement, at 32%. The reasons for this are discussed later in paragraphs 5.049-5.053.

⁸ Ministry of Education, *Forecast Report 1999-2000*, parliamentary paper E.1FR(99), page 38.

Forwarding the Annual Report to the Ministry

- 5.032 School boards are improving their compliance with the deadline for sending their annual report to the Ministry of Education. In 1994 only 63% of boards had audited financial statements by 31 May – the deadline for sending their annual report to the Ministry. By 1997 the figure was 87%, and for 1998 it was 89%.
- 5.033 In our view, strong incentives have supported this steady improvement in meeting the reporting requirement. Failure to comply with this particular deadline may, and sometimes does, result in the Ministry withholding the next quarterly payment of the operations grant.
- 5.034 A board that breaches the 31 May deadline is also at risk of being named in a report such as this. These consequences therefore represent a greater risk than not meeting the 30-day deadline for the audit report to be issued, from which no such consequences result.

Making the Annual Report Available to Parents

- 5.035 We are aware that the requirement to have audited financial statements available to the annual meeting (which must be held between 31 March and the third Tuesday in May) is important to some school boards. However, this is not the general case. While we do not have specific data, we know that:
- boards usually regard the annual meeting as –
 - a formality;
 - poorly attended; and
 - not an effective mechanism for communicating with parents;⁹
 - the Education Act allows boards to present unaudited financial statements to the annual meeting¹⁰; and

9 See also Wylie, C *The Impact of Tomorrow's Schools in Primary Schools and Intermediates 1990 Survey*, NZCER Wellington 1991, page 62. Over a quarter of schools had no parents at their annual meeting. The usual meeting attracted 1-20 parents. Later surveys of the impact of the reforms did not retain the question relating to annual meetings, as they were so poorly attended.

10 Education Act 1989, section 100(2)(b).

- there is no equivalent to the Companies Act requirement that all shareholders have a copy of the annual report and the audited financial statements not less than 20 days before the annual meeting.

5.036 Given the importance of accountability to parents, in our view the current requirement needs to be reviewed to better achieve the intent that parents be fully informed in a timely way of the state of the school. We believe that the requirements should be such as to ensure that:

- the audited financial statements are available to every parent within no less time than would be expected by the Minister or, for instance, the shareholders of any listed company;
- parents receive at the same time an appropriate statement about the school's performance in delivering education (its service performance – see paragraphs 5.037-5.040); and
- the statements are received with ample time to consider them before the annual meeting, since that is the appropriate opportunity for the board to answer to its parent community for its performance.

Reporting Service Performance

5.037 In our *First Report for 1997*, we drew to Parliament's attention the importance of reporting service performance and the adverse effects of exempting boards from the requirement to so report.

5.038 The Minister of Finance can exempt school boards from having to prepare any of the required financial statements that *would be unduly onerous on the Board*.¹¹ A result of this has been the exemption for several years of school boards from preparing a Statement of Service Performance (SSP). As a consequence a school board's financial statements may have no SSP or, if they do, the SSP may be of poor quality. If an SSP is presented it will not be audited.

¹¹ Public Finance Act 1989, section 41A(2)(b).

- 5.039 Parents have to depend for information about the educational performance of the school on the less frequent reviews by the Education Review Office. In our 1997 report we observed that:

It could be argued that, of all the financial statements prepared by a board, the SSP is the most important.

- 5.040 The issue of reporting service performance remains unresolved, despite some attention having been given to it by a Ministerial inquiry.¹² We intend to raise this matter again in a subsequent report.

Appropriateness and Feasibility of the Statutory Auditing Requirements

Time-related Requirements

- 5.041 The time within which a company's auditor must complete the audit is dictated solely by the requirement placed on the board to make its audited financial statements available in the annual report within five months of the balance date. The situation is quite different in respect of the audit of schools and other Crown entities. (See Figure 5.1 on page 85.)
- 5.042 Section 43 of the Public Finance Act requires the auditor of a Crown entity (including a school board) to issue the audit report within 30 days of receiving the annual financial statements. These must be forwarded to the auditor within 90 days of the end of the financial year.
- 5.043 Thus, company audit requirements are focused on the final outcome – the timely availability of the annual report and audited financial statements – while Crown entity audit requirements are aimed as much at each step in the process toward that outcome.

¹² *Review of the Education External Evaluation System*, Wellington, 1997.

- 5.044 In our view, the Public Finance Act's auditing requirements could be improved to focus on the outcome of a timely report to key stakeholders and to be more practical.

Accountability to Parliament

- 5.045 We believe that consideration needs to be given to the reasonableness of two other accountability requirements.
- 5.046 The Minister's annual schools' sector report is required to contain information for the immediately preceding financial year ended on 31 December.¹³ However, the 1998 report was published in June 1999, and contained financial information for the 1997 financial year – not *the immediately preceding financial year* – and non-financial data relating to 1998.
- 5.047 We also observe that audited financial statements are not always getting to members of Parliament within the time prescribed by the Public Finance Act. Not unexpectedly, the Ministry forwards the school board's annual report to the member of Parliament within a month of receiving it – not within a month of the issuing of the audit report (since it is not required to be forwarded to the Ministry at that point). Consideration needs to be given to whether this accountability requirement is realistic.

A Case for Different Treatment

- 5.048 The Public Finance Act (as noted in paragraph 5.038) acknowledges that school boards warrant different consideration from other Crown entities as far as reporting is concerned. We also note the following differences in audits between school boards and other classes of entity:
- two different times for reporting exist – one in the Public Finance Act and one under the Education Act – which tend to be counteractive (see paragraphs 5.017 and 5.022);
 - there is a considerably greater volume of school board audits (approximately 2,700) than for any other class of Crown entity; and

¹³ Public Finance Act 1989, section 44b.

- the quality of financial statements submitted by school boards for audit is not as consistently good as those submitted by other Crown entities.
- 5.049 The workload of school board audits falls on a small number of auditors (often domiciled outside the large centres). Most of the auditors handle between 10 and 60 school board audits in a year. One firm audits 200 boards, and several audit over 100 boards. Thus, it may be difficult for our auditors to achieve a turn-around on all of the audits in the 30 days required by the Public Finance Act.
- 5.050 Financial statements all tending to arrive at the same time exacerbates the effect of the high volume of audits. For the 1998 year (see Table 5.2 on page 96):
- only 23.7% of school financial statements were received by our auditors by early March 1999; and
 - nearly 60% of school financial statements were received in March 1999 – over a quarter in the last week, including the 14.8% that were received on the very last day of March.
- 5.051 The standard of the school board financial statements that are initially forwarded to our auditors is often of poorer quality than those of other Crown entities. The people preparing the statements, especially for the smaller school boards, may be relatively unskilled. Some financial statements forwarded to our auditors are of “first draft” standard.
- 5.052 The auditor may have to engage in a major reconstruction exercise on the material presented, involving numerous queries and consultations with the relevant staff or accounting services provider. Should on-site work be required in such circumstances, the schools – unlike other Crown entities – are often distant from the auditor.
- 5.053 The availability of staff and school board members in the period when the audit is meant (according to the Public Finance Act) to take place is considerably affected by the nature of the education business – schools go on holiday while the audit is in progress. This is not the case with other Crown entities. While other timeliness requirements in March and May have improved in spite of this, the audit process is more vulnerable.

5.054 For all of the reasons already outlined, and in keeping with the special circumstances that apply in the schools' sector, we believe variations to the accountability and (particularly) audit requirements are appropriate.

5.055 Instead of the current requirements, the accountability and audit requirements for school boards should:

- focus on the outcome of timely reports to the stakeholders – in particular parents and the Minister as the two principal stakeholders – rather than on the steps in the process towards that outcome;
- require the board to prepare its annual report – to include its audited financial statements – within five months of balance date;
- require the board to make its annual report¹⁴ available to all parents within five months of balance date (that is, by 31 May), but in any case at least 20 working days before the annual meeting; and
- require the board to make its annual report available to the Ministry within five months of balance date (that is, by 31 May).

5.056 The present deadline for forwarding the annual report to the Ministry by 31 May would not change. Some concerns have been expressed to us that removal of the requirement for school boards to forward the financial statements to the auditor within 90 days of balance date is unnecessary and risky, given the already good timeliness of boards. We have some sympathy for this view.

5.057 However, the suggested change would shift the emphasis from an inappropriate focus on the audit process to an accountability outcome. There could be a consequential need to adjust the annual meeting requirements of the board (see paragraph 5.019).

¹⁴ The Companies Act 1993 allows the shareholder to waive the right to receive the annual report, but the shareholder *must be sent* the audited financial statements.

- 5.058 We believe it is no more risky to shift the focus to the accountability outcome – the external reporting deadline (currently 31 May) – which already has the added advantage of being subject to strong incentives (see paragraph 5.033).
- 5.059 Our proposals have the added benefit of all parents – not only those attending the annual meeting – being properly informed.

Naming Of Boards That Failed To Meet the Statutory Reporting Requirement – 1999

- 5.060 We have twice – for the 1995 and 1997 financial years – named those school boards that had failed to meet the statutory reporting deadline of 31 May fixed by the Secretary for Education.
- 5.061 This year we have chosen again to name the boards for which the audit report was signed after 31 May 1999 and where the delay in reporting cannot be attributed, in part or in whole, to the auditor. The boards are listed in Table 5.3 on pages 97-98.

*Table 5.1
Compliance with Reporting Deadlines 1994-1998*

Financial Year	Financial Statements To Auditor %	Audit Report Issued %	Annual Report to the Ministry %
(to 31 December)	(+90 days)	(+30 days)	(by 31 May)
1994	65	30	63
1995	61	25	70
1996	69	28	78
1997	79	30	87
1998	83	32	89

Table 5.2
Distribution of Auditor Receipt of Financial Statements for the Year Ended 31 December 1998

Week Ended	Number of Financial Statements Received		% of Financial Statements Received	
	For the Period	Cumulative	For the Period	Cumulative
to 6 Jan 1999	8	8	0.3	0.3
13 Jan 1999	1	9	<0.1	0.3
20 Jan 1999	4	13	0.2	0.5
27 Jan 1999	14	27	0.5	1.0
3 Feb 1999	36	63	1.4	2.4
10 Feb 1999	75	138	2.8	5.2
17 Feb 1999	117	255	4.4	9.6
24 Feb 1999	177	432	6.6	16.2
3 Mar 1999	203	635	7.6	23.8
10 Mar 1999	247	882	9.2	33.0
17 Mar 1999	274	1,156	10.3	43.3
24 Mar 1999	322	1,478	12.1	55.4
31 Mar 1999	727	2,205	27.2	82.6
from 1 April	464	2,669	17.4	100.0

*Table 5.3
School Boards that Failed to Send Their 1998 Annual Report to the Secretary for Education by 31 May 1999*

Aranga	Paerata
Avalon Intermediate	Pakaraka
Avalon	Parkway
Bideford	Patutahi
Cannington	Penrose High
Cobham	Piopio
Collingwood Intermediate	Pongakawa
Dannevirke High	Pukekohe Intermediate
Evans Bay Intermediate	Pukeoware
Greytown	Punaruku
Hataitai	Puriri
Hinuera	Rangitahi College
Huntermere Consolidated	Raphael House Rudolf Steiner
Kotuku Rudolf Steiner	Raumanga Intermediate
Kuranui College	Rawene
Linden	Reporoa College
Mahana	Rewa Rewa
Masterton East	Riverdale (Gisborne)
Maungati	Riverview
Minginui Forest	Russell (Porirua)
North Taieri	Saint Bernard's (Brooklyn)
Omihi	Saint Joseph's (Dargaville)
Opoho	Saint Joseph's (Paeroa)
Opua	Saint Mary's (Blenheim)
Orauta	Saint Patrick's (Wainuiomata)
Oruawhoro	Saint Stephen's (Bombay)
Otangarei	Sara Cohen
Oxford Crescent	South End
Paekakariki	South Wellington Intermediate
Paengaroa	Taipuha



Tairangi	Te Kura Kaupapa Maori o Whakawatea
Tangiteroria	Te Kura Kaupapa o Nga Mokopuna
Taupo Intermediate	Te Kura o Rangiriri
Tawa College	Te Kura Reo Rua o Matawaia
Te Aro	Te Puia Springs
Te Horo (Whangarei)	Te Wharekura o Rakaumangamanga
Te Kopuru	Tikitiki
Te Kura Kaupapa Maori o Hoani Waititi Marae	Tirohia
Te Kura Kaupapa Maori o Mangere	Waikirikiri Bilingual
Te Kura Kaupapa Maori o Piripono Te Kura Whakahou (Otago)	Waiohau
Te Kura Kaupapa Maori o Te Raki Paewhenua	Waitara Central
Te Kura Kaupapa Maori o Waipiro	Waitotara
Te Kura Kaupapa Maori o Whakarewa Te Reo	Wakanui
	Whakatane High
	Wharekahika



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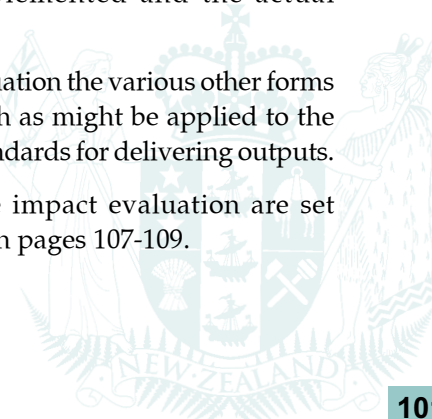
Introduction

Purpose of This Article

- 6.001 This article is intended to demonstrate the value of impact evaluation as a practical tool to enhance the quality of decision-making by the Government and Parliament. For impact evaluation to be valuable, decision makers need to:
- have a commitment to basing decisions on the best available information, consistent with their “world view” and the political context; and
 - accept that enhanced decision-making will contribute to optimising the effectiveness of government expenditure.

The Nature of Impact Evaluation

- 6.002 We understand “impact evaluation” to be a short-hand term for a particular form of performance assessment, the purpose of which is to:
- determine the actual outcomes from putting a policy into effect;
 - compare those outcomes with the desired outcomes when the policy was formulated; and
 - confirm or establish the causal link between the means by which the policy was implemented and the actual outcomes.
- 6.003 We do not regard as impact evaluation the various other forms of performance assessment such as might be applied to the achievement of performance standards for delivering outputs.
- 6.004 Our expectations for effective impact evaluation are set out in paragraphs 6.024-6.026 on pages 107-109.



A Survey and Case Studies

- 6.005 We conducted a survey to establish the extent to which government departments were using impact evaluation. We discuss the survey and its results in paragraphs 6.027-6.068 on pages 110-117.
- 6.006 To illustrate the subject, we present and comment on two case studies in paragraphs 6.069-6.130 on pages 118-130.

Other Commentary

- 6.007 We discuss the place of impact evaluation in the public management system in Appendix A on pages 131-136, and describe the current legislative framework in Appendix B on pages 137-139.

Our Objectives

- 6.008 Our overall objectives are to:
- develop the discussion of the subject that we began in our *Third Report for 1999 – The Accountability of Executive Government to Parliament*;
 - create a greater awareness among decision-makers of the practical value of impact evaluation; and
 - raise the expectations of decision makers and legislators that policy advice provided to them is informed by systematic, reliable, and relevant evaluation findings.
- 6.009 We do not expect that all Government policies will be evaluated. The overall net-benefit of such an approach would (in our view) undoubtedly be negative. However, it is desirable that, at a Government-wide level, a strategic selection of policy spending areas would be made (on the basis of stated criteria) to provide the basis for particular impact evaluations to be carried out. The resultant programme or schedule may include indicative timing for the evaluations to be undertaken over the medium to longer term.

The Significance of Impact Evaluation

6.010 In Part Four of our *Third Report for 1999 – The Accountability of Executive Government to Parliament*, we discussed issues affecting accountability for the outcomes of Government expenditure.¹ We framed the discussion in the context of the two critical questions that Parliament is presented with when determining whether or not to approve the Government’s expenditure proposals:

- What outcomes are the expenditure proposals intended to achieve (and should Parliament agree with them)?
- Is it likely that the proposed expenditure will achieve these outcomes?

6.011 In fact, the Government itself needs to be able to answer both questions in order to persuade Parliament of the soundness of its proposals.

6.012 Underlying those questions – and the ability to answer them – is the (apparently) simple concept of “cause and effect”, which in turn can be expressed in the form of three other questions:

- What policy objectives do we want to achieve?
- How do we go about achieving those objectives?
- Did we achieve the results we wanted to achieve, and did any unexpected results occur?

6.013 We can represent those three questions in the form of a “policy performance model” as shown in Figure 6.1 on page 104.

What Is Impact Evaluation?

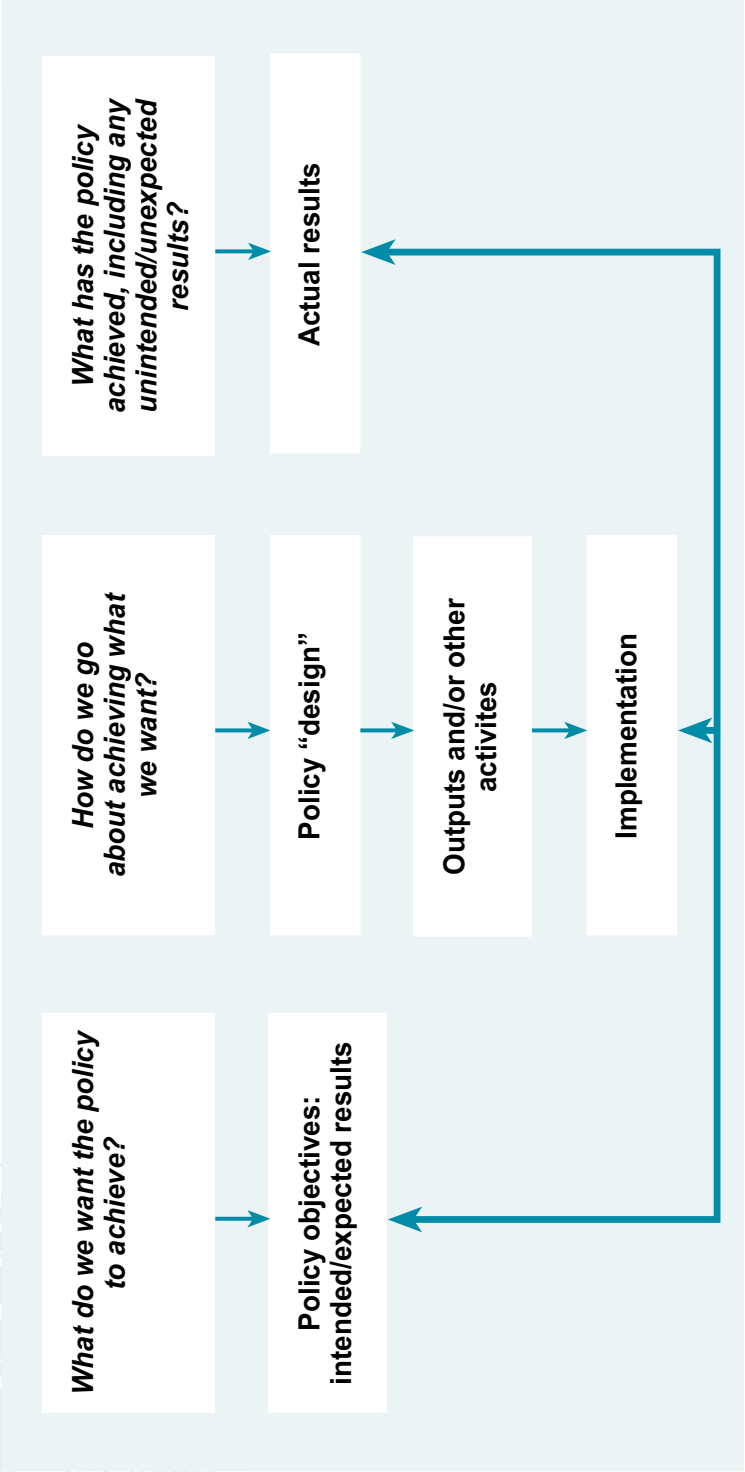
6.014 Impact evaluation can briefly be described as going about answering the third of the questions in paragraph 6.012 and, at the same time, assessing whether the answer chosen to the second question brought about the actual results.² In practice, however, this is not likely to be a straightforward exercise, because of difficulties in:

1 Parliamentary paper B.29[99c], pages 43-56.

2 An alternative description is determining “what happened” and “how” and the relationship between them.



Figure 6.1
A Policy Performance Model



- defining – in objective and quantifiable terms – the policy objectives that you want to achieve;
- identifying an appropriate and reliable means by which to achieve those objectives; and
- establishing – with the requisite degree of certainty – causality (i.e. How? and Why?) between the means used and the results achieved.

6.015 The third of those difficulties is the defining feature of “impact evaluation”, and is probably the hardest one to resolve.

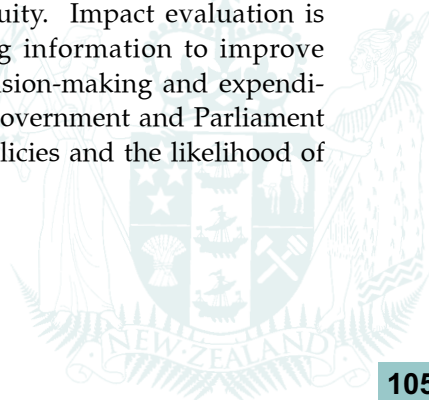
6.016 We canvassed aspects of these difficulties in Part Four of our *Third Report for 1999* and discuss them in more detail in the following sections of this article.

The Place of Impact Evaluation

6.017 We have stated previously our belief in the value of impact evaluation of key areas of government spending. In this article we address impact evaluation as a public management tool from the perspective of Ministers and Parliament as decision-makers.

6.018 The purpose of impact evaluation is to provide decision-makers with objective, frequently empirically based, information relevant to the decisions they are seeking to take.

6.019 Governments commit a significant amount of public money every year on both existing and new policies. All governments want the maximum possible impact from every taxpayer dollar they spend – in terms of efficiency, effectiveness and equity. Impact evaluation is an important tool in providing information to improve the quality of Government decision-making and expenditure, as it helps to inform the Government and Parliament about the success of existing policies and the likelihood of success of policy proposals.



- 6.020 To support its policy decision-making role, and its role in preparing legislative and budget proposals for consideration by Parliament, the Government should have some confidence that the objectives of both ongoing and new policies are achievable.
- 6.021 To support its scrutiny role in passing legislation and making appropriation decisions, Parliament should also have some confidence that both the ongoing and new policies proposed by the Government are likely to be successful.
- 6.022 The information generated through impact evaluation will inform decisions about the design, operation and retention of existing policies, and about the nature and design of new policies. Impact evaluation findings should identify:
- ineffective policy actions that need to be modified in order to achieve the desired outcomes or terminated (during policy implementation or service delivery); and
 - the probability that a new policy proposal will be successful (through the policy formulation process).
- 6.023 Thus, the Government and Parliament should review the continued relevance of existing policies to assess whether their objectives remain relevant to the Government’s overall goals, and whether and how well their implementation is contributing to the achievement of the intended policy objectives. Similarly, in determining whether to support new policy proposals, decision makers should ask how they are to know that the proposal is likely to be successful and over what period.



Our Expectations for Effective Impact Evaluation

6.024 We consider that there are a number of pre-conditions for effective impact evaluation at a Government-wide level:

- Policy advice and Government policy decisions will provide a sound basis for subsequently judging whether the policy was effective. Policy decisions will provide an indication of how the Government will know in the future that the policy has been successful and logical criteria for evaluation.
- In order to provide those evaluation criteria, policy advice and decisions will set out –
 - A definition of the problem(s) which the advice is addressing. The problem definition may itself be informed by previous empirical work (where evaluation of similar policies has been completed).
 - The purpose and objectives of the policy in a way that is clearly related to the problem(s) identified. Policy objectives may be statements of desired outcomes at different levels of specificity, outcome targets over different periods, and other expectations.
 - The characteristics of the recommended policy, including the limits of its implementation – such as the characteristics of target groups; financial, age and other thresholds; and regulatory constraints.
 - A soundly based argument for why and how the recommended policy is expected to address the problem(s) successfully – including any critical inter-dependencies and risks, and options for managing both.
- Systematic measurement of critical outcome indicators, and indicators of the implementation of the policy, will occur throughout the life of the policy in order to provide some of the data to be used to assess its success.³

3 Where the policy action is an output, the data may be the same as that reported by agencies and Ministers for accountability purposes.

6.025 Those pre-conditions are based on the assumptions that:

- impact evaluation is a critical source of information for the provision of high-quality policy advice to Ministers and the Government;
- the conduct of impact evaluations is an integral part of, and not additional to, the policy development process;
- not all policies will or necessarily should be evaluated; and
- impact evaluations will usually focus on those policies that –
 - have a significant strategic focus for the Government; or
 - are of a significant cost to the community; or
 - have characteristics that suggest that the continued relevance of the policy is doubtful (even if the amount of public expenditure involved is relatively small); or
 - affect other significant policy areas where there is a need to understand the success of the policy before proceeding with a new policy.

6.026 We expect that each impact evaluation project would:

- Be explicitly assessed as being practicable before the project is undertaken, based on consideration of –
 - whether meaningful data has been or can be measured, meaningful analysis of data is feasible, causal relationships will be discernible through modelling, extrapolation and so on; and
 - the general nature of findings means that they are likely to be useful and able to be acted on by Ministers.
- Be well designed before the project commences, preferably based on the policy decision.
- From the wide range of evaluation methodologies and techniques available, utilise tenable methodologies appropriate to the policy being evaluated. The chosen approach should be free of avoidable biases and should have addressed other ethical considerations.

- Involve analysis of comprehensive, valid and reliable data.
- Be reported to the Government (or an agent, such as a government department) with conclusions that are explicitly derived from the analytical findings.



Our Survey of Impact Evaluation in Use

6.027 This section sets out the results of the survey we conducted to establish the extent to which government departments were using impact evaluation.

What Did We Want to Examine?

6.028 As stated in paragraph 6.015, the defining feature of impact evaluation is the analysis of causal relationships, which itself requires systematic measurement of both aspects of performance being examined – i.e. the action and the impact.

6.029 Therefore, we wanted to establish both whether departments were involved in evaluative activity and the extent to which that activity focused on seeking to establish the impact of Government policies. That is:

- the extent to which departments were measuring, over time, selected dimensions and indicators of both Government policies and their associated outcomes; and
- whether departments were analysing the strength of the link or causal relationship between the two.

How Did We Undertake the Survey?

6.030 We conducted a survey of the 31 central government departments that we considered most likely to be using impact evaluation or other forms of evaluative activity. We provided the departments with our definition of impact evaluation and a summary of our expectations.

6.031 The survey was based on a questionnaire broadly based on the expectations set out in paragraphs 6.024-6.026. We visited each department to discuss the questionnaire before the department completed it and undertook follow-up visits to clarify aspects of the department's responses when asked to do so.

6.032 We asked each department to identify three of the most significant Government policy initiatives taken in relation to their responsibilities over the last five years. For each of these policy initiatives we sought information on whether:

- the policy advice that the department had provided was supported by evaluations of existing or past programmes or empirical research evidence;
- clearly specified, measurable outcomes and policy objectives were articulated as part of the policy decision;
- dimensions of the objectives(s) and the actual outcome(s) had been measured since the decision had begun to be implemented; and
- analysis of the strength of the relationship between the policy design and intended outcome(s) had been undertaken.

What Did the Survey Show?

6.033 In summary, our survey showed that:

- departments are undertaking useful evaluative activity (refer paragraph 6A.005 on page 132), although little impact evaluation;
- departments do not have a clear, common understanding of the nature of impact evaluation (the understanding that departments have is influenced by the nature of their role and functions);
- despite these different starting points, our discussions with departments showed that they support the concept of impact evaluation that we have used;
- desired outcomes and policy objectives are generally poorly specified and therefore provide an inadequate basis for impact evaluation; and
- departments are using a range of evaluation techniques.

6.034 The survey also confirmed concerns about the relatively short times for both Government budget cycles and parliamentary terms compared with the length of time frequently required for the achievement of policy objectives.

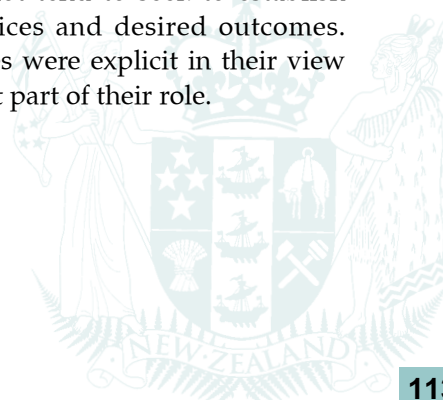
- 6.035 Finally, the survey raised general issues relating to the public management system and (in particular) the requirement of the Public Finance Act for departments to report the link between outputs and outcomes.
- 6.036 Each of these findings is discussed in paragraphs 6.037-6.068.

Departments Are Undertaking Useful Evaluative Activity

- 6.037 We were impressed with the level of general evaluative activity being conducted by departments, and also by the work being done to start systematic outcome measurement. We were able to identify few departments undertaking impact evaluation, but a number of departments are moving towards it – as the two case studies in the final section of this report show.
- 6.038 The main focus of evaluative activity centred on measuring and monitoring aspects of output performance and reviewing delivery methods and processes in order to improve output delivery.
- 6.039 Some departments have been involved in systematic outcome measurement for some time. We were pleased to note that a number of other departments are also beginning to measure aspects of outcome performance.
- 6.040 Generally, departments were conducting evaluative activity in relation to new, small and discrete policy initiatives at the margin of Government expenditure. We did not find any clear indications that impact evaluation was being undertaken in relation to large or strategic policy initiatives.
- 6.041 There appear to be few examples of systematic analysis of the linkages between the outputs delivered and the outcomes achieved, as in impact evaluation. Departments seldom are able to reliably identify the manner in which the implementation of a policy has contributed to outcomes.

There Is No Clear, Common Understanding of Impact Evaluation

- 6.042 Analysis of the questionnaire responses identified that departments held differing views of what constitutes impact evaluation – as opposed to, for instance, research. Some departments regarded impact evaluation as being distinct from, rather than an integral element of, policy analysis.
- 6.043 Some departments considered that measuring dimensions of either output or outcome performance was sufficient on its own, without establishing the linkages between them. Other departments discussed seeking to establish the relationship between policy advice and desired outcomes. This approach creates additional external factors relating to the differences between the advice tendered and the policy decision. The issues that arise in seeking to evaluate the impact of policy advice are discussed further below.
- 6.044 Each department’s view of evaluation and the type and extent of evaluative activity being undertaken was influenced by the role of the department.
- 6.045 As expected, with impact evaluation being integral to policy analysis, policy agencies – in particular sector-based agencies – appeared to have a stronger understanding of impact evaluation. Policy agencies indicated that policy advice was frequently informed by analysis of research findings, and accepted the value of impact evaluation findings as another important source of data.
- 6.046 Service delivery agencies tended to focus their evaluative activities on dimensions of output performance and service delivery processes and did not tend to seek to establish linkages between those services and desired outcomes. Some service delivery agencies were explicit in their view that impact evaluation was not part of their role.



Departments Support the Value of Impact Evaluation

- 6.047 Despite the above differences in starting points, all of the departments surveyed supported our concept of impact evaluation and its potential value for policy analysis and advice and decision-making by the Government and Parliament.
- 6.048 No departments gave technical difficulties or excessive costs in establishing linkages as the reason for not yet undertaking impact evaluation. Some departments commented on cost as a general constraint.
- 6.049 While many policy agencies were at the early stages of designing or conducting impact evaluations, they acknowledged that they still have a considerable way to go to implement impact evaluation as a routine, integral element of policy analysis.

Desired Outcomes and Policy Objectives Are Poorly Specified

- 6.050 Clearly specified, measurable outcomes are not articulated consistently well as part of policy advice and policy decisions. Departments acknowledged that while high-level goals may be specified, more explicit focus was required on the specification of policy objectives and outcome indicators and measures. This information would then provide the basis for examining the success of the policies.
- 6.051 One of the reasons given for inadequate articulation of policy objectives was that policy advice is sometimes tendered directly in response to ministerial direction rather than as the result of a systematic or comprehensive policy formulation process.
- 6.052 A number of departments discussed the inadequacy of the strategic result areas and strategic priorities and overarching goals for analysing the impact of policies. Some departments indicated that, in a general sense, more meaningful policy objectives are sometimes discernible from the objectives specified in legislation. They evaluate compliance with those objectives, although these objectives also tended to be inadequate for assessing impact.

Different Types of Policies Require Different Evaluation Approaches

- 6.053 The inherent nature of some policy initiatives and, to a lesser extent, different policy sectors, means that some outcomes may be easier to measure than others and some causal relationships may be easier to establish. For example, social policy and environment initiatives tend to present more particular difficulties than other policy areas due to the generally long time over which outcomes are expected to be realised. This constraint may be addressed through establishing hierarchies of outcomes with intermediate outcomes to be realised in a shorter time.
- 6.054 A further constraint identified was that policy initiatives are seldom implemented in isolation. This constraint requires careful selection of the evaluation methodology and specific techniques that are appropriate for addressing the particular Government policy.
- 6.055 Departments will sometimes be able to identify clear linkages and a strong causal relationship, but in other situations may rely on less direct indicators and greater use of explicit deduction.

Systemic Issues

Timing

- 6.056 The survey also confirmed a number of time-related weaknesses that are inherent in the public management system.
- 6.057 The one-year Government budget cycle is not conducive to impact evaluation, even with the financial planning period covering three years. Few new policy initiatives can be introduced and fully implemented within one year, and it frequently takes longer for an initiative to reach sufficient maturity to enable any analysis of its impact to be evaluated meaningfully. Evaluations that are carried out during a pilot programme tend to focus more on matters of implementation than impact.

- 6.058 Because of the three-year parliamentary term Ministers frequently seek to establish that they have made a difference and are increasingly requesting evaluations as soon as the policy has been implemented. As discussed above, it is difficult for impact evaluation to be meaningful when full implementation may take a number of years, and the real effects of the policy may not be realised for considerably longer than that.
- 6.059 A further consequence of ministerial expectations is that evaluation findings are not necessarily feeding into decision-making. Frequently, the pressure to move on to the next decision means that advice is tendered and decisions taken before a meaningful impact evaluation of an earlier related decision is possible.
- 6.060 In our view these timing factors lead to ‘evaluations’ being driven towards process reviews and analyses. These evaluative activities are intended to confirm compliance of implementation with design and budget parameters and to improve delivery methods, rather than to identify causal relationships between the policy actions and actual outcomes.

Other Issues Raised by the Survey

Evaluating the Impact of Policy Advice

- 6.061 The survey raised a general issue relating to whether it is meaningful to require a link to be reported between policy advice outputs and the impact of the Government policies that to varying degrees are based on that advice. However, examining such a link is unlikely to be practicable given its tenuous nature and the external factors involved in policy making.
- 6.062 This issue is in even sharper focus when it is considered in relation to policy agencies that have a “second opinion” role, such as population-based policy agencies like Te Puni Kokiri, or central agencies involved in policy development led by other agencies.

- 6.063 In a technical sense, the desired outcomes of policy advice tendered by a lead policy agency – such as the Ministry of Women’s Affairs – relate to the nature and quality of Government decision-making and the nature of Government policy initiatives. Similarly, the impact of the policy advice provided by service delivery agencies – such as the Department of Work and Income – during the policy development process relates to the extent to which they are successful in persuading the lead agency to tailor the advice to address the particular concerns of the different populations and other interest groups.
- 6.064 In our view, these relationships are not suitable for examination through impact evaluation.

Impact Evaluation and Service Delivery Agencies

- 6.065 The primary incentive of those agencies with a largely service delivery role is to focus their evaluative activities on the delivery of outputs, including output measurement and process reviews. Our survey results indicate that agencies seldom appear to analyse the impact of their services. However, given the closeness of the relationship between impact evaluation and policy analysis, perhaps it is not reasonable to expect service delivery agencies to undertake impact evaluation.
- 6.066 The issue raised by these findings is whether the Public Finance Act requirement to identify the link between outputs and desired outcomes is reasonable or even meaningful in all situations. Greater consideration needs to be given to determining the nature of the information that will satisfy the requirement.
- 6.067 For instance, it may be sufficient for a service delivery agency to assert the link broadly based on the objectives articulated in policy decisions. On the other hand, policy agencies may be required to set out the outcomes that provide the focus of their policy work programme.
- 6.068 Both service delivery agencies and policy agencies could demonstrate in their annual reports to Parliament the links between policies and outcomes based on the findings of impact evaluations completed in (say) the previous three years.

Two Case Studies

- 6.069 In this section we briefly describe two examples of evaluative activity recently carried out by different departments. The purpose of presenting the case studies is to demonstrate that impact evaluation is a practical tool for both policy advisers and policy makers.
- 6.070 The case studies are the evaluations of:
- the Home Detention Pilot Programme of the Department of Corrections (June 1997); and
 - the Supplementary Road Safety Package (LTSA and the Police – July 1998).
- 6.071 The findings from these case studies, in conjunction with other information, have been used to inform further policy advice to Ministers on modifications to the characteristics of the policy initiatives.
- 6.072 Each of the cases clearly indicates progress towards the use of impact evaluation studies. Each study:
- has some characteristics that are consistent with our expectations of what constitutes impact evaluation; and
 - in some respects and to differing degrees, falls short of those expectations.
- 6.073 The completed evaluations tended to focus as much if not more on assessing aspects of delivery than the relationship between the actions and the desired outcomes. Nevertheless, the evaluations provided useful insights and recommendations for modifying aspects of the delivery, at a management level, to better achieve the desired outcomes.
- 6.074 Overall, the case studies point to the progress the government sector is making towards undertaking impact evaluation of the kind discussed in this article.
- 6.075 The case studies do not involve a direct examination of the evaluations themselves, and therefore they do not consider our expectations relating to individual evaluations (paragraph 6.026).

Home Detention Pilot Programme

The Policy Being Evaluated

- 6.076 The Criminal Justice Amendment Act 1993 provided for the establishment of pilot home detention schemes. The Department of Corrections (and before the restructuring the Department of Justice) operated a pilot scheme with the first inmates released to home detention in March 1995. The pilot was to run for two years.
- 6.077 Two types of surveillance were used, designed to provide support and control structures for detainees:
- Passive electronic monitoring of the detainees, involving random telephone calls and a combination of visual and voice verification, in order to confirm compliance with the primary conditions of their release. A home detention officer was available at all times to verify violations recorded by the equipment.
 - A supervisory relationship with each detainee by a home detention officer, including a regime of visits and random telephone calls to the detainee’s home and workplace.
- 6.078 The legislation set out criteria for determining the eligibility of inmates to participate in the pilot and the conditions that the detainees must meet while on home detention.
- 6.079 The pilot was designed to cater for a maximum of 30 detainees at any one time, although the actual maximum was 12 with an average of seven.



The Policy Objectives/Desired Outcomes

- 6.080 The reported objectives of the home detention policy were to:
- ease the transition of inmates back into the community through a staged release process and thus to achieve reintegration; and
 - provide home detention as an option only for eligible inmates not otherwise able to be released on parole.
- 6.081 As a reintegrative programme, the home detention policy aimed to reduce reoffending by detainees both during and after the home detention period. However, reducing reoffending was not reported as a formal objective of the home detention policy.
- 6.082 The policy also aimed to release some inmates from prison earlier than would otherwise have been the case, even though eligibility for the programme coincided with eligibility for parole. As home detention was regarded as part of the prison sentence, the pilot sought to avoid releasing inmates on home detention who would have been granted parole.
- 6.083 The evaluation also considered a number of objectives that, while not formally part of the policy objectives, were considered important in assessing the policy's effectiveness. These additional objectives related to:
- the cost-effectiveness of the programme, relative to other forms of imprisonment;
 - compliance with the conditions of the programme by detainees;
 - reducing reoffending by detainees; and
 - minimising the (negative) impact of the home detention programme on families.

Methodology Used for the Evaluation

- 6.084 The evaluation was to cover the first 18 months of the pilot programme and had three parts.
- 6.085 The **overall objectives** addressed the effectiveness of the programme in meeting its objectives (see paragraph 6.080) and whether the programme could be extended to a national system. This part of the evaluation also sought to identify any improvements needed and the features of a national home detention system.
- 6.086 The **process objectives** related to describing the operation of the programme – including the roles and relationships of key personnel, the use of electronic monitoring, and the views of the inmates and their families on the adequacy of the services.
- 6.087 The **outcome objectives** addressed the additional objectives listed in paragraph 6.083. The outcome objectives encompassed:
- describing the rates of successful completion and of reoffending while on home detention;
 - assessing the appropriateness of home detention in terms of the impact on family members and different ethnic groups; and
 - assessing the costs of home detention relative to other forms of imprisonment and parole.
- 6.088 The data gathered during the evaluation was analysed to assess the relationship between the use of home detention and the desired outcome of easing the transition of inmates from prison to the community. Information was gathered from different sources using different methods. The following techniques were used:
- semi-structured interviews (both face-to-face and telephone) with detainees and their families, employers of detainees, and a range of key informants, including Department of Corrections staff (employed in prisons, probation and home detention areas), chairpersons of District Prisons Boards, the contractor for the electronic monitoring element, and prison inmates;

- analysis of case records (including data on rates of successful completions, breaches, reoffending, reviews and recalls to prison), activity logs kept by home detention officers for two separate weeks during the evaluation period, and departmental expenditure records; and
- observation, with home detention officers, prison staff and District Prisons Boards.

6.089 The evaluation was carried out by members of the Criminal Justice Policy Group of the Ministry of Justice and the former Policy and Research Division of the Department of Justice.

Findings of the Evaluation

6.090 In relation to the two policy objectives (paragraph 6.080), the pilot home detention programme was found:

- to be of variable value as a reintegrative programme; and
- not to have a net-widening impact.

6.091 The findings relating to the effectiveness of the pilot as a reintegrative programme primarily addressed issues relating to the impact of home detention on the detainees themselves, their families and their workplaces.

- For the detainees, the findings included improvements in their personal relationships – particularly with their partners, children and parents – improvements in work habits and experience and associated income, and positive comparisons with prison.
- For families, the findings included benefits for family life, relationships and household income, despite some additional burdens.

6.092 The evaluation also reported reservations in the extent to which some of these improvements could be attributed to home detention.

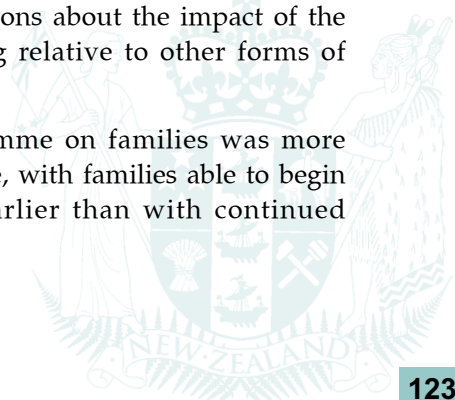
6.093 For all parties involved in the pilot – the detainees, their families and workplaces, and home detention officers – the findings included a number of negative characteristics of

the surveillance aspects of the programme. The legislated requirements for the programme, as it was piloted, concentrated on restricting the detainee – making the predominant focus of the programme one of control rather than rehabilitation.

6.094 The findings relating to entry of inmates to the programme were more conclusive, with the results indicating that introducing the programme as a parole option had not led to widespread net-widening. However, the legislated requirements for the programme created little incentive for inmates to agree to home detention since the release conditions were more restrictive than standard parole.

6.095 The findings relating to the additional objectives for the evaluation (paragraph 6.083) were that:

- The annual cost for each home detention detainee was calculated to be comparable to the annual cost of minimum-security imprisonment for one inmate. However, this calculation was qualified in that –
 - a number of other factors such as the effects of reduced reoffending could not yet be taken into account; and
 - the programme was operating below its full capacity and, as a pilot, was not able to generate economies of scale.
- Compliance with the conditions of the programme was satisfactory, within the discretion available to the home detention officers, although some detainees reported rule breaking that was not detected by the monitoring systems. Only one detainee was recalled to prison.
- The number of detainees on the programme was too low to be able to draw conclusions about the impact of the programme on reoffending relative to other forms of release.
- The impact of the programme on families was more often positive than negative, with families able to begin restoring relationships earlier than with continued imprisonment.



6.096 The evaluation report went on to make a number of suggestions for improvement, most of which related to:

- improving aspects of delivery through better communication and understanding about all aspects the programme;
- modifications to monitoring equipment; and
- some opportunities for staffing efficiencies.

6.097 The report:

- suggested that it was appropriate to consider the use of an active monitoring system (involving attaching a transmitter to the wrist or ankle of each detainee) rather than the passive system used in the pilot;
- highlighted a number of possible weaknesses in the legislative requirements for both eligibility for, and conditions of, home detention; and
- indicated that a number of the other policy parameters would need to be modified to facilitate reducing prison populations, if that was to become a fundamental policy objective.

6.098 Finally, the report stated that, even with improvements in delivery as discussed above, extending the programme to a national system in the form in which it was piloted would appear to have little purpose.

How the Findings Were Used

6.099 The findings of the evaluation were used, in conjunction with additional information from other local and overseas research evidence, to provide policy advice to the Government on the future of home detention.

6.100 The evaluation also enabled the Department of Corrections to identify areas where improvements in service delivery and performance could be made.

How Did the Evaluation Compare With Our Expectations?

- 6.101 This evaluation met a number of the pre-conditions we expected and clearly indicates progress towards impact evaluation.
- 6.102 Where the objectives of Government policies are not always clearly specified or meaningful the evaluators must establish outcome-related objectives at the start of the evaluation – as in the Home Detention Pilot Programme. (A useful evaluation may still be carried out in this situation. However, it is not ideal as poor policy objectives mean that systematic measurement over time of key aspects of outcome achievement is precluded and information is consequently unavailable to the impact evaluation.)
- 6.103 Most notably, policy advice and policy decisions as presented in the evaluation report included two high-level desired outcomes with no targets. However, the nature of the programme was clearly articulated and systematic measurement of aspects of both the programme and the outcomes occurred – although the report did not explicitly discuss those things.
- 6.104 The evaluation provided useful insights and recommendations for modifying both the characteristics of the programme, at a policy level, and aspects of the delivery of the output, at a management level, to better achieve the desired outcomes.

Supplementary Road Safety Package

The Policy Being Evaluated

- 6.105 The Supplementary Road Safety Package (the Package) was a package of modifications to and extensions of the Government's enforcement and publicity activities, aimed at drink-driving, speeding and seat belt offences.⁴ The Package was to run over four years from 1995-96 to 1998-99.

⁴ The focus on seat belt offences was added to the Package in 1996-97 and was included in the evaluation.

- 6.106 The key actions in the Package were to:
- improve the targeting of speed camera and compulsory breath testing (CBT) enforcement programmes;
 - increase the hours of operation of the speed camera programme; and
 - provide sustained publicity to support the speed camera and CBT programmes.
- 6.107 The Package also involved the introduction of some new equipment:
- advanced laser speed detectors to augment the speed camera programme; and
 - additional breath testing devices to support the CBT programme.
- 6.108 In addition, an independent evaluation of the safety outcomes achieved from the Package was required each year, and modifications to the Package would be made where appropriate.
- 6.109 This evaluation considered the operation of the Package and the outcomes achieved during the two years 1995-96 and 1996-97.
- 6.110 Thus, the Government policy being evaluated was a package representing a combination of modifications to some of the performance characteristics of existing outputs purchased by the Government, new inputs in the form of specific equipment, and management performance through the requirement for regular evaluation and adjustment.

The Policy Objectives / Desired Outcomes

- 6.111 Three critical documents relating to this evaluation provided statements of the Government's policy objectives:
- the National Road Safety Plan 1994-2001 (the Plan);
 - the Safety (Administration) Programme (the Programme) 1995-96 to 1998-99; and
 - the Package.

- 6.112 The Plan set outcome targets – relating to the numbers of persons killed and the numbers of Police-reported injuries on roads in the year 2001– that reflected significant reductions over 1994 levels. The Programme set intermediate targets showing a progressive decrease and also set out targets for a number of behavioural measures (or intermediate outcomes), both of which were considered necessary to achieving the overall outcome targets.
- 6.113 The Package, which was intended to supplement the Programme, set out targets relating to cumulative road trauma reductions in respect of road fatalities, serious injuries and minor injuries.

Methodology Used for the Evaluation

- 6.114 The scope of the evaluation was threefold, with one area of review most pertinent to our exercise on impact evaluation – an assessment of the effectiveness of the Package during 1995-96 and 1996-97. The evaluation also included a review of:
- the evaluation processes established within the Land Transport Safety Authority and other agencies for assessing the effects of the Package; and
 - the implementation of the Package.
- 6.115 The Land Transport Safety Authority contracted independent evaluators (from Australia) to undertake the evaluation.
- 6.116 Completing the assessment part of the evaluation drew heavily on data generated by systematic measurement over time (by different agencies) of the large number of variables required for analysis. These variables included aspects of output delivery performance, environmental characteristics, and outcome achievement.
- 6.117 Quantitative data was available on output delivery, including data on the number of events – such as the number, timing and location of breath screening tests – and on time – such as Police time spent on mobile speed camera activity and driving offences. Data was also routinely collected on the placement and frequency of road safety advertising. Market survey results were available,

providing data that focused on both recall of road safety advertising and views on the likelihood of “being caught” with Police involvement in driving offences.

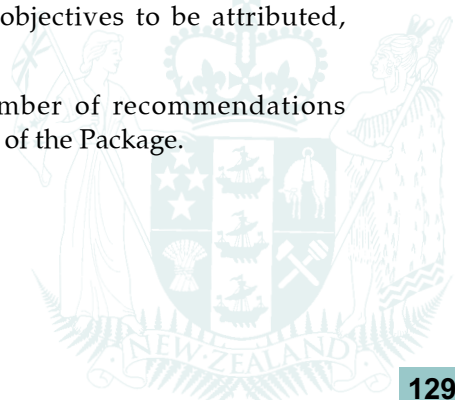
- 6.118 Data was available on the location of accidents, road conditions at the time, driver characteristics and behaviour, vehicle characteristics and condition, and so on. Data was also available on the intermediate and overall outcomes sought through the policy – the number and type of driving offences and the number of road trauma incidents, including details of fatality and injury type.
- 6.119 The primary technique applied during this evaluation was a time-series analysis of serious casualties and fatalities, taking into account characteristics of the Package and factors outside the Package. The analysis took into account the introduction of CBT and speed cameras during 1993, socio-economic factors that may be linked to changes in road use (especially high-risk travel), and trends and seasonal variations in road trauma. For instance, additional time-series analysis was undertaken for serious casualty crashes in terms of both high and low alcohol hours of the week and the location of crashes – urban and rural.
- 6.120 While some factors may have an effect on the outcomes sought, it is not always feasible to include them in the analysis. In particular, it was also acknowledged that although on-going improvements to roads have made a contribution to the downward trend in road trauma, their gradually increasing effect (relatively small change from year to year) made them unsuitable for explicit consideration in the analysis.

Findings of the Evaluation

- 6.121 The evaluation report stated that it had been possible to estimate the effectiveness of the Package and to comment on the contributions of its separate elements. A number of findings were reached about the relationship between the aspects of the Package and the level and type of road trauma and estimates were made of the savings in road fatalities and injuries that could be associated with the Package. Overall, the evaluation concluded that it was likely that the

targets for the reduction in fatalities and injuries during the four years of the Programme had already been met or exceeded in its first two years.

- 6.122 The degree of causal relationship was qualified through reporting a number of indicators that suggested that part of the reduction in the risk of death or serious injury on the roads during 1995-96 and 1996-97 could be attributed to the components of the Package. The findings were graduated with:
- the drink-driving component of the Package being described as suggesting a substantial contribution;
 - the speeding component as suggesting a smaller contribution; and
 - the seat belt component as probably suggesting some contribution in 1996-97 only.
- 6.123 The evaluation also concluded that *the procedures established by the Land Transport Safety Authority for monitoring and evaluating the outcomes of the Supplementary Road Safety Package . . . allow the effects of the SRSP to be seen in terms of changes of advertising awareness, public attitudes, on-road behaviours, and road trauma levels related to drink-driving and speeding.*
- 6.124 The report recommended a number of additional policy initiatives and analysis of existing programmes, with specific reference to speed cameras.
- 6.125 One recommendation related to the development of a mathematical model. The discussion indicated that use of such as model would enable any causal relationship between the components of the Package and achievement of the Government's policy objectives to be attributed, rather than estimated as now.
- 6.126 The report also made a number of recommendations relating to the implementation of the Package.



How the Findings Were Used

- 6.127 The findings from the evaluation of the Package were used by:
- the Ministry of Transport in providing policy advice to the Government concerning the continuation of the Package;
 - the LTSA and the Police; and
 - by other agencies in modifying aspects of the delivery of the outputs for which they are responsible.

How Did the Evaluation Compare With Our Expectations?

- 6.128 This was an impact evaluation that provided a practical tool for both policy advisers and policy makers. The pre-conditions we expected were sufficiently in place through the Government policy decision.
- 6.129 For the Package, the policy advice and policy decisions included clear, specific articulation of both the desired outcomes and the nature of the Package; and the agencies undertook systematic measurement of aspects of both the actions and the outcomes. Outcomes were articulated at several levels of specificity, with:
- ultimate targets for achievement by the end of seven years;
 - intermediate targets for the intervening years; and
 - an additional set of intermediate outcomes and targets that were argued as being necessary to the achievement of the overall outcome.

- 6.130 The evaluation also provided useful insights and recommendations for modifying both the characteristics of the actions within the Package (at a policy level) and aspects of the delivery of those outputs (at a management level) to better achieve the desired outcomes.

Appendix A

Impact Evaluation in the Public Management System

6A.001 The purpose of this section is to describe the place of impact evaluation in the public management system. In conjunction with our expectations relating to its use within the system (paragraphs 6.024-6.026), the section provides the basis for our survey (paragraphs 6.027-6.068) and a framework for considering the two case studies reported (paragraphs 6.069 to 6.130).

The Significance of Impact Evaluation

- 6A.002 Officials are increasingly acknowledging the importance of evaluation as a public management tool. There are numerous conferences on evaluation each year and papers by various government agencies and commentators.⁵
- 6A.003 However, agreement has not necessarily been reached about the nature (definition) or characteristics of good evaluation, or even the language of evaluation. Nor has there been systematic or consistent use of evaluation practices.
- 6A.004 The topic is vast and this article is neither a general exploration and discussion on the various approaches to evaluation used by government agencies nor a theoretical or conceptual paper on definitions of and differences between various types of evaluation or evaluation methodologies.

⁵ For instance, *Looping the Loop: Evaluating Outcomes and Other Risky Feats*, State Services Commission (1999).

- 6A.005 We use the term “evaluative activity” for describing numerous situations in which government agencies measure, monitor, review and analyse aspects of entity performance – including outcome achievement or status, output delivery, and input use. These activities do not constitute impact evaluation.⁶
- 6A.006 Impact evaluation findings are generated through two stages:
- First, systematic measurement over time of selected dimensions and indicators of both policy actions – primarily outputs – and their associated outcomes.
 - Secondly, analysis of the causal relationships between the two, which is the critical characteristic of impact evaluation.
- 6A.007 Impact evaluation is not limited to measuring and reporting outcome achievement, output delivery or the operation of other (non-output) Government policy actions.
- 6A.008 However, evaluation findings will seldom demonstrate causality conclusively, and the strength of causal relationships that can be demonstrated will be weaker in some situations than others. Systematic measurement of the characteristics to be studied and comprehensive analysis of trends and patterns is required to be able to attribute changes to a particular factor with sufficient confidence for the findings to be meaningful.
- 6A.009 These limitations are recognised and accepted characteristics of impact evaluation. Nevertheless, findings of reliable impact evaluations will always provide a more objective and higher-quality platform of information on which:
- policy advice may be tendered by departments;
 - policy decisions may be taken by Ministers and the Government; and
 - legislative decisions may be taken by Parliament.

⁶ Evaluative activities include operational audits, performance auditing, reviews, customer satisfaction surveys, and routine measurement of aspects of output delivery.

Impact Evaluation and Policy Advice

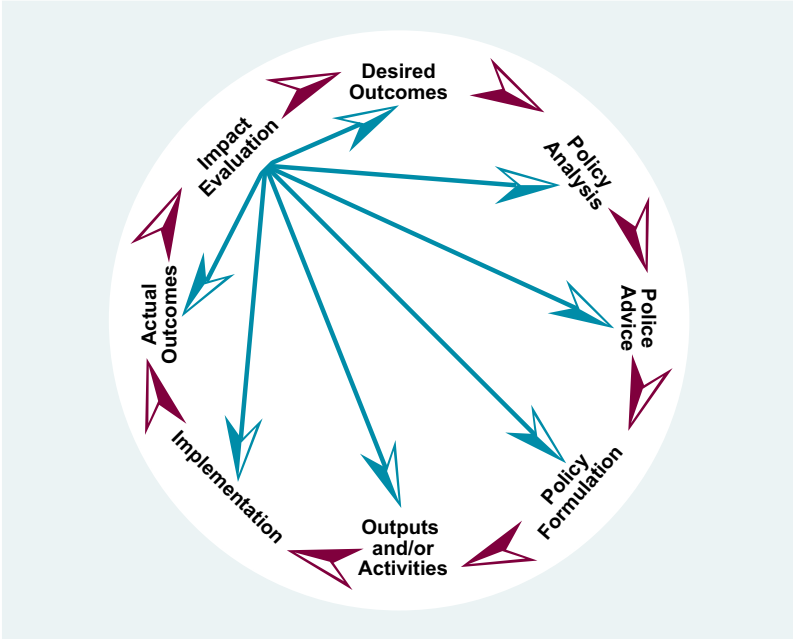
Policy Agencies

- 6A.010 Policy agencies are responsible for providing policy advice to their Ministers and the Government and, as an inherent element of that advice, for presenting a view on the nature of the causal relationship between different policy design options and the Government’s desired outcome(s).⁷
- 6A.011 Greater use of empirically based policy advice is likely to inform higher-quality decision making – and a movement away from largely deductive approaches to policy advice. Thus, in order to be high-quality policy advice, that advice should be informed by (among other things) current information and empirical data on the effectiveness of related existing Government policies and how those policies have affected achievement of the outcomes the Government is seeking.
- 6A.012 Impact evaluation is an important source of such data. Impact evaluation is also an important source of information to determine the level of consistency between the design of a policy and the way in which it has been implemented.
- 6A.013 The place of impact evaluation in the policy circle is illustrated in Figure 6.2 on page 134.

⁷ Limitations on impact evaluation arguably also apply to policy advice – see paragraphs 6.061-6.064.



Figure 6.2
The Policy Circle



6A.014 Evaluation during formulation of a new policy is likely to be a desk-based exercise using empirically based findings from evaluations of similar policies as well as relevant research material. Using these critical sources of information advisers extrapolate conclusions about the likely success of different options for addressing a particular policy problem.

6A.015 In this way, evaluation findings are used to give shape to policy actions and assist decision-makers to determine the “right things to do” to address particular policy problems. Evaluation findings also assist decision-makers to determine the general design of the policy actions and the parameters under which they will be implemented.

6A.016 Impact evaluation during policy implementation will also consider whether the findings demonstrate that the policy design is the “right thing” for achieving the desired objectives. In addition, impact evaluation at this stage will consider whether any differences between the policy design itself and implementation of the design have improved or lessened the effectiveness of the policy.

Service Delivery Agencies

6A.017 On the other hand, service delivery agencies are responsible for optimising the achievement of desired outcomes within the policy design and other parameters agreed by the Government, through the selection of service delivery methods. Fulfilling this responsibility is helped by ongoing monitoring of the implementation in order to inform operational decisions about those aspects of a policy that are (reasonably) controllable by the service delivery agency.

6A.018 While being important for management purposes, evaluative activities of that type do not constitute impact evaluation as discussed here. Such monitoring considers whether implementation of the policy is consistent with the policy design and may identify ways in which altering the service delivery methods or approaches (consistent with the policy design) may improve the effectiveness of the policy. Such evaluative activities will identify whether the agency is “doing things the right way”.

The Focus and Findings of Impact Evaluation

6A.019 The focus of an impact evaluation will depend on the nature of the policy question being considered and the purpose of the information that is sought. Similarly, the methodology adopted for an impact evaluation will depend on the nature of the policy being examined.

6A.020 Impact evaluations may, for instance, seek to identify:

- the actual effect of a particular Government policy; or
- the policies that are contributing to a particular outcome area.

- 6A.021 Thus, impact evaluation may relate to a complex umbrella Government policy involving a number of policy initiatives expressed through several appropriations and a number of Votes or departments. Impact evaluations may also relate to a specific policy expressed through a single or multiple appropriation and single or multiple Votes or departments.
- 6A.022 Evaluation findings may relate to:
- the design of the policy;
 - the manner in which the policy has been implemented, especially where there may be some differences between implementation and policy design; or
 - the definition of the problem which the policy was intended to address.
- 6A.023 Findings may be based on explicitly stated logic (deductive reasoning) – supported by a correlation between data sets, data modelling and extrapolation – and other analytical techniques.
- 6A.024 Thus, impact evaluation is a critical and systematic analysis, using empirical data, of whether the results intended by a policy have been or are being achieved (for ongoing expenditure) or are likely to be achieved (for policy and expenditure proposals). Impact evaluation may also indicate whether the design of current policies may need to be changed to better contribute to desired outcomes.



Appendix B

The Current Legislative Framework

6B.001 The Public Finance Act 1989 (the Act) reflects the first two elements in our policy performance model (Figure 6.1 on page 104) by:

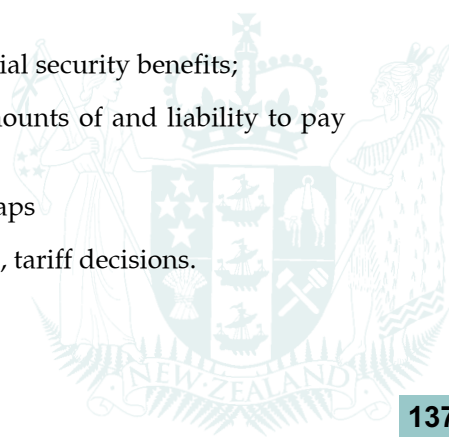
- defining “outcomes” as *the impacts on, or consequences for, the community of the outputs or activities of the Government*; and
- requiring the *Estimates of Appropriations* to *identify the link between the classes of outputs to be purchased by the Crown and the Government’s desired outcomes*.

6B.002 However, what the Act does not do is to provide any guidance on:

- how to describe outcomes, with associated measures or criteria, in such a way as to be able to establish whether or not they have in fact occurred; and
- how strongly the “link” between outputs and outcomes should be identified.

6B.003 Furthermore, the Act does not explain what is meant by “activities” (as something different to outputs) of the Government, nor does it require that any link between “activities” and outcomes be identified. We assume that the term embraces such significant aspects of Government fiscal measures as:

- transfer payments, e.g., social security benefits;
- revenue decisions, e.g., amounts of and liability to pay taxes;
- capital spending; and perhaps
- non-budgetary actions, e.g., tariff decisions.



- 6B.004 Nevertheless, probably the greatest omission from the Act is any explicit requirement to report what outcomes have occurred, with an explanation of how they compared with the intended outcomes. (It is possible to interpret the Act as inferring such a requirement through the obligation to produce statements of objectives and statements of service performance. However, those statements are directed only at outputs.)
- 6B.005 Thus, the extent to which our policy performance model is reflected in the Act can be represented as shown in Figure 6.3 on page 140.

Difficulty In Defining Outcomes

- 6B.006 There are a number of inherent hurdles for governments in articulating desired outcomes, meaningful policy objectives, and (especially) targets for the achievement of outcomes. The primary hurdles are the knowledge that in reality many factors contribute to the achievement of outcomes – only some of which are within the reasonable control of any government – and that outcomes are generally achieved over periods longer than parliamentary terms.
- 6B.007 Outcome specification – and subsequently impact evaluation as a practical tool – should properly be limited to outcome targets that indicate progress towards the desired outcomes and policy objectives that are intermediate to the achievement of high-level outcomes.⁸ These approaches are likely to address any concerns about the time required for the achievement of outcomes.
- 6B.008 For instance, a health policy decision may include purchase of both education and regulatory services. The objectives of this policy, the desired outcomes, may relate to reducing the level of tobacco-related disease and deaths. The relationship between these services and the incidence of disease over time could be the subject of an impact evaluation.

⁸ Other forms of evaluative activity, such as social science research, which are better placed to address these higher level questions, are outside the scope of this study.

- 6B.009 Progress towards the achievement of the outcomes may be measurable over a relatively short time. A correlation is likely to be able to be demonstrated between changing levels of disease-causing behaviour in that period and the policy actions, once external factors such as other known causes of the same diseases have been taken into account.
- 6B.010 It is unlikely that an impact evaluation would be able to indicate a clear causal relationship between a policy such as this example and the health status of the general population as compared with the smokers in the population.



Figure 6.3
The Public Finance Act Policy Performance Model

