Controller and Auditor-General
Tumuaki o te Mana Arotake

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Reflections from our audits: *Governance and accountability*

Photo acknowledgement: The artwork *Universal* by New Zealand artist Gordon Pope

Reflections from our audits: *Governance and accountability*

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Auditor-General's introduction

High standards of public sector governance and accountability are essential to healthy democracies at both a national and local level. They enable the effective and efficient use of public resources in the wide range of entities that make up New Zealand's public sector.

For the purpose of this report, I define:

- **governance** as the system by which an organisation or project is directed and controlled; and
- **accountability** as the way in which people can see how their taxes and rates are used by public entities.

Accountability requires public entities to report useful and timely information about what they have achieved with the resources they have used, so that Parliament, taxpayers, and ratepayers can hold them to account for their performance.

Good governance and accountability need and support each other and, if done well, enhance the public's trust in our system of government. Good governance encourages and can result in good accountability. In turn, accountability is a vital element of good governance.

Most public entities exercise the powers of the state and/or use public resources. If people are to continue to support the democratic process, they must trust the institutions of the state. This means trusting that:

- public entities will act impartially and lawfully;
- public entities will use public resources wisely;
- people will have equity of access to government services;
- people will be treated fairly; and
- people will have access to useful information about the activities and achievements of public entities.

The private sector also depends on good public sector governance and accountability. Our economy is based on international trade – our reputation for being largely free from corruption and an easy country to do business with is a competitive advantage.

In my opinion, the quality of governance in the public sector can be improved. It is not working as well as it should in some entities and problems have occurred and will continue to do so, unless the standard is raised.

One matter for improvement is the clarity of role definition between the responsibilities of governance and management at both an organisational and project level. This report identifies examples of good and poor practice in this regard.

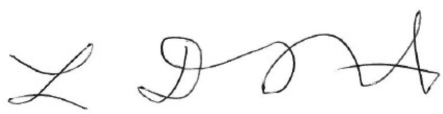
A second matter for improvement is risk management. Top-class examples of good practice are hard to find.

In New Zealand, there is an expectation of accountability and transparency. Fortunately, New Zealand has a well-established public management system with strong accountability foundations. However, we should not take this for granted or be complacent. Our recent fall from second to fourth in Transparency International's Corruption Perceptions Index 2015 gives us an opportunity to pause and ask what we can do better.

This report reflects on common issues and challenges, and examples of good and emerging practice, that public entities can use to help improve their governance and accountability arrangements. From the practices we observe and assess during our audits, we have identified eight elements of good governance. I encourage entities to use these to consider their own governance arrangements. I also highlight some emerging trends, such as new reporting standards that present both challenges and opportunities.

We are not alone in considering governance to be important. "An honest and responsive government" was ranked fourth (behind a good education, better healthcare, and better job opportunities) by the 9.7 million respondents to the 2015 United Nations-led MY World survey. The survey asked citizens to pick six out of 16 possible issues that would make the most difference to their lives.

I encourage everyone reading this report to ask themselves how they can build on the solid foundations and apparent opportunities to improve the governance and accountability of our public sector.



Lyn Provost
Controller and Auditor-General

8 April 2016

Governance and accountability

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1.1 Every year, we audit those public entities that are required to publicly report (about 3700) and prepare 20-30 in-depth reports on specific matters. This work brings us into direct and regular contact with the governors, managers, and staff of public entities.

1.2 Much of our work involves auditing the financial and performance information reported by public entities to Parliament and the public. They, in turn, hold these entities to account.

1.3 Our unique view of the public sector and, in particular, of matters relating to the governance and accountability of public entities, provides an opportunity to highlight and share examples of good and poor practice to help the public sector to improve.

1.4 This report reflects on the findings from my Office's work in 2014/15 that focused on governance and accountability. We chose this theme for three main reasons:

- Changes arising from ongoing fiscal constraints, a strong focus on better public sector performance, and structural changes have resulted in an increasing need for high-quality governance.
- Accountability is fundamental to our system of government.
- There have been changes to financial reporting and public sector accountability legislation that took effect from 1 July 2014.

1.5 We also note the increasing emphasis on governance and accountability arrangements beyond traditional organisational boundaries, which makes our focus timely.

What is public sector governance?

Public sector governance is different

1.6 Governance refers to the systems and processes for leading and guiding an organisation. It is about the arrangements and practices that allow an entity to set its direction and manage its operations to achieve its outcomes and to fulfil its accountability obligations.

1.7 There are a number of factors that make governance in the public sector complex and challenging. Some of the essential elements needed for effective governance are not always clearly present in the public sector:

- public entities sometimes do not have a conventional company/board structure (for example, government departments and statutory officers);
- some public entities are statutory bodies required to operate within a particular legal framework – they can do only what their founding/enabling legislation permits;

- there can be conflicting objectives – profit or public good; risk or return;
- some public entities are established to achieve only a particular purpose – for example, Treaty settlements that give rise to co-governance (and co-management) arrangements;
- governors can be elected, appointed, or a mixture of both – creating the possibility of capability issues, and/or mixed obligations to one or more constituencies;
- there are understandably greater expectations of accountability and transparency for those using public resources, meaning governors are usually operating in the public eye; and
- public entities are often subject to strict expectations and rules for conflicts of interest.

1.8 In Part 2, we use the findings from our work to identify the elements of governance that work in the public sector and we highlight examples of good – and not so good – practice.

What is accountability?

Accountability enables trust in government and needs constant attention

1.9 Developing and maintaining citizens' trust in government is vital to maintaining a healthy democracy. It requires credible and reliable information about the performance of public institutions and their future intentions. Public trust depends on, among other things, good governance and accountability and they can be a catalyst for it; governance and accountability need and support each other.

1.10 With the trust of its citizens, a government is better able to move beyond short-term, reactive approaches to governing to a more holistic, strategic, and longer-term vision. Trust in public institutions is driven, in large part, by:

- the way policies are designed and implemented; and
- the way policy-makers comply with standards to ensure that their behaviour is in the interest of citizens.[1]

1.11 Public accountability enables citizens to see how their taxes and rates have been used. It should also provide an insight into what has been achieved by the public sector. Those responsible for governance need to be accountable for the decisions that they make and the basis on which they are made. Their decision-making processes need to be legitimate and be seen to be so.

1 Organisation for Economic Co-operation and Development (2014), *Partners for Good Governance: Mapping the role of Supreme Audit Institutions.*

1.12 Increasingly, they also need to be accountable for the stewardship of the organisations and assets they govern. This gives a forward-looking as well as backward-looking dimension to governance and accountability responsibilities.

1.13 Good government requires that those in power, and the public entities that work for those in power, be held publicly accountable – for what they do, and what they omit to do.

1.14 In a report on a recent inquiry, we noted:

> *It is ... fundamental that public entities should be able to demonstrate what they are doing and why, when that is questioned. Public entities should expect to be tested, whether by members of the public, the media, or the courts. This is accountability in action, and public entities need to be ready to explain themselves. That has implications for how public entities operate on a daily basis: they need full and proper records of their work that show what decisions were made, who made them, and the basis on which they were made.*[2]

1.15 A public entity's processes must not only be right, but be seen to be right. Without accountability and transparency, allegations of bad practice and corruption can flourish.

1.16 In essence, public accountability is necessary for the public to be able to see that public resources – the taxes and rates that most of us pay – are being used appropriately and effectively.

What accountability arrangements have changed?

Changes to state sector and public finance legislation

1.17 The State Sector and Public Finance Reform Bill 2013 amended the three main Acts that govern how the State sector and the finances of public sector entities are managed. These Acts are the State Sector Act 1988, Public Finance Act 1989, and Crown Entities Act 2004.

1.18 The Acts were changed to:

- improve the focus on results;
- encourage improved service levels and value for money;
- support meaningful reporting so that Parliament and the public can more easily see what has been achieved; and
- strengthen leadership at the "system", sector, and agency levels.

2 Controller and Auditor-General (2013), *Inquiry into the Mangawhai community wastewater scheme*, Wellington, page 16.

Changes to local government legislation

1.19 Section 39 of the Local Government Act 2002 outlines the governance principles that local authorities must act in keeping with. In August 2014, the Act was amended. The changes have shaped how local authorities are now required to consult with their communities on long-term plans and introduced new requirements for infrastructure strategies. We consider that these changes should enhance the accountability of local authorities to their communities.

Amendments to other relevant legislation

1.20 There have also been recent changes to the Financial Reporting Act 1993 and the Companies Act 1993. In 2013, the Financial Reporting Act 1993 was replaced by the Financial Reporting Act 2013, and the reporting requirements for companies are now set out in the amended Companies Act 1993.

1.21 The broad aims of the changes were to introduce the new accounting standards framework, reduce compliance costs, and streamline reporting by companies and their subsidiaries.

Changes in financial reporting standards

1.22 In our recent report, *Improving financial reporting in the public sector*, we described the positive changes made to accounting standards in the public sector. These changes include adopting accounting standards in New Zealand based on International Public Sector Accounting Standards (IPSAS) for most public entities.

1.23 The framework uses tiers so that financial reporting requirements reflect the different size and nature of reporting entities. The tiered structure is likely to help smaller entities achieve a better balance between the costs and benefits of general purpose financial reporting.

1.24 We encourage all public entities to take full advantage of any financial reporting concessions that are available to them in the tiered reporting structure.

1.25 The changes have better positioned the public sector to report in a manner that better meets user needs. Public entities now need to take advantage of the flexibility within the new framework by focusing on users' information needs and reporting what matters most.

1.26 The way is open for public entities to change the focus of their reporting from complying with specific accounting standard requirements to better communication with users of their financial statements. This should enhance accountability.

1.27 The setter of accounting standards in New Zealand, the External Reporting Board, also has an important ongoing role in helping to resolve some of the more challenging areas of general purpose financial reporting.

1.28 In Part 5, we highlight our observations about how well the public accountability system is working.

2 How to get governance right to strengthen accountability

2.1 There are many different definitions of, and principles for, good governance. There is no single right or wrong set of guidance or rules. Many factors need to come together for a governing body to perform its role effectively.

2.2 Our governance-focused work has covered a broad range of entities that manage important, high-value projects and programmes for New Zealanders.

2.3 We examined the governance arrangements for a business transformation programme in the Inland Revenue Department (Inland Revenue); three projects to rebuild essential facilities in Christchurch after the Canterbury earthquakes; and six entities responsible for ensuring that New Zealanders have access to our arts, culture, and heritage. Appendix 1 lists the reports we published under this theme and other relevant reports.

2.4 This Part expands on the eight elements we consider are essential for governance to be effective. Although the elements are important in their own right, those involved in public administration need to consider how they apply to the particular context of the entity or project that they are involved in. This applies to members of governing bodies and also to chief executives and senior managers who report to, and work with, governing bodies.

2.5 The elements apply to organisational (or corporate) governance and programme or project governance.

2.6 Appendix 2 sets out some links to good practice guides, useful toolkits, and other governance-related resources.

Element 1: Set a clear purpose and stay focused on it

2.7 Governors of an organisation should set out a clear strategic purpose and a clear direction for how to achieve that purpose. Governors' strategic thinking and planning to prepare a coherent strategy is fundamental to effective governance. It is one of their most important roles.

2.8 Governors need to contribute to, and challenge, the strategic planning process, based on an understanding of stakeholder expectations and the wider context that their organisations operate in. Strategic direction-setting includes setting realistic medium- and long-term outcomes and short-term priorities, and expenditure/investment choices and budgets.

2.9 Once established, the governing body needs a shared and strong understanding of the strategy and use that understanding to inform its decisions. The governing body must also consider how it maintains oversight of progress against the strategy and any significant deviations from it, emerging risks, and the delivery of planned benefits from any major change programmes. The governing body may need to review and update the strategy to adapt to changing circumstances.

2.10 Governors have told us that it is easy for governing bodies to become too focused on details – to manage rather than govern. It takes discipline to stay focused on strategy and to take a long-term view.

2.11 Clarity of purpose is also important at the specific project and programme of work levels. The absence of a consistent explanation of the aims of Whānau Ora contributed to confusion among many of the people we spoke to as part of our audit of that initiative.

2.12 Inland Revenue did a good job in setting a clear direction for its business transformation programme. Clearly understood aims generally lead to clear accountability and useful and timely reporting.

Element 2: Have clear roles and responsibilities that separate governance and management

2.13 This element is one of two where we found the greatest room for improvement. The roles and responsibilities of each party, including governing board members, shareholders, management, staff, and other parties (such as stakeholders) must be clearly defined. Clear roles and responsibilities make the differing interests transparent and foster effective decision-making. It is important to clearly define roles and responsibilities right at the start of an entity's or project's life, and to revisit them periodically.

2.14 A governance charter, or governance statement, can be a useful way to outline the structures, principles, and processes to be followed. However, the art of effective governance is in the execution of what is set out in the charter.

2.15 Good governance requires a clear distinction between the role of governance and the role of management. Governance involves ensuring that systems and processes are in place that shape, enable, and oversee the management of an organisation. Management is concerned with carrying out the day-to-day operations of the organisation. There is a need to guard against the risk of governors becoming involved in operational decisions because it limits their ability to then hold management to account.

2.16 We have noted a recent increase in the liability of governors. This could have the unintended consequence of driving governors deeper into management and operational matters, potentially undermining the work of management.

2.17 In practice, the separation between governing bodies and management is often not a black and white split but more of a grey zone – how well that zone operates is a function of trust and confidence based on honesty and open communication.

2.18 If there is limited trust and confidence between governors and managers, it is more difficult to build an environment in which an organisation can succeed. With stronger trust and confidence, the grey area can work to everyone's advantage – governors can probe and be "let in" to issues by managers. This can build governors' understanding of the issues and confidence in how management is dealing with them.

2.19 Clear roles and responsibilities and a clear separation between governance and management is made challenging by the fact that many project governance groups often include, or are even entirely comprised of, managers. Such groups can operate either outside or alongside the organisational governance structure. This raises questions about the understanding managers are able to bring to an internal governance role and how they are able to reconcile that role with their managerial responsibilities.

2.20 When an organisation is facing particularly challenging issues, it can be appropriate for the governing body to become more closely involved in operational matters. A recent example of this was the more hands-on role played by the board and, in particular, the chairman of Te Papa Tongarewa (the Museum of New Zealand) during the transition phase between chief executives. The chairman became more involved in operational decisions, providing visible leadership to the organisation and being the spokesperson for media inquiries.

2.21 An important aspect of the distinction between governance and management is the allocation and delegation of decision-making rights. Governance documents, such as charters and terms of reference for the governing body and any sub-committees, provide a vital framework for clarifying and delegating respective roles and responsibilities. Formal instruments of delegation are an important part of governance documents.

2.22 Our audit of governance in the arts, culture, and heritage sector found that the boards of six entities we looked at were clear about the difference between the roles and responsibilities of the board and those of management. These roles were well set out in the board charters and policies of the entities.

2.23 In our audit of the Auckland Manukau Eastern Transport Initiative (AMETI) programme, we found that a change in the composition of the Programme Control Group led to the same person being the chairperson of that group as well as the programme sponsor, manager of the division responsible for delivering the programme, and line manager of the programme director.

2.24 This person was also responsible for chairing the AMETI advisory group and the main stakeholder forum. In our view, this placed too much responsibility in the hands of one person and reduced the reliance that the Board of Auckland Transport could place on the Programme Control Group for independent guidance and advice.

2.25 A strength in Inland Revenue's governance of the business transformation programme was that, despite a complex governance structure, the roles of the many separate groups that had governance roles were clear; each of these groups had clear terms of reference and clearly defined accountabilities.

2.26 In our audit of the three Christchurch rebuild projects, we found that the governance arrangements for the bus interchange had been well thought out. There were clear roles for each part of the governance structure, and people understood these roles.

2.27 However, the governance arrangements for the new central library project were initially not well defined, with no clear separation of governance and management. During our audit, Christchurch City Council made substantive changes to its governance arrangements for this project and provided more clarity about the project's governance.

The art of governance against the discipline of project management

2.28 Good governance is necessary to oversee major programmes and projects so that they deliver their intended benefits, at the intended price, at the intended time. We found examples of governance and project management being merged and confused. This is worrying.

2.29 Independent quality assurance is important in large projects to provide assurance to the project manager and those charged with governance that a project is being run successfully. In some projects that we looked at, governance and project management were being confused. As noted above, the new central library project in Christchurch initially did not have a clear separation of governance and management. The Project Control Group was acting at a management level and did not show the level of oversight we expect for a governance group.

2.30 We found similar issues in the AMETI programme – the purpose of the Programme Control Group was not well understood, and the chairperson had both governance and project management responsibilities.

2.31 Many projects have long lives. Inland Revenue's business transformation programme is expected to take a further 10 years to be fully implemented. The Auckland Manukau Eastern Transport Initiative (AMETI) has a planned delivery timescale to 2028. Therefore, it is important that the people responsible now for governing and managing this programme clearly understand its purpose and continuing strategic fit with other regional plans for Auckland.

2.32 Projects will often be broken down into manageable tasks. Although it is possible to separate tasks at a working level, project governors need to keep oversight of the project as a whole, while the organisational-level governance (often a board) needs to provide oversight of projects as well as the entity's "business as usual" activities.

Element 3: Lead by setting a constructive tone

2.33 The leadership role of governors is to set a suitable tone from the top that shapes the culture and demonstrates the desired values and ethics of the organisation. This is achieved through establishing and approving policies, making decisions, and the approach and behaviour the board takes to its work, both with management and external stakeholders.

2.34 In our audit in the arts, culture, and heritage sector, we identified four factors that contribute to good leadership and culture:

- a clear distinction between governance and management;
- the chairperson's relationship with other governors and management;
- an effective relationship between governance and management; and
- the governors' ability to challenge the management team.

2.35 The chairperson is the cornerstone of effective governance arrangements and the governing body working together well. The governing body appoints the chief executive. The chairperson and chief executive need to develop and maintain a relationship based on mutual trust and respect. However, in this relationship, the chairperson still needs to be able to challenge the management team.

2.36 The quality of this relationship will determine how easy it is for the governing body to ask questions openly, freely challenge management, and get the answers it needs. A strong relationship between the chairperson and chief executive is critical in supporting an effective overall relationship between governors and managers.

2.37 As well as providing the basis for governance to be effective, strong leadership is also necessary to address difficult situations when they arise.

2.38 A positive aspect of the acute services building project in Christchurch was the strong leadership provided by the Hospital Redevelopment Partnership Group. This group's leadership kept the project moving despite the difficulties in other parts of the governance arrangements.

Asking powerful questions

2.39 The governing body's questioning of management needs to be constructive and testing. Effective governors use their combined experience and skills to query information, to probe, and to challenge so they can make informed decisions. Governing bodies need to keep asking questions until they understand what they are being asked to approve. Sometimes decisions need to be deferred until further information is supplied.

2.40 It helps if governors ask powerful questions. One governor shared these questions with us and they seem to be a useful guide for a governing body to have the right conversation with management:

> What are the entity's three top risks and how did you arrive at those risks?
>
> Who are our customers?
>
> Have we carried out a project of this size before? If so, what did we learn?
>
> Do we have the right team in place to carry out this project and realise the benefits?
>
> What are the three top risks in this project?
>
> Why should the entity carry out this project and how does it link to our strategic plan?
>
> How clear are the accountabilities and ownership for this initiative?
>
> How could this service be delivered differently?
>
> Do we understand our project portfolio? What are the main links and interdependencies?
>
> What are our most important performance indicators?
>
> How will we know whether we are successful?

Element 4: Involve the right people

2.41 Governance is characterised by a series of personal interactions between people operating within structures and policies. Good governance needs good people.

2.42 For governance to be effective, it is critical that the right people are involved. The level of trust between people – between governors, management, and stakeholders – affects the effectiveness of the governance arrangements.

2.43 Having the right mix of people and skills on a governing body should help it to be more effective. An effective board will have members who bring multiple perspectives, who debate issues robustly, and who then speak with unity of voice and message about the decisions made.

2.44 Governing bodies need to invest in capability so that the right mix of skills are applied to ensure that organisations deliver value and manage risks effectively.

2.45 Having a mix of wise heads and newer governors who can learn from them is important, as is having a mix of "big picture" thinkers and people who bring much-needed specialist knowledge.

2.46 The wise heads, those people with the skills and experience to take a strategic view, identify the issues and risks to focus on, and who know how and when to dive deeply to probe specific opportunities or risks, add huge value to boards.

2.47 Demographic changes are resulting in New Zealand's population becoming older and more ethnically diverse. There is a need for governing bodies to change their membership to reflect this changing demographic. Diverse backgrounds and ways of thinking provide a depth of perspective to the role of governance.

2.48 In our 2014 report, *Maintaining a future focus in governing Crown-owned companies*, some interviewees told us that it was a challenge to achieve the right mix of skills while maintaining a positive team dynamic at the board table.

2.49 Identifying gaps in the board's skill set and filling vacancies accordingly can be very beneficial. Some governing bodies have a mix of members – some appointed by the Government and others elected by the public. Some governing bodies compensate for skills gaps by bringing the relevant skills onto their audit committees through the appointment of independent members.

2.50 Co-governance arrangements in the environment sector illustrate well the challenges with getting the right people in governance roles. Experienced people are in short supply and those who are experienced are busy. Another feature of the governance of these arrangements is that some iwi members might not be experienced in governance matters but bring a depth of connection, perspective, and cultural knowledge that others might not have.

2.51 For longer term projects, such as AMETI and Inland Revenue's business transformation project, governance arrangements might need to change over time. Change can be necessary because individuals, both governors and managers, might change during the life of a project, as might the nature and risks of the project. Adapting the governance arrangements will help to ensure that the right skills are brought to bear as the project evolves.

Induction and training

2.52 How entities invest in and develop new governors is important. It is vital that new people receive a formal induction into the organisation they will be governing. This is an important first step to becoming an effective member of that organisation's governing body: that is, developing an understanding of how the organisation is meant to function, and its business and goals.

2.53 In our work in the arts, culture, and heritage sector, we identified that the training and professional development available to board members could be improved. The governance induction workshops for new board members run by the Ministry for Culture and Heritage could be extended to provide ongoing programmes for boards and senior managers in that sector.

2.54 Spending time on a board will equip members with the knowledge and experience required to contribute to that organisation's governance. The ongoing interactions and discussions with managers and other board members provide valuable on-the-job training.

2.55 From our work on audit committees, we know that committee members value the opportunity to share and discuss experiences in safe, collegial environments. We convene a regular forum for chairpersons of audit committees to have relatively informal discussions about matters of mutual interest.

2.56 Depending on a person's background, there can also be a need for formal training for governors on topics such as changes to financial reporting standards and to legislation (for example, the Health and Safety at Work Act 2015).

Board appointments process

2.57 Many governors and some officials have talked to us about the public sector board appointments process, particularly for appointed governors.

2.58 Some governors have expressed the view that they would like more of a voice in identifying new governors who could offer the particular skills and experience that their governing body needs, and then recruit new board members to meet these needs.

2.59 It is beyond our mandate to comment on the government appointment process. The State Services Commission, the Treasury, and specific departments have a role to advise Ministers on such matters.

2.60 For council-controlled organisations (CCOs), local authorities are required by the Local Government Act 2002 to have an objective and transparent process for appointing CCO governors. In our report on CCOs, we recognised the value of including the chairperson of the CCO board in that process.

2.61 Regardless of the approach taken, good governance needs good people. It is important that a board's needs are identified and directors appointed who can meet those needs.

Element 5: Invest in effective relationships built on trust and respect

2.62 Effective relationships are critical for good governance. We have already noted that strong relationships between governors and management are essential. These relationships should be based on mutual respect and trust. However, they should not become too cosy.

2.63 Strong relationships between governors and stakeholders are also important. Effective stakeholder engagement is of particular value in understanding stakeholder views when making important decisions, forming strategies, and identifying sources of funding. Good practice involves preparing formal stakeholder engagement plans or formal relationship protocols with important stakeholders.

2.64 In our report looking at the governance and accountability of CCOs, we found that a CCO's success depends largely on an effective relationship between the CCO and its local authority shareholders. Such a relationship goes beyond the statutory requirements and requires ongoing commitment from both parties.

2.65 Despite the name "council-controlled", we found that CCOs are most successful when the local authority seeks to influence rather than control the CCO. To work in practice, the relationship needs to be close enough for the local authority to know how the CCO is performing but allow the CCO to operate at arm's length.

2.66 In our work on co-governance arrangements in the environmental sector, we noted the importance of taking the time to build and maintain relationships, and of maintaining a shared understanding of different parties' aspirations. The quality of the relationship between the parties to a co-governance arrangement affects its chances of success.

2.67 The parties need to invest in their relationships and involve people who value relationships. This means having people who are willing to work together, listen to and learn from each other, and who are willing to try and understand each other's perspectives. Co-governance requires diplomacy, a willingness to compromise, and the ability to persuade and influence without being domineering or disrupting.

2.68 Our February 2015 report on education for Māori highlighted the importance of effective relationships between schools and whānau, in which a school's governors, teachers, students, and families work together to improve students' overall performance.

2.69 These relationships are more effective when there is clear communication, there is a willingness to be flexible to enable effective participation, and communities feel listened to. This is not easy and requires constant attention.

Element 6: Be clear about accountabilities and transparent about performance against them

2.70 Governance practices need to support accountability. Governance structures should include a clear accountability framework that shapes how an organisation's (or project's) financial and operational performance will be monitored and reported. The framework should also cover how the governing body will be accountable for future-focused decisions, such as maintaining and enhancing the capability of the organisation.

2.71 Effective governance depends on governing bodies receiving regular reports that provide a clear and objective view of an organisation's (or project's) performance. Governing bodies need to be provided with enough detail to support performance management and decision-making, while avoiding unnecessary details about operational matters.

2.72 We found that the three rebuild projects in Christchurch we reviewed would benefit from producing a clearer accountability framework that includes specific and general accountabilities for all levels of these projects.

2.73 We also found that accountability to the public worked best when people were told how their input had been used in a project. We saw good public accountability when a range of social and other media were used to keep people up to date about project progress.

2.74 We see challenges for local authorities in setting up CCOs because the local authority remains accountable to its community for the CCO's performance. The local authority needs to have in place effective monitoring processes to enable it to discharge its accountability obligations. This requires the local authority to:

- have structures, systems, information, and capability to promote its interests in the CCO, influence the direction of the CCO, and monitor its performance; and
- show its community that it is managing the community's financial and operational interests in the CCO in an effective and efficient manner.

Element 7: Manage risks effectively

2.75 In our view, risk management is one of the two least mature elements of governance in the public sector. We see few examples of excellence.

2.76 Identifying, understanding, and managing risks is a fundamental part of effective governance. As a senior public servant said recently, "good governance keeps the fan clean".

2.77 As well as avoiding failures, good governance can ensure that opportunities are not missed. Governing bodies that think strategically and consider their organisation's role in a wide context are more likely to identify and be in a position to take opportunities for better financial or operational performance, or to achieve benefits faster.

2.78 Governing bodies have a leading role in establishing an organisation's overall understanding of risk, including the potential effect of its strategic, financial, operational, and reputational risks.

2.79 Effective risk management by public entities involves identifying, analysing, mitigating, monitoring, and communicating risks. We expect to see a risk management framework and register that is formally defined, widely understood, and aligned to the organisation's strategy, risk appetite, objectives, business plan, and stakeholder expectations.

2.80 In our inquiry work, it is often clear, with the benefit of hindsight, that there were warning signs that things were going wrong. The inability of an entity to identify these signs, or to "join the dots" between pieces of information, is often a reason why problems arise. Good governance of risks or threats to an organisation can prevent such failures.

2.81 One good example we saw was Inland Revenue's approach to managing risks to its business transformation programme. Strengths of the approach included a strong focus on risk identification and management. The risk management culture appeared mature and a good risk management framework and associated reporting structure were built into the design of the programme's governance.

2.82 In managing risks, Inland Revenue's approach included scheduling reviews of governance structures and focusing on balancing executive leadership's time between programme governance and managing the current tax system. We recommended that Inland Revenue keep doing these things during the life of the business transformation programme.

2.83 In contrast, for the five governance aspects we looked at in our audit of governance in the arts, culture, and heritage sector, we found that, while entities had formal risk management frameworks, practices were variable. Risk registers tended to focus on operational rather than strategic risks and they had not been reviewed for some time.

Getting the best from audit and risk committees

2.84 Effective risk management also involves having clear roles for audit and risk committees.

2.85 All organisations need governance arrangements and practices to continuously evolve and to manage risk. Many public sector entities choose to establish a group of advisers to give advice to, and to test and challenge, the governing body and management. Such groups go by many names (such as audit, risk, or assurance committees or advisory groups). They take a range of different approaches, from those that are largely reactive to those that take a forward-thinking, proactive, and more strategic approach.

2.86 For example, an audit committee could focus on the evaluation of compliance and financial effectiveness for the purchase of an asset, or it could play a broader and deeper role and focus on the useful life of an asset. Through our work with members of audit and risk committees, we identified principles that help an audit committee add value: independence; clarity of purpose; competence; and open and effective relationships. What makes a committee work best is applying these principles in the context of the entity.

2.87 We released a discussion document to start the conversation about how public entities use audit committees. Many members of audit committees told us that there is not necessarily a "best practice" way of solving the issues that audit committees in the public sector face.

2.88 This is because solving these issues requires experience, judgement, perspective, and knowledge of the entity's context. Those involved with committees told us that discussions with people in similar situations are helpful, as is knowing how others manage similar issues, risks, and opportunities.

2.89 We also consider that discussions between audit committees and their external auditors can be a useful way to highlight issues and bring a different perspective to them.

2.90 We have resources about audit committees on our website. The aim is to support discussions between audit committee members so that they can learn from each other about what works well – and what does not.

Element 8: Ensure that you have good information, systems, and controls

2.91 Governors are accountable for the decisions they take. Therefore, they need relevant, accurate, and up-to-date information to make good decisions.

2.92 Governing bodies also have a role in assessing the design and effectiveness of an organisation's internal systems and controls. These systems and controls are organisational (terms of reference, independence, and separation of duties), operational (planning and budgeting) and about personnel (recruitment, training, and development).

2.93 These systems and controls are critical to providing assurance that an organisation's activities are compliant and in line with expectations. The governing body has a role to review them regularly to ensure that they remain fit for purpose.

2.94 Our 2012 inquiry into aspects of the board-level governance of the Accident Compensation Corporation (ACC) followed allegations that an ACC claimant had benefited from approaching a member of the ACC board whom she knew. We found no evidence that the approach had affected her claim.

2.95 However, we found that the board, at that time, had no formal policy to guide board members on communication with individual claimants when there is a high risk that board members will know claimants, given that most New Zealanders will be a claimant at some time. In early 2014, we noted that ACC had addressed the concerns we had raised.

2.96 An "off the shelf" set of policies and controls will not always be enough. Governing bodies need to think about their organisation's particular circumstances.

2.97 Our inquiry into Health Benefits Limited (HBL) identified a similar problem; that HBL's board lacked timely and accurate information to inform its decisions. We noted the changes that HBL made to address this problem. A lesson from that inquiry is that governing bodies need good-quality information before making significant decisions and must be confident that they have enough information before making a decision to proceed with a programme.

2.98 As well as needing good systems and information to support internal decision-making, good information is also required to keep stakeholders informed of progress and of important decisions that are made.

2.99 Today, the public has access to more information and data than ever before. People expect public entities to keep them informed and engaged. Members of the public have a right to know that their taxes and rates are being used appropriately and they deserve answers when things go wrong.

2.100 Good information supports public entities' effective engagement with the public.

3 Governance in government departments is different

3.1 The public sector has many forms of governance. In this report, we have discussed councils in local government and boards in Crown entities and State-owned enterprises. The governance structures for these entities is clear, at least in theory. The governance structure for government departments is less clear. We have often been asked how governance works in government departments.

3.2 The governance of departments is shared between the responsible Minister and the chief executive. In practice, chief executives have dual roles as both governors and managers of their departments. This duality is also present in the roles of departmental leadership teams, which are expected to function as both governance and management bodies. The challenge associated with having these dual roles – the need to be clear about when to act as a governor and when to act as a manager – needs ongoing attention.

3.3 In understanding these particular arrangements, it needs to be remembered that constitutional conventions and norms play an important role in guiding how the system of public service responsibility to Ministers works. The public service is politically neutral; it serves the Government of the day and its neutrality is protected by the State Services Commissioner. In New Zealand, senior public sector leaders do not change because a new government is elected.

Ministers' role

3.4 The Cabinet Manual sets out the role, responsibilities, and powers of ministers (this relates to the element of good governance: roles and responsibilities). The manual also sets out the relationship between Ministers and the public service, and in particular with chief executives. Among other responsibilities, Ministers:

- make significant decisions and determine government policy collectively, through the Cabinet decision-making process (*clarity of purpose – element 1*);
- determine both the policy direction and the priorities for their departments (*clarity of purpose – element 1*);
- are supported by and (to varying degrees, depending on the nature of the entity) direct officials in the State services and the wider State sector (*good leadership – element 3*);
- are members of Parliament and accountable to the House for their policies, their performance, and the performance of entities within their portfolios (*clear accountabilities – element 6*); and
- have a political role in maintaining government stability, which requires maintaining close working relationships with all other parties as issues arise (*effective relationships – element 5*).

3.5 In general terms, Ministers are responsible for determining and promoting policy, defending policy decisions, and answering in the House on both policy and operational matters. A department must provide information to its Minister about its strategic intentions. However, Ministers should not be involved in their departments' day-to-day operations.

Ministers' relationships with chief executives

3.6 The formal relationship between Ministers and the public service is governed primarily by the State Sector Act 1988 and the Public Finance Act 1989. The relationship is also governed by convention, important aspects of which are set out in the Cabinet Manual.

3.7 The main point of contact between the Minister and a department in the public service is the chief executive. Chief executives are responsible to their portfolio Ministers, under section 32 of the State Sector Act 1988, for:

- carrying out of the functions and duties of the department (including those imposed by statute or by the policies of the Government);
- tendering advice to their own Minister(s) and other Ministers;
- the general conduct of the department; and
- the efficient, effective, and economical management of the department.

3.8 Chief executives are responsible to their responsible Ministers for the financial management and performance of their departments under section 34 of the Public Finance Act 1989. This is important for accountability and relies on effective risk management and good information systems and controls.

3.9 Also, the 2013 amendments to the State Sector Act 1988 set out chief executives' responsibilities for the stewardship of:

- the department or departmental agency including of its medium- and long-term sustainability, organisational health, capability, and capacity to offer free and frank advice to successive governments;
- assets and liabilities on behalf of the Crown that are used by or relate to (as applicable) the departmental or departmental agency; and
- the legislation administered by the department.

3.10 There are also system-wide stewardship expectations for chief executives set by the State Services Commission to:

- collaborate with others to improve service delivery and the achievement of outcomes; and
- create a larger and deeper pool of leaders with the skills and experience to fill senior positions in the public service and the wider State services, now and in the future.

3.11 As well as the core expectations of chief executives, in late 2015, two areas of performance were singled out for stretch system-wide stewardship expectations: delivery of results and people leadership.

3.12 We expect these changes to the public management system will drive new governance arrangements, such as cross-agency and network governance, which we highlight in Part 6.

3.13 In summary, departmental chief executives have dual roles as both governors and managers of their departments. Some also have functional leadership responsibilities. Chief executives need to balance the strategic view with "business as usual" activities. This involves balancing how they develop and maintain the long-term capability of the department with the day-to-day management responsibilities of running the department and delivering the advice, programmes, and services to meet the Government's policy objectives.

Managing conflicts of interest

4

4.1 Some of my Office's inquiry work is about actual or perceived conflicts of interest. Conflicts of interest are ever-present for those in governance roles, particularly given New Zealand's small population. Conflicts of interest exist when two different interests are opposed, or are in conflict to some degree. For governors, the conflict needs to be with a governor's obligations as a governor, and/or with the interests of the organisation.

4.2 It is inevitable that those in governance roles will have interests that could come into conflict (whether real or perceived) and create risks to the impartiality of decision-making. For example, in small communities, elected members of local authorities will have many connections through family and friends with many of the matters coming to the Council for a decision.

4.3 Conflicts of interest are not necessarily problems – they are a reality. It is how they are identified and then managed that determines whether they are a problem.

4.4 Those in governance roles need to manage their interests in a way that is transparent and does not compromise the decision that is being made by the public entity. In many of our previous publications on conflicts of interest, we have said that there are three steps that governors and public entities need to take:

- recognising that there is a conflict of interest;
- disclosing the conflict of interest; and
- managing the risks associated with the conflict of interest.

4.5 For elected councillors, the Local Authorities (Members' Interests) Act 1968 is a small subset of the law about conflicts of interest that must be considered. That Act has two specific rules – elected councillors cannot:

- enter into contracts with their local authority worth more than $25,000 in a financial year; or
- participate in matters before their local authority in which they have a financial interest (referred to as a pecuniary interest in the Act) other than an interest in common with the public.

4.6 If an elected member has a financial interest, they must consider the requirements of the Act in recognising, disclosing, and managing their conflict. Some of the actions below for managing and mitigating a conflict of interest will not be available to elected councillors with a financial conflict of interest.

Recognising a conflict of interest

4.7 In the public sector, there is a conflict of interest where:

> *A member's or official's duties or responsibilities to a public entity could be affected by some other interest or duty that the member or official may have.*[3]

4.8 There are many different types of conflicts, from financial conflicts of interest to a conflict in roles or duty.

4.9 Most people in governance roles understand when they have a conflict of interest. There is a small minority who do not, and this can cause significant difficulty – from fractious relationships in the governing body, to judicial reviews of decisions, to community mistrust.

Disclosing the conflict of interest

4.10 Most governors and officials are good at disclosing conflicts of interest. When disclosing a conflict of interest, it is better to err on the side of openness. This is the responsibility of the person who has the conflict.

4.11 Many governing bodies have an established practice of their members declaring their interests as a matter of routine at the start of each meeting. Many entities require this – having a policy that sets out how members should declare interests is good practice.

Managing the conflict of interest

4.12 However, simply declaring the conflict of interest is not usually enough. The person declaring the conflict is not best placed to decide how it should be managed. The governing body needs to consider carefully what needs to be done to manage the risks associated with a conflict. The notion of managing conflicts of interest as a peer-driven activity around the board table is useful.

4.13 Our experience is that conflict of interest questions are more likely to be grey than black and white. Deciding how to manage them is sometimes neither clear nor straightforward and requires careful judgement.

4.14 There is a broad range of options for managing or mitigating a conflict of interest. The options (listed roughly in order of lowest to highest severity) include:

- taking no action, transparency is enough;
- asking whether all affected parties will agree to the person's involvement;
- seeking a formal exemption to allow participation (if such a legal power applies);
- imposing additional oversight or review over the person;

3 Controller and Auditor-General, (2007), *Managing conflicts of interest: Guidance for public entities*, Wellington, page 13.

- withdrawing from discussing or voting on a particular item of business at a meeting;
- exclusion from a committee or working group dealing with the issue;
- re-assigning certain tasks or duties to another person;
- agreement or direction not to do something;
- withholding certain confidential information, or placing restrictions on access to information;
- transferring the person (temporarily or permanently) to another position or project;
- relinquishing the private interest; or
- resignation or dismissal from one or other position or entity.[4]

4.15 It ought to be rare that a conflict of interest is so pervasive and all-encompassing that a person cannot remain a member of the governing body.

4.16 When we considered allegations of conflicts of interest affecting Ashburton District Council's decisions on a second bridge, we noted that, although our good practice guides on conflicts of interest encourage a precautionary approach (with the advice "if in doubt, stay out"), for matters of high community and political significance, an elected member with a marginal non-financial interest might decide that this approach was unduly restrictive.

4.17 Our observation is that taking a precautionary approach has often become the "rule" in managing conflicts of interest, as opposed to careful consideration of the range of options outlined in paragraph 4.14.

4.18 Although this is often the result of the public entity and person trying to "do the right thing", the stand-down might not be necessary nor the best outcome.

4.19 It is reasonable that members of a governing body will bring their own experience and knowledge to a decision-making process. Often, people are in governance roles for this very reason. It would be unreasonable to expect that this knowledge is not used. In many instances, we have concluded that it would still be reasonable for the affected party to continue to be involved in the decision-making process with the consent of affected parties.

4.20 In our consideration of allegations of conflicts of interest relating to Katherine Rich's roles as a board member of the Health Promotion Agency and as chief executive of the New Zealand Food and Grocery Council, we noted that the Crown Entities Act 2004 states that a person does not have a conflict of interest only because they have "past or current involvement in the relevant sector, industry, or practice".

4 Controller and Auditor-General, (2007), *Managing conflicts of interest: Guidance for public entities*, Wellington, page 31.

4.21 That said, we note that, in the recent Problem Gambling Foundation case,[5] the High Court set a high standard for public entities managing conflicts of interest in a procurement process. The Court applied the rules set out in the then Ministry of Economic Development's *Mandatory Rules of Procurement by Departments* and the Ministry of Health's own internal procurement policies. The Court held that several members of the evaluation panel were biased because they had prior knowledge about the organisations submitting proposals and had a current or previous working relationship with them.

4.22 This means that public entities need to consider very carefully the standards they set for managing conflicts of interest and how they then meet those standards. We note that this case is currently subject to appeal.

4.23 It is necessary to point to a specific connection between the person's other interest and a particular matter or decision coming before the public entity. Public entities need to take responsibility for considering the options available and working with the person who has disclosed the conflict of interest. Wise heads, careful consideration, and sound judgement are necessary to better manage these situations. It might be necessary to seek appropriate specialist advice. However, the onus is on the person to comply with the appropriate course of action agreed.

4.24 With Ashburton District Council, we found that a councillor did not take the advice that Council staff obtained for him. It is possible that the councillor exposed the Council decision to some level of risk. However, the decision to participate in the decision-making process was a choice that was open to him.

4.25 In situations where a governor refuses to acknowledge or accept that they might have a conflict of interest, the chairperson has an important role to play in managing the situation.

4.26 Potential conflicts of interest were one of the issues we examined in our inquiry into two property investments, at Luggate and Jacks Point, by Delta Utility Services Limited (Delta), a council-controlled trading organisation of Dunedin City Council (the Council).

4.27 We found no evidence of impropriety or of poorly managed conflicts of interest for either investment. However, we did identify some breaches of the Local Government Act 2002 and the Companies Act 1993, and instances of Delta using alternative business structures to avoid public accountability.

5 Problem Gambling Foundation of New Zealand v Attorney General [2015] NZHC 1701.

4.28 The extent of the interests and involvement of one of Delta's directors in Jacks Point and how these interests and involvement were managed gave us cause to pause and think. These interests also concerned the members of the public who contacted our Office. In public office, having multiple roles and interests requires careful management. People with such interests need to behave with the utmost integrity and transparency to avoid real or perceived conflicts and risks to the public entities they serve.

4.29 Although Delta's overall management and disclosure of conflicts of interest were largely adequate, we identified some instances where there should have been earlier or fuller disclosure for better transparency. There was one instance where the director's involvement in both sides of a venture would have been problematic if the venture had proceeded.

4.30 Conflicts of interest also need to be managed so that they do not stop someone from doing their job. During our inquiry into how Queenstown Lakes District Council managed the chief executive's interest in a proposed special housing area, we noted that the conflict affected the chief executive's ability to meet his responsibilities. He was not able to advise the Council about special housing areas nor provide leadership to Council staff in this matter.

5 Being accountable to the people you serve

5.1 Citizens hold their elected representatives accountable for their decisions and actions. These representatives, in turn, hold accountable those who implement their decisions. As noted in Part 1, public accountability enables trust in government and is vital to maintaining a healthy democracy.

5.2 In our view, public entities should consider the following elements that support effective accountability:

- meeting the public's expectations;
- meeting public reporting obligations;
- improving financial and service performance reporting;
- reporting in a timely manner;
- being open to scrutiny; and
- handling complaints effectively.

Meeting the public's expectations

5.3 In New Zealand, there are quite rightly high expectations of the public sector. These expectations are the foundation of good accountability. In general, good accountability comes from being guided by principles that support trust between citizens and the public sector:

- **Openness** – being transparent.
- **Value for money** – using resources effectively, economically, and without waste while having due regard for costs and benefits, as well as the contribution to outcomes.
- **Lawfulness** – acting within the law and meeting legal obligations.
- **Fairness** – meeting a general public law obligation to act fairly and reasonably.
- **Integrity** – managing public resources with the utmost integrity.

5.4 The quality of information that governing bodies use to make decisions, and to inform their public reporting about their performance, are also important features in supporting effective accountability.

Meeting public reporting obligations

5.5 Public entities need to provide information about their performance so that elected representatives, stakeholders, and the public can understand what a public entity is trying to achieve, how it has used public resources, and what it has achieved.

5.6 The information needs to give a complete and accurate account of the use the entity has put public funds to, including funds passed on to others for particular purposes.

5.7 Public entities should report information in a form that their stakeholders, including the public, can readily access, and is easy to understand and use.

5.8 Our role in providing independent assurance over the financial and performance information in public reports helps Parliament and the public to “close the accountability loop”, using these reports to hold public entities to account.

Improving financial and service performance reporting

Financial reporting

5.9 Most public entities are required to produce general purpose financial reports. Usually, legislation requires that the information in general purpose financial reports must comply with generally accepted accounting practice (also known as GAAP), or, for certain small public entities, non-GAAP standards.[6]

5.10 GAAP and non-GAAP standards are the overall body of accounting standards and other guidance issued by the External Reporting Board. The standards set out how an entity should prepare financial reports. GAAP and non-GAAP standards are a set of objective principles that are not subject to the individual preferences of the person who prepares the reports.

5.11 Our report on improving financial reporting in the public sector notes positive changes made to the accounting standards framework during the last 6-7 years. The changes mean that there is now a tailored approach to financial reporting for the public sector and a foundation for better reporting in the future.

5.12 The positive changes include establishing a single, independent accounting standard-setting body, the External Reporting Board, and adopting a new accounting standards framework for all reporting entities.

5.13 The new accounting standards framework is designed so that financial reports will better meet the needs of users. It separates accounting standards for public benefit entities from entities that have a focus on achieving a commercial return, and uses tiers to reflect the different size and nature of reporting entities in New Zealand. We encourage public entities to take full advantage of any financial reporting concessions that are available in the new tiered structure.

5.14 We also encourage public entities to take advantage of the flexibility within the new requirements by focusing on users’ information needs and reporting what matters most.

6 See section 18 of the Financial Reporting Act 2013 for reference to non-GAAP standards.

5.15 The External Reporting Board also has an important ongoing role in helping to resolve some of the more challenging areas in general purpose financial reporting.

Service performance reporting

5.16 Service performance reports are expected to disclose what the entity set out to achieve and what it actually achieved. As well as supporting its accountability, an entity's service performance reporting should be focused on performance improvements and based on the information necessary to run its business. Entities can be truly accountable only if they are transparent about both their financial and service performance and the relationship between the two.

5.17 For more than 25 years, there have been statutory requirements for a range of public entities to report on their service performance. We have long been active in promoting improvements in how public entities fulfil these requirements and we have seen improvements.

5.18 We have seen some evidence of stronger performance frameworks that bodes well for improved reporting in the future.

5.19 However, there is still a fair way to go, particularly in reporting that enables users to understand an entity's longer-term strategic objectives and how well it has performed against them.

5.20 From our audits of central government and local government entities' service performance reports in 2014/15, the aspects that still require further focus and improvement by public entities are:

- striving for more relevant performance measures that better reflect the real performance of the entity;
- better understanding of the systems, processes, and controls required to support new measures; and
- better internal verification processes and assurance reviews for performance reports, particularly the information from third parties.

5.21 The 2013 amendments to central government public sector legislation included changes to:

- require more meaningful reporting on what entities intend to achieve and what they do achieve; and
- lift the strategic focus of statements of intent to drive a clearer focus on results and outcomes.

5.22 In part, the changes were designed to bring financial (including more flexible funding arrangements) and service performance reporting closer together. Based on our 2014/15 annual audit work, it appears that many entities have yet to fully consider these amendments.

5.23 We found that some entities used their management commentary in the annual report as a substitute for reporting against formal performance measures. We do not consider this appropriate and our auditors will be discussing this with entities during 2015/16.

Don't be late – timely reporting is essential for good accountability

5.24 If public entities' reporting is not timely, the information they provide is less relevant and proper accountability is more difficult to achieve.

5.25 In our report on the timeliness of public entities' reporting in 2013/14, we found that most public entities (80%) met their reporting obligations. The entities whose audit reports were issued late or had not been issued were mostly subsidiaries of public entities and small public entities.

5.26 Some entities can and need to do better. Some are struggling, which could be a result of limited internal capability to meet the requirements or questions about the value of, and priority given to, such reporting. Not surprisingly, very small public entities struggle the most.

5.27 The recent legislative changes and changes to accounting standards mentioned above are expected to help improve the quality and timeliness of reporting by public entities. Some subsidiaries no longer need to separately report, and some other entities have had their reporting obligations simplified.

5.28 However, the balance between the costs of compliance (including audits) and the benefits to the users of those audit reports might still not be right. In our view, there are opportunities for further changes to the public accountability requirements, particularly for very small entities such as cemeteries and reserve boards.

Being open to scrutiny

5.29 High-performing organisations look for opportunities to learn and improve. They welcome feedback, see complaints as opportunities to learn, and understand the roles that internal and external audits play in providing independent assurance and advice over their activities and reporting.

Handling complaints effectively

5.30 An important aspect of effective accountability is the ease with which members of the public can make complaints if they are dissatisfied with a service they have received from a public entity, or if they want to resolve a matter of importance to them. Public entities are responsible for dealing with the complaints they receive.

5.31 In my view, making a complaint or raising a concern with a public entity can be difficult. If a person exhausts all of the entity's own complaint and review processes and remains dissatisfied, it can be difficult to work out where to go. One reason for this is that little or no easily accessible information explains the subsequent options.

5.32 New Zealand's arrangements for making complaints and raising concerns are a complex web of accountability functions and agencies. In my view, these arrangements are not as well connected as they could be. Inquiry agencies work under different pieces of legislation and, because they need to protect people's privacy, there can be challenges to regularly working together.

5.33 We consider that improving connections between inquiry agencies is likely to improve the quality and timeliness of services and improve how public services are used. I encourage all inquiry agencies to continue to collaborate and look for new ways to improve their connections with each other. In the end, improving these connections will make it easier for people to get the right help soon enough.

Emerging trends presenting opportunities and challenges

6

Governance in the public sector is increasingly complex

6.1 The changing public sector landscape, fiscal pressures, demographic changes, and new ways of working all demand effective governance. Cross-agency and cross-sector developments, public private partnerships, and increasing third-party service delivery are all driving changes to governance and accountability arrangements in central and local government.

Co-governance and network governance

6.2 As well as governance at the entity, programme, and project levels, there is an increasing focus on the need for governance at the sector or network level. Examples of this include changes in governance arrangements in the social sector with the establishment of the Social Sector Board, the Vulnerable Children's Board, and the Joint Venture Board to oversee the social sector trials. We have also seen an increase in the number of co-governance arrangements in the environment sector.

6.3 Our work in the environment sector found that there are new and different governance arrangements being established, with a range of purposes. We identified some principles to consider when setting up and maintaining effective co-governance and co-management arrangements. The principles are:

- build and maintain a shared understanding of what everyone is trying to achieve;
- build the structures, processes, and understanding about how people will work together;
- involve people who have the right experience and capacity;
- be accountable and transparent about performance, achievements, and challenges; and
- plan for financial sustainability and adapt as circumstances change.

6.4 During our visits with public entities, we often hear about examples of collaboration that are working well. One such example is where Canterbury District Health Board and West Coast District Health Board have set up an alliancing arrangement. The two organisations have come together with a shared vision and put people at the centre of it. As a result, there is a strong service-delivery focus to how the district health boards work. There should be a direct benefit to the West Coast residents who should now receive better access to health services in their own community.

6.5 We have also found examples where collaboration has not been as effective. In our audit of the Whānau Ora programme, we found that the relationships between the agencies involved had not fully matured at the time of our audit. This was a barrier to achieving the full potential of Whānau Ora.

6.6 There is an increasing focus on collaboration between government agencies and between local and central government, for example in relation to Canterbury's earthquake recovery, and tackling housing and transport issues in Auckland. Increasingly, this collaboration is seen as the most effective way to solve complex problems and to ensure that entities are using public assets effectively and efficiently.

6.7 This could lead to different organisational models or structures. There is a need for governance and accountability systems to keep up with the changes arising from this collaboration. Cross-sector governing bodies need to ensure that they remain focused throughout the delivery phases of work programmes that implement strategy. These governing bodies play an important role in unblocking systemic obstacles to delivery, such as the challenges organisations face in sharing data and information due to privacy or security concerns.

6.8 But working collaboratively is not "all or nothing". Agencies still need to deliver their core business. Collaboration should be for a purpose and agencies should be deliberate about identifying those areas or topics or initiatives where collaboration is necessary, and those where they just need to get on with their own job. This is a balancing act and prioritisation is required.

Adapting governance to support changing needs

6.9 Governance models need to be adapted for the specific goals and outcomes required for different situations; one size does not fit all.

6.10 Inland Revenue plans to update the governance roles and responsibilities for the different stages of its business transformation programme, and also to support board member training. Both of these are elements of good practice.

6.11 Te Wānanga O Raukawa provides an interesting perspective on how entities can combine the requirements of the Crown with ensuring that the role of the iwi is not lost. At the Wānanga, accountability to its founding iwi is the primary concern for the Tumuaki (chief executive) and she is supported by Te Mana Whakahaere (the Council). The role of the founding iwi in the Wānanga's governance and accountability arrangements is seen as non-negotiable. This is an example of good relationships being critical to good governance.

6.12 The quality of governance in local government is coming under increasing scrutiny. Local Government New Zealand has a programme on leadership and governance. We consider that improved governance will aid better decision-making and outcomes for communities. It should also assist in enabling better accountability.

6.13 The nature and style of governance in local government is not static. It has been continually tested through structures such as the introduction of local boards in Auckland. Similarly, events have tested the strength of existing governance arrangements.

From governance to stewardship

6.14 As highlighted in Part 3, departmental chief executives have specific stewardship responsibilities for their departments. There are now also system-wide expectations for chief executives to work collaboratively with other agencies to improve service delivery and achieve outcomes.

6.15 Stewardship is not a new concept. However, as the legislative changes become more established and better understood, we expect new approaches to be taken to governing public entities and shared programmes of work that span organisational boundaries.

Accountability trends – integrated reporting

6.16 The emergence of integrated reporting provides an opportunity for agencies to better tell their whole performance story, with a focus on reporting what matters most for the individual entity and its stakeholders.

6.17 This is a broader story than general purpose financial reports currently provide. Integrated reporting aims to provide users with more information about the value and long-term sustainability of the entity.

6.18 An integrated report provides insight about the use of resources (such as funding and human resources), the external environment affecting the entity, and how important relationships with stakeholders are maintained.

Accountability trends – consultation and social media immediacy

6.19 Social media provides a channel for citizens to talk about and to public entities. Its widespread use is increasing the interaction between citizens and many public entities. It enables public entities to consult with the public in new and faster ways than traditional public consultation exercises.

6.20 Many public entities are still working out how best to take advantage of social media platforms, considering how they can best listen to feedback, and use it to improve the services they deliver.

6.21 Entities need to think about how they can best engage with their communities and stakeholders in a way that is open, able to be resourced, and that helps to improve how services are delivered.

6.22 "Bespoke" consultation processes are also emerging, sometimes in response to legislative requirements. For example, under the Local Government Act 2002, local authorities are required to have significance and engagement policies in place that outline how and when communities can expect to be asked about or involved in decisions. In our view, this consultation needs to be supported by robust processes to ensure procedural fairness. The consultation also benefits from local authorities applying sound judgement and using professional advice.

Accountability trends – where next for financial reporting?

6.23 In our report, *Improving financial reporting in the public sector*, we highlighted the main challenges facing standard-setters, preparers, and auditors to ensure that general purpose financial reports are relevant and useful. These include continuing to focus on users' needs; helping users understand the performance story; preparers focusing on reporting what matters most; reducing the number of reporting entities; and keeping pace with technology.

6.24 These trends will affect the nature of our audit and assurance work. For example, there is likely to be increased demand for real-time assurance for programmes and projects. We will need to continue to work closely with standard-setters and public entities to ensure that our work adapts appropriately to changes in how information is reported.

Appendix 1
Our reports relevant to governance and accountability

- *Public sector accountability through raising concerns* (March 2016)
- *Improving financial reporting in the public sector* (February 2016)
- *Principles for effectively co-governing natural resources* (February 2016)
- *Governance and accountability for three Christchurch rebuild projects* (December 2015)
- *Earthquake Commission: Managing the Canterbury Home Repair Programme – follow-up audit* (December 2015)
- *Reviewing aspects of the Auckland Manukau Eastern Transport Initiative* (October 2015)
- *Governance and accountability of council-controlled organisations* (October 2015)
- *Inquiry into Health Benefits Limited* (October 2015)
- *Effectiveness of governance arrangements in the arts, culture, and heritage sector* (May 2015)
- *Being accountable to the public: Timeliness of reporting by public entities* (May 2015)
- *Whānau Ora: The first four years* (May 2015)
- *Health Promotion Agency – Katherine Rich – possible conflicts of interest* (May 2015)
- *Inland Revenue Department: Governance of the Business Transformation programme* (April 2015)
- *Education for Māori: Relationships between schools and whānau* (February 2015)
- *Making the most of audit committees in the public sector* (November 2014)
- *Ashburton District Council: Allegations of conflicts of interest affecting decisions on a second bridge* (October 2014)
- *Effectiveness of arrangements for co-ordinating civilian maritime patrols – follow-up report* (July 2014)
- *Inquiry into property investments by Delta Utility Services Limited at Luggate and Jacks Point* (March 2014)
- *Maintaining a future focus in governing Crown-owned companies* (February 2014)
- *Summary: Inquiry into the Mangawhai community wastewater scheme* (November 2013)
- *Inquiry into aspects of ACC's Board-level governance* (August 2012)
- *Guardians of New Zealand Superannuation: Governance and management of the New Zealand Superannuation Fund* (May 2008)
- *Managing conflicts of interest: Guidance for public entities* (June 2007).

Appendix 2
Useful links

- Lessons about managing change and setting up shared services arrangements from our report on Central Agencies Shared Services (oag.govt.nz/2014/cass/appendix2.htm)
- Lessons for public entities dealing with significant change agendas from our inquiry into Health Benefits Limited (oag.govt.nz/2015/inquiry-hbl/part6.htm)
- Some challenges and questions to consider when governing programmes from our report on Inland Revenue's business transformation programme (oag.govt.nz/2015/ird-business-transformation/part5.htm)
- Conflicts of interest guidelines (2007) (oag.govt.nz/2007/conflicts-public-entities)
- Board self-assessment tool from our report on governance in the arts, culture, and heritage sector (oag.govt.nz/2015/arts-governance/assessing-performance/assessing-performance-pdf/view)
- List of questions boards should ask – audit committee resources (oag.govt.nz/our-work/audit-committees/what-works/powerful-questions)
- Audit committee resources (oag.govt.nz/our-work/audit-committees)
- The Institute of Directors in New Zealand (Inc) has a range of governance tools and resources, including governance practice guides (for example, Conflicts of Interest) available at iod.org.nz.

Publications by the Auditor-General

Other publications issued by the Auditor-General recently have been:

- Local government: Results of the 2014/15 audits
- Department of Conservation: Prioritising and partnering to manage biodiversity – Progress in responding to the Auditor-General's recommendations
- Public sector accountability through raising concerns
- A review of public sector financial assets and how they are managed and governed
- Improving financial reporting in the public sector
- Principles for effectively co-governing natural resources
- Governance and accountability for three Christchurch rebuild projects
- Central government: Results of the 2014/15 audits
- Delivering scheduled services to patients – Progress in responding to the Auditor-General's recommendation
- Matters arising from the 2015-25 local authority long-term plans
- Earthquake Commission: Managing the Canterbury Home Repair Programme – follow-up audit
- Ministry for Primary Industries: Preparing for and responding to biosecurity incursions – follow-up audit
- Governance and accountability of council-controlled organisations
- Queenstown Lakes District Council: Managing a conflict of interest in a proposed special housing area
- Reviewing aspects of the Auckland Manukau Eastern Transport Initiative

Website

All these reports, and many of our earlier reports, are available in HTML and PDF format on our website – www.oag.govt.nz.

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