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Improving value through better Crown entity monitoring

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Contents

Auditor-General's overview

E ngā mana, e ngā reo, e ngā karangarangatanga maha o te motu, tēnā koutou.

Crown entities carry out a wide range of important public services and functions. These services include education, health care, accident and earthquake insurance, public broadcasting, and construction and maintenance of national infrastructure such as roads. In 2020/21, Crown entities were responsible for 39% of central government expenditure, 46% of central government assets, and 74% of the central government workforce.

Crown entities are set up to operate under varying degrees of government influence. The Crown Entities Act 2004 specifies how much control Ministers have over the Crown entities they are responsible for. In general, Ministers have less day-to-day influence over a Crown entity than they do over a government department. However, Ministers are still accountable to Parliament and the public for the performance of the Crown entities that they are responsible for.

A governance board is usually responsible for the governance and oversight of a Crown entity. Ministers' responsibilities include making or recommending appointments to the Crown entity board and participating in setting and monitoring the Crown entity's strategic direction and targets. Monitoring departments support Ministers to carry out their duties and functions in relation to Crown entities.

The network of roles, responsibilities, and relationships between Ministers, monitoring departments, Crown entity governing boards, and Crown entities is complex. This report refers to this network as the Crown entity monitoring system.

There are inherent tensions in the Crown entity monitoring system. For example:
- Monitoring departments and Crown entities need to work closely to develop monitoring frameworks and common expectations. However, a monitoring department must retain enough independence to take an objective view of Crown entity performance.
- The board has primary oversight and accountability for the Crown entity's performance. However, monitoring departments are expected to form a judgement on the performance of a Crown entity and might need to challenge its board.
- To carry out their role effectively, monitoring departments must provide good information, analysis, and advice to Ministers about the effectiveness, efficiency, and performance of any Crown entities that they monitor. At the same time, monitoring departments must respect the arm's-length relationship between the responsible Minister and the Crown entity, and the monitoring, governance, and oversight responsibilities of the Crown entity's governance board.

These tensions are not always easy to manage.

Monitoring arrangements work best when responsible Ministers, Crown entities, and monitoring departments are clear about their roles and responsibilities. There also needs to be effective communication, engagement, and a shared understanding between all of the parties about what good performance looks like.

I have heard a range of concerns about the quality of monitoring that takes place. In recent years, there have been well-publicised performance issues in some Crown entities. I decided to carry out an audit to assess how effective monitoring arrangements are and identify opportunities to improve the Crown entity monitoring system.

In my view, a strong monitoring system will support improved performance of Crown entities. This will help ensure that the critical services Crown entities provide consistently meet the expectations of Parliament and the public.

What we found

In 2009, we carried out an audit of how government departments monitor Crown entities. From that audit, we made recommendations for monitoring departments to:

- better understand their roles and responsibilities;
- improve the timeliness and content of each Crown entity's performance information;
- better plan for the board appointment process; and
- work to improve the preparation of each Crown entity's Statement of Intent.

Since our 2009 audit, some aspects of monitoring have improved. There is now good guidance available, a strong community of practice, and monitoring agencies serve Ministers and Crown entities well in facilitating key processes.

However, some issues remain. The extent to which monitoring adds significant value to understanding Crown entity performance is still unclear.

Monitoring frameworks still tend to focus on key milestones or the timing of monitoring activity. They often lack information about roles and responsibilities and fail to set clear expectations about how performance issues will be dealt with. In most cases, Crown entities have not been consulted in the development of these monitoring frameworks. As a result, monitoring frameworks are not always appropriate to the scope, scale, or level of risk associated with the Crown entity being monitored.

Monitoring departments effectively support Ministers to carry out some of their responsibilities, and Crown entities view the support they receive for parliamentary processes and budget bids as positive. However, other monitoring practices could be improved. Ministers, Crown entities, and monitoring departments noted that monitoring departments' feedback on accountability documents lacks depth. As a result, opportunities to influence the strategic

direction of Crown entities, make connections across the sector, and support Crown entities to identify and resolve problems are being missed.

Monitoring reports to Ministers do not generally include enough information to enable good analysis of performance. In my view, there is not enough information in these reports about the risks that Crown entities face, how they are being addressed, and what they might mean for future performance. Although there are a range of levers that Ministers can use to address poor performance, some monitoring departments we spoke to felt that these levers are insufficient or ineffective.

In my view, there is a risk that monitoring has become a compliance exercise generating little value. This is not what the Crown entity monitoring system was set up to achieve.

My staff did observe a genuine willingness to improve the Crown entity monitoring system and draw more value from the monitoring being carried out. I have recommended that monitoring departments and Crown entities continue to work together to improve their monitoring frameworks. I have also identified minimum standards that, in my view, improved monitoring frameworks should meet.

Te Kawa Mataaho Public Service Commission administers the Crown Entities Act 2004. It is well placed to assume a system leadership role for Crown entity monitoring. I have recommended that Te Kawa Mataaho consider how it can play a stronger role in supporting monitoring departments and Crown entities to create further improvements in the Crown entity monitoring system.

Te Kawa Mataaho told us it has several initiatives under way that will address some of the challenges identified. I am encouraged by this and will maintain an interest in the progress of that work.

Improving the Crown entity monitoring system will be challenging. However, when monitoring is done well, it can help Crown entities deliver better outcomes for New Zealanders. I thank the many people who contributed to this audit and took the time to talk with my staff, including Ministers and staff from Crown entities and monitoring departments.

Nāku noa, nā

John Ryan
Controller and Auditor-General

22 June 2022

Our recommendations

We recommend that monitoring departments and Crown entities:

1. work together to clearly document the monitoring framework they will use to support their monitoring arrangements. Monitoring frameworks should at a minimum:
   - set out the purpose and objectives of the monitoring;
   - set out the respective roles and responsibilities for the monitoring arrangements;
   - describe the information the monitoring department needs to monitor effectively. This should include the outcomes the Crown entity is trying to achieve, the information that measures a Crown entity's progress, any gaps the Crown entity should address, and an understanding of what "good" performance looks like;
   - set out how performance issues will be managed. This should include what happens if a Crown entity does not meet performance expectations and when and how monitoring departments should advise a responsible Minister about how a board is managing performance;
   - be developed in consultation with the relevant Crown entities, and take into account an entity's specific circumstances, functions, and activities; and
   - be supported by the responsible Minister;

2. ensure that there is meaningful engagement in the development of Crown entities' accountability documents. This should include engagement on the operating context, challenges, goals, expectations, and performance measures; and

3. share knowledge and seek to understand each other's operating context. This should include monitoring departments:
   - giving feedback to Crown entities about their performance in the context of the relevant sector and communicating key events that might affect relevant Crown entities; and
   - briefing other teams in their department about the challenges facing the Crown entities that they monitor to identify appropriate support where needed.

We recommend that monitoring departments:

4. improve the quality of performance reporting about Crown entities, ensuring that reports to Ministers provide an independent view on:

    •   a Crown entity's strategic and operational performance;

    •   how the Crown entity is managing risk;

    •   the potential impact of risks to both performance and outcomes; and

    •   the results of regular board evaluations in a timely way.

We recommend that Te Kawa Mataaho Public Service Commission:

5. continue to strengthen its support for, and oversight of, the Crown entity monitoring system. In particular, how it could:

    •   assist monitoring departments and Crown entities in creating and applying effective monitoring frameworks;

    •   promote good practice in monitoring departments and Crown entities, including supporting communities of practice and professional development for monitoring practitioners;

    •   set expectations with chief executives of monitoring departments about the priority that needs to be given to effective Crown entity monitoring;

    •   regularly assess the effectiveness of monitoring carried out by monitoring departments and hold departmental chief executives to account for meeting these expectations;

    •   support effective Crown entity governance, such as providing advice for succession planning, talent management, and good practice tools; and

    •   where monitoring is ineffective, provide additional advice and support to help monitoring departments and Crown entities improve.

6. We recommend monitoring departments, Crown entities, and responsible Ministers regularly review monitoring arrangements to ensure that they remain fit for purpose.

1

Introduction

1.1   In this Part, we describe:
- why we did our audit;
- what we looked at;
- what we did not look at;
- how we carried out our work; and
- the structure of this report.

1.2   There are more than 2700 organisations in the public sector that sit outside central government. Many of these are Crown entities.[1] Crown entities are established by statute and carry out important public services or functions. They are funded in various ways but often receive some Crown funding.

1.3   Crown entities deliver significant public services. In 2020/21, they were responsible for 39% of central government expenditure, 46% of central government assets, and 74% of the central government workforce.

1.4   All Crown entities are set up to be at "arm's length" from government.[2] We looked at statutory Crown entities.[3] There are three types of statutory Crown entities with different degrees of autonomy:
- **Crown agents** have the closest relationship to government. Responsible Ministers can direct Crown agents to give effect to government policy that relates to their functions and objectives. This includes core public-facing service delivery.
- **Autonomous Crown entities** must have regard to policy that relates to their functions and objectives if directed by their responsible Minister.
- **Independent Crown entities** cannot be directed by their responsible Minister on matters of government policy unless its statute specifically provides for it.

1.5   In this report, we use the term "Crown entity" to mean statutory Crown entities.

1.6   The Crown Entities Act 2004 provides the basis for establishing, governing, and operating all Crown entities. Each Crown entity has a board (or equivalent)[4] and a Minister responsible for the performance of a Crown entity (responsible Minister) – both have responsibilities under the Act. The responsible Minister's role is to oversee and manage the Crown's interests in each Crown entity.

1.7   A "monitoring department" is a government department that supports responsible Ministers to carry out their functions and duties in relation to a Crown

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1   There are five categories of Crown entities. These are statutory Crown entities, Crown entity companies, companies listed in Schedule 4 and 4A of the Public Finance Act 1989, tertiary education institutions, and schools.

2   Arm's length means the Crown entity operates with less influence from government.

3   Statutory Crown entities are defined in Schedule 1 of the Crown Entities Act 2004.

4   Some Crown entities have Commissioners that fulfil both the governance and executive functions of a Crown entity. Examples include the Productivity Commission, the Commerce Commission, and the Privacy Commission.

entity, including ensuring that the Crown entity meets its statutory obligations. Monitoring departments normally monitor multiple Crown entities in the same sector. For example, the Ministry of Transport monitors Maritime New Zealand, Waka Kotahi New Zealand Transport Agency, the Civil Aviation Authority, and the Transport Accident Investigation Commission.

1.8   In this report, we use the term "Crown entity monitoring system" to describe the network of roles, responsibilities, and relationships between responsible Ministers, monitoring departments, Crown entity governing boards, and Crown entities.

1.9   We refer to the arrangements between a responsible Minister, a monitoring department, and an individual Crown entity as "monitoring arrangements".

Why we carried out this audit

1.10   Concerns are sometimes raised about the quality of Crown entity monitoring. In recent years, some Crown entities have had well-publicised performance issues. We wanted to assess the effectiveness of Crown entity monitoring arrangements and identify opportunities where monitoring could be improved.

1.11   Specifically, we wanted to:
- understand the challenges and opportunities experienced across the public sector of current monitoring arrangements;
- better understand the role of the Treasury and Te Kawa Mataaho Public Service Commission (Te Kawa Mataaho) in providing leadership for monitoring arrangements; and
- observe whether the Crown entity monitoring system is effective.

1.12   In 2009, four years after the Crown Entities Act came into effect, we carried out an audit in which we assessed how well three monitoring departments were supporting responsible Ministers in carrying out monitoring activities.[5] We also wanted to provide assurance that these monitoring departments had effective mechanisms to support responsible Ministers with their responsibilities for Crown entities, including their specific functions under the Crown Entities Act.

1.13   Our 2009 report highlighted several areas that those three monitoring departments needed to improve. This included clarifying roles and responsibilities, making better use of information about issues and risks to inform their monitoring work, and providing relevant, timely advice to Ministers about each Crown entity's statement of intent and its financial and non-financial performance.

1.14   In carrying out this audit, we took a broader view of the Crown entity monitoring system. We were interested in whether we could identify improvements to monitoring arrangements since our 2009 report.

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5   Office of the Auditor-General (2009), *How government departments monitor Crown entities* at oag.parliament.nz.   **9**

What we looked at

1.15   We wanted to understand whether the monitoring arrangements for statutory Crown entities are effective. Specifically, we looked at whether:

- monitoring departments have a comprehensive framework for monitoring statutory Crown entities;

- the monitoring activity is appropriate and proportionate to the Crown entity being monitored; and

- monitoring departments use the information they get from monitoring effectively.

1.16   Our audit looked at statutory Crown entities. We based our assessment on *It Takes Three: Operating Expectations Framework for Statutory Crown Entities*,[6] which is the main guidance that monitoring departments use. We discuss this guidance in more detail in paragraphs 2.23-2.25.

What we did not look at

1.17   We did not look at state-owned enterprises, Crown entity companies or subsidiaries, district health boards, tertiary education institutions, school boards of trustees, or local government organisations. However, some of our findings might apply to them.

1.18   We wanted to develop system-level observations and recommendations. Therefore, we did not assess:

- how any single monitoring department or Crown entity was performing; or

- the effectiveness of any individual Crown entity board.

1.19   We did not look specifically at the quality of Crown entities' performance frameworks or accountability documents.

How we carried out this work

1.20   We looked at nine different monitoring arrangements between Crown entities and their monitoring departments. These monitoring arrangements involved five monitoring departments and nine Crown entities. For each arrangement, we spoke with the Crown entity and its monitoring department. These organisations ranged in size and role and covered several sectors.

1.21   We also spoke with the Treasury and Te Kawa Mataaho because of their roles supporting the Crown entity monitoring system.

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6   Te Kawa Mataaho Public Service Commission (2014), *It Takes Three: Operating Expectations Framework for Statutory Crown Entities*, at publicservice.govt.nz.

1.22   We analysed documents and interviewed people, including:

- some responsible Ministers;
- chairpersons of the governance boards of Crown entities;
- chief executives and senior managers of Crown entities;
- those responsible for monitoring teams within monitoring departments; and
- those who carry out day-to-day monitoring within monitoring departments and Crown entities.

1.23   We also surveyed the board chairpersons and chief executives of 58 Crown entities[7] and the senior managers of monitoring teams in 12 monitoring departments. Of those organisations, 67% of Crown entities and 100% of monitoring departments responded to our survey. The responses gave us a wide view of the monitoring experiences and practices of Crown entities and monitoring departments. The findings from the survey and our more detailed review of the monitoring arrangements were consistent.

1.24   We looked at several Performance Improvement Framework reviews, which Te Kawa Mataaho carry out. Performance Improvement Framework reviews inquire into the capability and delivery of government departments and what the department needs to improve in the medium term. They look at the monitoring functions of departments if it is a substantial part of the department's operations.

Structure of this report

1.25   In Part 2, we consider the framework for Crown entity monitoring.

1.26   In Part 3, we discuss Crown entity monitoring practices and activities.

1.27   In Part 4, we discuss how well Crown entity performance information is understood and used.

1.28   In Part 5, we discuss the challenges we saw and identify opportunities to improve Crown entity monitoring arrangements.

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7   Our survey excluded some statutory Crown entities, including the New Zealand Walking Access Commission and the New Zealand Antarctic Institute. The departments that monitor these entities, the Ministry for Primary Industries and the Ministry of Foreign Affairs and Trade respectively, were excluded because they do not monitor any other Crown entities. We also excluded district health boards because we considered that the high number of them could have a disproportionate effect on the survey results.

2

The framework for monitoring

2.1 In this Part, we look at:
- the overall framework for Crown entity monitoring;
- the guidance available for Crown entity monitoring; and
- how monitoring departments develop monitoring frameworks.

2.2 We expected that:
- monitoring departments would use a clear framework for monitoring that is consistent with the statutory requirements and good practice guidance;
- monitoring frameworks would set out roles, responsibilities, and expectations;
- monitoring departments would develop frameworks in consultation with the Crown entities they monitor; and
- the monitoring framework would be appropriate and proportionate to the circumstances of the Crown entity being monitored.

Summary of findings

2.3 The main guidance published by Te Kawa Mataaho for monitoring Crown entities has clear expectations for responsible Ministers, Crown entities, and monitoring departments. Other guidance is also available and a group of officials meet monthly to share and develop good practice.

2.4 The guidance provides a strong basis for monitoring departments and Crown entities to create effective monitoring frameworks.

2.5 However, we found that the monitoring frameworks themselves need improvement. We reviewed frameworks used in nine monitoring arrangements. None of these frameworks:
- set out a full, clear, and documented understanding of the role and responsibilities that monitoring departments have for each Crown entity;
- reflected an understanding of the Crown entity's operations and context to help define monitoring expectations or activities; or
- were developed in consultation with the Crown entities being monitored to secure their engagement and buy-in to monitoring and to improve relationships.

2.6 We recommend that monitoring departments work with the Crown entities they monitor to review the monitoring frameworks. This will help monitoring departments better understand the role and context of the Crown entities they monitor and the challenges they face. It should also lead to more monitoring arrangements that are fit-for-purpose and help to establish a common understanding of each other's roles and responsibilities.

The Crown Entities Act sets out the overall monitoring framework

2.7 Crown entities are established by statute, which typically defines a Crown entity's functions, objectives, and governance arrangements.

2.8 The Crown Entities Act 2004 sets out the accountability relationships between Crown entities, their boards, and responsible Ministers. Figure 1 shows the relationship between the different groups in the Crown entity monitoring system. Most Crown entity monitoring arrangements follow the accountability and assurance relationships described in Figure 1.[8]

Figure 1
The accountability and assurance relationships in a Crown entity monitoring arrangement
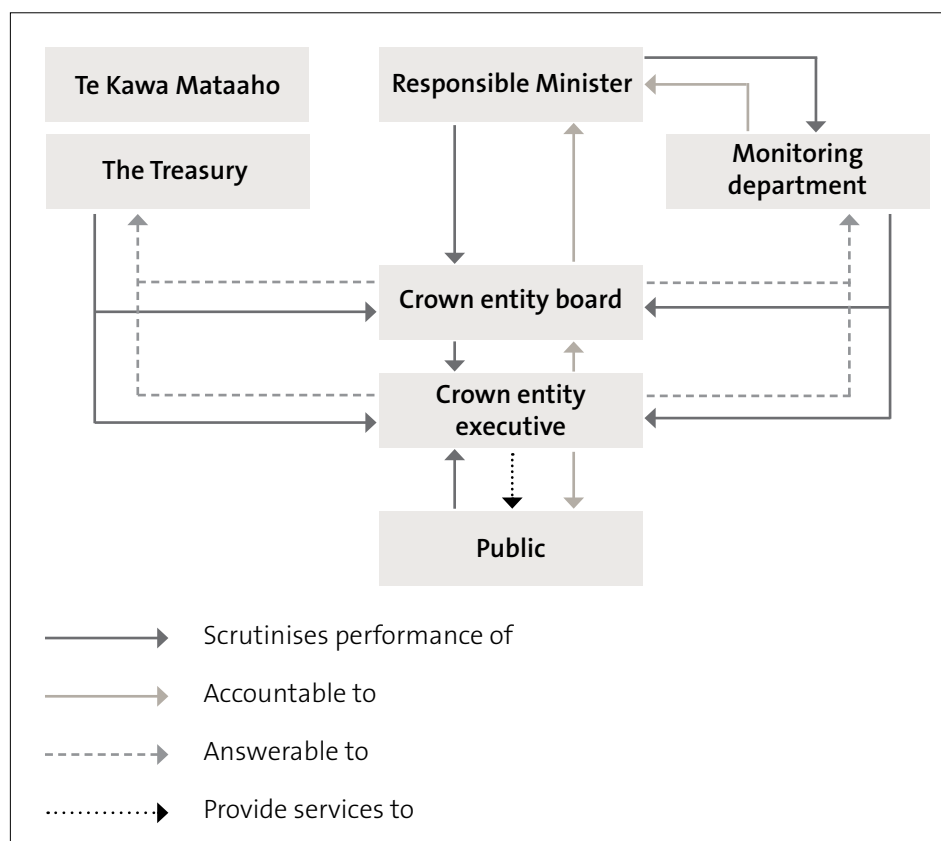
Source: Te Kawa Mataaho Public Service Commission.

2.9 The Crown Entities Act defines the role, accountabilities, and responsibilities of the Crown entity board, responsible Ministers, and monitoring department.

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8 Some Crown entities have Commissioners that fulfil both the governance and executive functions of a Crown entity. Examples include the Productivity Commission, the Commerce Commission, and the Privacy Commission.

Crown entity board members must carry out their duties in a way that is consistent with their statutory obligations. A mutual understanding of each other's role is necessary to ensure that Crown entities, responsible Ministers, and monitoring departments work together effectively.

Each Crown entity has a responsible Minister

2.10   The responsible Minister's role is to oversee and manage the Crown's interests in the relevant Crown entity. The responsible Minister has statutory responsibilities such as:

- appointing and removing Crown entity board members;

- giving the Crown entity direction;

- reviewing the operations and performance of the Crown entity;

- seeking information from the Crown entity;

- participating in setting the Crown entity's strategic direction and performance expectations; and

- monitoring the Crown entity's performance.

2.11   Parliament also scrutinises Crown entity performance. This is usually done through select committees and the annual review process where the Crown entity board, executive, or responsible Minister is questioned.

Crown entity boards are the entity's primary monitor

2.12   A Crown entity board governs its Crown entity. The board's role is to ensure that the Crown entity's executive acts consistently with the entity's objectives, functions, and current accountability documents.

2.13   The board is accountable to the responsible Minister for the Crown entity's performance. The board is the primary monitor of a Crown entity's performance and is expected to raise significant concerns and risks directly with the responsible Minister. It must give the responsible Minister any information about the operations and performance of the Crown entity that the responsible Minister asks for.

2.14   Board members have a set of collective and individual duties, which are similar to the duties of a director in the private sector. The Crown Entities Act sets out the collective duties of board members to ensure that the Crown entity:

- performs its role effectively, efficiently, and in the spirit of public service (in collaboration with other public organisations where practicable); and

- operates in a financially responsible way, prudently manages its assets and liabilities, and strives to ensure its long-term financial viability.

2.15   The Crown entity's executive is responsible for the day-to-day management of the Crown entity. The executive reports to the Crown entity board about the entity's progress and performance.

Monitoring departments help responsible Ministers carry out their role

2.16   Usually, the government department that administers a Crown entity's enabling legislation is also its monitoring department.

2.17   The monitoring department supports the responsible Minister and provides advice about whether the Crown entity is performing to expectations. This includes advising the responsible Minister and administering appropriations and legislation relevant to the Crown entity.

2.18   Monitoring departments also provide advice to the responsible Minister about appointing members to a Crown entity board and manage the appointment process. For Crown agents or autonomous Crown entities, the responsible Minister appoints board members. For independent Crown entities, the Governor-General appoints the board members on the recommendation of the responsible Minister.

2.19   Monitoring departments typically monitor Crown entities that are in the same sector.

Central agencies play a role in supporting the system

2.20   The Treasury and Te Kawa Mataaho jointly administer the Crown Entities Act. The Treasury administers the part of the Act that details Crown entity reporting and financial obligations. Te Kawa Mataaho administers parts of the Act that detail establishing, governing, and operating Crown entities.

2.21   Both Te Kawa Mataaho and the Treasury provide guidance for Crown entities and monitoring departments. For example, Te Kawa Mataaho has published the main guidance for monitoring departments. The Treasury has published guidance on preparing end-of-year performance information for Crown entities.

Good system-level guidance and support is available

2.22   Te Kawa Mataaho has published a suite of guidance to support responsible Ministers, monitoring departments, and Crown entities.

2.23   The main guidance is *It Takes Three: Operating Expectations Framework for Statutory Crown Entities*.[9] This guide sets out the roles, responsibilities, and operating expectations of monitoring departments, Crown entities, and

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9   This guidance is available at publicservice.govt.nz. It was last updated on 14 July 2014.

responsible Ministers under the Crown Entities Act. It also provides context about how the Crown entity monitoring system works.

2.24   *It Takes Three* sets out four guiding principles:

- **Clear roles and responsibilities**. All parties in the monitoring arrangement fulfil their critical roles and responsibilities. They have a shared understanding of their statutory roles and responsibilities, meet all statutory accountabilities, and follow the "no-surprises" convention.

- **Strategic alignment**. Policies strategically align so the same principles drive relevant parties to the same outcomes. There is cross-government engagement between Crown entities and other parts of the relevant sector.

- **Efficient and effective monitoring**. Performance monitoring, data collection, assessing and managing risk, and resource management are customised and proportionate to each Crown entity.

- **Trusted engagement**. The parties in the monitoring arrangement commit to good practice to ensure that their relationships are trusting and productive.

2.25   The four principles are each supported by sets of "working principles". These working principles define the specific expectations of each party at a high level.

2.26   There are two more guides, one for monitoring departments and one for responsible Ministers. There is also guidance material for Crown entities on Te Kawa Mataaho's website.[10]

2.27   In our view, the guidance available is of good quality and reasonably comprehensive. The guidance clearly sets out the roles, responsibilities, relationships, and statutory requirements for each organisation. It also provides helpful information about why specific activities are important and assists organisations to understand how they should carry out activities.

2.28   There is also a voluntary cross-agency network of monitoring practitioners – the Monitoring, Appointments and Governance Network. It aims to build a community of practice to support and improve the performance of managers and advisers through hosting networking opportunities, sharing experiences and information, encouraging good practice, and helping the professional development of officials.

Monitoring departments are expected to develop monitoring frameworks

2.29   Te Kawa Mataaho prepared *It Takes Three* for responsible Ministers, monitoring departments, and Crown entities. Because of this, it is general in nature. The guide sets an expectation that each monitoring department should develop and

maintain a monitoring framework that is appropriate and proportionate to the Crown entity it is monitoring.

2.30 Monitoring frameworks help ensure that there are common expectations between monitoring departments and Crown entities and that roles and responsibilities are well understood.

2.31 In our view, to be effective, monitoring frameworks should clearly set out:

- the purpose of the monitoring and the value gained;

- how the monitoring department will carry out its monitoring role. This includes who is responsible for monitoring, the scope of monitoring, relevant accountabilities, frequency of reports, when and why different staff will meet, and an escalation process for risks;

- the information the monitoring department needs to monitor effectively. This includes the outcomes the Crown entity is trying to achieve, the information that will be used to measure a Crown entity's progress, any gaps the Crown entity should address, and an understanding of what "good" performance looks like; and

- how performance issues will be managed. This should include what happens if a Crown entity does not meet performance expectations, how monitoring departments will advise responsible Ministers about how a Crown entity is managing poor performance, and the interventions available.

Monitoring frameworks need improvement

2.32 In our 2009 report, we recommended that monitoring departments have a clear and documented understanding of the monitoring role they have for each Crown entity and their responsibilities in fulfilling this role.

2.33 When we looked at monitoring frameworks for this audit, we found mixed results. Some monitoring departments had frameworks that were spread across multiple documents or were only partially documented.

2.34 There are no requirements on what form a monitoring framework should take. Monitoring departments and Crown entities can record their monitoring framework in a single document or across multiple documents. However, to be well understood and provide a useful basis for monitoring, frameworks need to be accessible for monitoring staff and the Crown entity.

Frameworks do not fully define roles and responsibilities

2.35 All of the monitoring departments that responded to our survey told us that they had a document or documents that outlined the roles and responsibilities of organisations involved in a monitoring arrangement. However, nearly half of

Crown entities that responded said they did not have, or were not aware of, an agreement in place that set the monitoring and reporting requirements. This suggests that roles and responsibilities were not fully defined and understood.

2.36   We asked to see the frameworks related to nine monitoring arrangements. Overall, the documents we received varied in quality. We were typically provided with internal guidance documents about how staff members should carry out their roles. This included dates when quarterly reporting was due or when board members' terms were up for renewal or replacement.

2.37   Although these frameworks provided guidance to monitoring staff for some matters, they were not comprehensive. Frameworks did not fully document all aspects of the monitoring department's role for each Crown entity. For example, frameworks we saw:

- stated that part of a Crown entity's performance would be based on measures in its Statement of Performance Expectations. However, frameworks did not cover what the monitoring department should do if performance did not meet expectations, or how to influence performance expectations that were not aligned to the responsible Minister's or the Government's priorities;

- stated that a Crown entity's quarterly report is due one month after the end of a quarter. However, monitoring frameworks did not cover what monitoring staff should do if a report is delayed, did not contain the information required, or highlighted poor performance;

- stated that a quarterly report should have information on risks. However, frameworks did not clearly outline how to gather information on risks or, after they were identified, how to prioritise, escalate, or track them; and

- had a calendar of due dates for certain reports. However, frameworks did not specify how monitoring departments should engage with a Crown entity on certain reports, such as when a monitoring department receives a draft Statement of Performance Expectations.

2.38   When roles and responsibilities are not clear, there can be confusion. In practice, we found that monitoring departments and Crown entities rely on relationships to address any ambiguity in roles and responsibilities. Although a strong relationship supports effective monitoring, in our view formalising and documenting expectations helps ensure that they are understood by all parties.

Monitoring arrangements tend to be "one size fits all"

2.39 Crown entities and monitoring departments are expected to adapt the expectations set out in Te Kawa Mataaho's *It Takes Three* to their specific circumstances.

2.40 *It Takes Three* states that monitoring departments need to customise their approach to monitoring so it is proportionate to the profile (for example, the size, role, and risk profile) of each Crown entity (see paragraph 2.24). Customising the approach helps to ensure that monitoring does not impose an excessive burden on a Crown entity for limited benefit.

2.41 We expected to see evidence that monitoring departments understood the profile of the Crown entities they were monitoring and adapted their monitoring approach appropriately. For example, monitoring departments could change the quantity or frequency of information the Crown entity reports to them and how often officials met to discuss issues and challenges.

2.42 However, we found that most monitoring departments use the same framework for all the Crown entities they monitor. Although we saw monitoring departments sometimes try to understand the scope, scale, complexity, and risk profile of the Crown entities, we did not see them use this information to help inform the monitoring expectations or activities. For example, we saw a situation where a small Crown entity had the same reporting requirements as a Crown entity that manages significant assets.

2.43 This is consistent with the findings of at least three Performance Improvement Framework reviews we saw. One review commented that the monitoring department "needs to develop its engagement and monitoring approach to better reflect the scale, size and complexity of the individual Crown entities". Another review said that "Crown entities consider much of the monitoring is low level, with a compliance rather than strategic approach".

2.44 Many Crown entities we spoke to consider the current monitoring requirements to be an administrative burden without an equivalent benefit. We heard that one of the biggest challenges is that monitoring departments do not focus on the right things and do not fully understand the Crown entities they are monitoring. Through our survey, Crown entities told us that information requests often do not reflect realistic time frames because they have not considered a Crown entity's capacity to respond.

Monitoring frameworks are not developed in consultation with Crown entities

2.45 In our view, the issues we have described highlight the importance of Crown entities and monitoring departments working together to understand one another's roles, establish common expectations about the monitoring relationship, and test the practicality of those expectations.

2.46 The advice monitoring departments provide Ministers should be independent of Crown entities. However, a monitoring department and Crown entity working together does not necessarily undermine the independence of this advice.

2.47 In our view, monitoring departments and Crown entities working together will more likely secure engagement and buy-in to monitoring and strengthen relationships. These factors will facilitate better information sharing, make it more likely that issues can be identified early, lead to more effective and enduring solutions, and improve the quality of advice to Ministers.

2.48 Te Kawa Mataaho's guide, *It Takes Three*, sets similar expectations. For example, it states that monitoring departments should work with the Crown entity to ensure that performance reports provide enough detail on the entity's progress.

2.49 However, in our view, Crown entities were not adequately consulted in the development of the monitoring frameworks we looked at. We heard from Crown entities that they felt the monitoring frameworks were imposed on them.

2.50 Several Crown entity chairpersons told us that it would be helpful to document the purpose of monitoring and the respective roles and responsibilities that are agreed between individual Crown entities and their monitoring departments. We agree. In our view, the purpose and objectives of a monitoring arrangement should be set out clearly in the relevant monitoring framework.

2.51 Crown entities and monitoring departments working together to develop a monitoring framework that is consistent with statutory requirements and available guidance would provide an opportunity for monitoring departments to:

- learn more about the context in which the Crown entity operates;
- learn more about the nature and scope of the Crown entity's functions; and
- discuss, test, and document the boundaries of the respective roles and responsibilities in the monitoring arrangements so that they are well understood.

2.52 In our view, frameworks should also be reviewed periodically to ensure that they reflect the latest expectations of responsible Ministers as well as major changes

in the Crown entities' operating environment. It would be useful if these reviews took place, at a minimum, after significant change in the size, role, risk profile, performance, or leadership of Crown entities. We discuss this further in paragraphs 5.30-5.37.

Recommendation 1

We recommend that monitoring departments and Crown entities work together to clearly document the monitoring framework they will use to support their monitoring arrangements. Monitoring frameworks should at a minimum:

- set out the purpose and objectives of the monitoring;

- set out the respective roles and responsibilities for the monitoring arrangements;

- describe the information the monitoring department needs to monitor effectively. This should include the outcomes the Crown entity is trying to achieve, the information that measures a Crown entity's progress, any gaps the Crown entity should address, and an understanding of what "good" performance looks like;

- set out how performance issues will be managed. This should include what happens if a Crown entity does not meet performance expectations and when and how monitoring departments should advise a responsible Minister about how a board is managing performance;

- be developed in consultation with the relevant Crown entities, and take into account an entity's specific circumstances, functions, and activities; and

- be supported by the responsible Minister.

3

Monitoring Crown entities in practice

3.1 In this Part, we discuss:

- how monitoring departments support key processes;
- how well monitoring departments are influencing the strategic direction of Crown entities; and
- how well monitoring departments are using their sector-wide knowledge to inform Crown entities.

3.2 We looked at nine Crown entity monitoring arrangements. We spoke with the Crown entity and its monitoring department in each arrangement.

3.3 We expected that monitoring departments would:

- support Crown entity engagement in budget and other financial management and policy processes where appropriate;
- support the appointment process to Crown entity boards;
- participate in setting direction and performance expectations for the Crown entities they monitor; and
- carry out monitoring activity that is appropriate to the circumstances of the Crown entity they monitor.

Summary of findings

3.4 Monitoring departments support most administrative processes between Crown entities and their responsible Minister well. However, some of these processes are still challenging or need improving. For example, although monitoring departments are experienced at identifying skill gaps on boards, they still find it difficult to identify suitable candidates to appoint.

3.5 Although monitoring departments support the process for Ministers signing off accountability documents, they engage with those documents in a limited way. This is a missed opportunity to influence the strategic direction of the Crown entities they monitor. Monitoring departments support the process for issuing letters of expectations by Ministers, but it is not clear how effectively these letters are used to influence Crown entity performance.

3.6 The knowledge that monitoring departments gain through their work should make them well positioned to support Crown entities. However, opportunities are often missed. For example, Crown entities have said they would like more support from monitoring departments to understand what is happening across their sector, but we observed that monitoring departments tend to view the performance of each Crown entity in isolation.

Monitoring departments support some processes well

3.7   There are a range of processes between responsible Ministers and Crown entities that monitoring departments are required to assist with, including preparing accountability documents (the Statement of Intent, Statement of Performance Expectations, and the annual report) and annual letters of expectations. Monitoring departments also support Crown entities with parliamentary processes, such as responding to parliamentary questions and preparing funding bids for the annual Budget process.

3.8   We heard that monitoring departments support these processes for Crown entity monitoring well.

3.9   Crown entities said that the support that monitoring departments provided for Budget bids and parliamentary questions was positive. Crown entities told us that the monitoring departments' expertise, systems, and processes were efficient and easy to engage with.

3.10   For the Budget bid process, one Crown entity told us that, even if the bid was not successful, the engagement it had with their monitoring department was valuable and improved the relationship between them.

Board appointment processes are well supported, but are still challenging

3.11   Monitoring departments are responsible for ensuring that Ministerial appointments to Crown entity governance boards are carried out effectively and efficiently. A responsible Minister we spoke to emphasised the importance of appointing the right people to support effective governance.

3.12   In our 2009 report *How government departments monitor Crown entities*, we found that some board appointment processes were not carried out effectively because of a lack of planning by the monitoring departments. We recommended that monitoring departments plan carefully before starting the board appointment process and consider the steps and timing required for the appointment.

3.13   For this audit, we did not look the processes of individual monitoring departments in detail. Instead, we sought feedback and looked at documents from a range of monitoring departments and Crown entities on the board appointment process.

3.14   In general, we found that monitoring departments support board appointment processes well. We saw evidence that monitoring departments advise Ministers on the skills and experience of board candidates and how they fit with the requirements of the board. They also receive advice on how to ensure that there is diverse board membership.

3.15   Monitoring departments have good methods of identifying what skills and experience board candidates require. All monitoring departments told us that they seek the views of board chairpersons to help identify skill gaps. We also saw some monitoring departments use skills matrices to identify skill gaps.

3.16   However, monitoring departments also highlighted several challenges with board appointments, including that it is time-consuming, public sector governance capability needs developing, and flexibility for reappointments is limited. The challenge that monitoring departments highlighted most was the difficulty in identifying enough suitable candidates for appointment.

3.17   Monitoring departments have developed tools to help identify suitable candidates. Some monitoring departments also maintain databases of potential board candidates. Although these are useful, we did hear concerns that there was not a wide enough pool of candidates in these databases.

3.18   Several monitoring departments that responded to our survey felt it would be beneficial to have a central source of candidates that was continually refreshed and supported by improved sourcing practices.

3.19   Crown entities also highlighted the importance of input from the board chairperson and chief executive, good communication throughout the process, and support after an appointment is made.

Greater monitoring department involvement in board inductions is needed

3.20   Of the Crown entities we surveyed, 38% said their board members and board chairpersons received an induction from their monitoring departments.

3.21   Some board members who responded to our survey said they would like the monitoring department to have greater involvement in the induction process and more information about the monitoring department's role and expectations. We also heard that board members would find refresher sessions useful. Board inductions happen early in a board member's term and there are limited opportunities to refresh their knowledge over time.

3.22   In our view, monitoring departments should work with Crown entities to ensure that there are adequate board induction processes carried out in a timely manner. These inductions should cover the role of the monitoring department. Monitoring departments and Crown entities should also consider whether regular refresher workshops are required.

Monitoring departments could be influencing strategic direction

3.23 The Crown Entities Act 2004 gives monitoring departments mandate to participate in setting strategic direction and performance expectations on behalf of the responsible Minister.

3.24 One of the main ways monitoring departments can do this is by providing the Crown entity with input into the development of its Statement of Intent and the Statement of Performance Expectations.

3.25 The Statement of Intent outlines the Crown entity's strategic intentions and medium-term activities. Crown entities prepare a Statement of Intent at least once every three years. The Statement of Performance Expectations identifies what Crown entities intend to achieve, how they will measure achievement, and how they will assess performance against strategic intentions in the upcoming financial year.

3.26 Te Kawa Mataaho's *It Takes Three* sets an expectation that monitoring departments provide comments on these documents and work with Crown entities to ensure that Statements of Intent are fit for purpose and strategic direction is appropriately responsive to government objectives.

Advice and input on draft accountability documents is limited

3.27 In our view, monitoring departments should be assessing and routinely providing feedback on how well draft accountability documents demonstrate clear links between strategic intent, proposed interventions, and investment.

3.28 We saw examples where monitoring departments did this. However, we found that, more generally, monitoring departments' feedback and advice on draft accountability documents was limited. Reviews of Statements of Intent and Statements of Performance Expectations tended to be superficial and lacked discussion about how proposed interventions contribute towards the strategic outcomes of the Crown entity and the sector it is in.

3.29 We regularly heard from both Crown entities and monitoring departments that the measures in a performance framework do not accurately tell a Crown entity's performance story. Although Crown entities and monitoring departments told us they know that specific measures are inadequate, we did not see evidence that monitoring departments regularly provide this feedback to the Crown entity or responsible Minister. We saw examples where Crown entities and monitoring departments appeared indifferent to the continued use of inadequate measures.

3.30   In our view, monitoring departments should more consistently challenge Crown entities to improve performance metrics and provide feedback to ensure that they are adequate and robust. Working together to agree on more comprehensive and appropriate performance metrics will enable a more accurate assessment of performance, including the Crown entity's contribution to strategic outcomes.

Recommendation 2

We recommend that monitoring departments and Crown entities ensure that there is meaningful engagement in the development of Crown entities' accountability documents. This should include engagement on the operating context, challenges, goals, expectations, and performance measures.

Letters of expectations could be better leveraged

3.31   Responsible Ministers set their expectations for Crown entities through an annual letter of expectations. These letters can be used to direct a Crown entity to complete specific pieces of work, meet certain performance targets, and follow government guidance where appropriate. Typically, monitoring departments prepare letters of expectations on behalf of the responsible Minister.

3.32   We heard that monitoring departments generally manage the process efficiently. In the examples we reviewed, monitoring departments helped Crown entities link a responsible Minister's letter of expectations with the performance measures in a Crown entity's Statement of Performance Expectations.

3.33   Ministers we spoke with felt this process could be improved. They recognised the importance of these letters to convey expectations to Crown entities.

3.34   Responsible Ministers also acknowledged that they could use these letters of expectations to better influence priorities and drive performance. We agree. These letters give the responsible Minister, the monitoring department, and the Crown entity important opportunities to have meaningful discussions about the Crown entity's operating context, challenges, goals, and expectations.

3.35   We acknowledge that there are certain areas where a responsible Minister cannot intervene, such as in statutorily independent functions. However, we strongly encourage Ministers, Crown entities, and monitoring departments to consider how they make the most of this opportunity without compromising existing accountabilities and responsibilities.

Important connections are not being made

3.36   A monitoring department can add value by making connections between its knowledge of the Crown entity's sector, the regulatory environment, the department, and the responsible Minister's office. Where appropriate, the monitoring department can share that information with its Crown entity. This can help Crown entities understand what is happening across government that could affect them.

Monitoring departments struggle to take a sector-wide view

3.37   Te Kawa Mataaho's guide *It Takes Three* sets out an expectation that monitoring departments take a sector-wide view to monitoring. Monitoring departments should consider how Crown entities contribute to the Government's wider policy priorities and co-ordinate work within portfolios as well as connecting to work in other portfolios.

3.38   Monitoring departments are often responsible for more than one Crown entity. The monitoring departments we talked to tended to look at the Crown entities they monitor in isolation from one another. Although many Crown entities are part of the same sector, we did not see monitoring departments bring together an integrated view of how Crown entities are achieving sector performance.

3.39   This view was also reflected in some Performance Improvement Framework reviews we looked at. We saw references in these reviews about the need for monitoring departments to focus on strategic outcomes for the sector and take a more system-based or outcomes-focused approach.

3.40   Crown entities told us that they would like monitoring departments to keep them informed about what is going on across their sector and help them understand how their individual performance contributes to their sector's performance overall. Monitoring departments' communications about issues and risks across the sector was the lowest-rated aspect of communication in our survey of Crown entities. More than 35% of Crown entities said it was "poor" or "very poor".

Monitoring departments can support Crown entities to address regulatory challenges

3.41   Through their work, monitoring departments should have a good understanding of Crown entities' operating context, strategic objectives, and the financial and non-financial performance challenges they face. However, it was unclear to us to what extent monitoring departments use their understanding of Crown entities

to proactively identify opportunities to improve performance or help policy teams improve regulatory settings, where appropriate.

3.42   Many of the Crown entities we spoke with commented on how monitoring teams are siloed within departments. We heard that Crown entities struggled to engage with other teams of the monitoring department (such as the policy team), which made it difficult for Crown entities to influence policies that negatively affected their performance.

3.43   In our view, linking functions within monitoring departments is one of the most important opportunities that effective monitoring arrangements can create. Monitoring teams are uniquely placed to understand the challenges a Crown entity faces and should work with other teams in their department to help the Crown entity find and progress solutions to improve performance.

Recommendation 3

We recommend that monitoring departments and Crown entities share knowledge and seek to understand each other's operating context. This should include monitoring agencies:

- giving feedback to Crown entities about their performance in the context of the relevant sector and communicating key events that might affect relevant Crown entities; and

- briefing other teams in their department about the challenges facing the Crown entities that they monitor to identify appropriate support where needed.

Understanding Crown entity performance

<div style="text-align: right">4</div>

4.1   In this Part, we discuss:

- how well monitoring departments understand the context and business of the Crown entities they monitor;
- the quality of the performance information that monitoring departments use;
- the options available to address performance issues; and
- how often information on board performance is provided to responsible Ministers.

4.2   We expected that monitoring departments would:

- use a wide range of information to assess and evaluate the performance of Crown entities;
- identify risks to the performance of Crown entities and the wider sector;
- provide reliable and accurate advice to responsible Ministers about those risks and a Crown entity's performance more generally; and
- provide advice to responsible Ministers about using available levers to improve Crown entity performance.

Summary of findings

4.3   We looked at a range of monitoring reports to responsible Ministers. We found that they did not capture a full view of the Crown entity's performance. They generally lacked depth of analysis, did not report enough about risks, did not report on board performance regularly, and offered limited advice about actions that responsible Ministers could take when Crown entities were not meeting expectations.

4.4   From the information provided in monitoring reports, we could not see how monitoring departments could make a well-informed and reliable judgement on Crown entity performance. Both monitoring departments and Crown entities need to produce quality performance information to properly advise the responsible Minister on Crown entity performance.

4.5   Requesting or developing better quality information, especially on risks, would enable monitoring departments to help a Crown entity avoid an issue before it occurs. When issues do occur, there is no clear escalation process.

4.6   A well-functioning board is integral to the Crown entity monitoring system. However, when information on board performance is not routinely collected, it is difficult to determine how well a board is functioning. Monitoring departments should regularly seek to understand how effectively a board operates and report this to the responsible Minister.

Monitoring departments need to better understand the Crown entities they monitor

4.7   A monitoring department's ability to add value is highly dependent on its knowledge of the sector that the Crown entity is part of.

4.8   It is important that monitoring departments understand:

- the Crown entity's environment and regulatory context;
- the nature and scope of the Crown entity's role and functions;
- which organisations the Crown entity needs to work with to carry out its functions;
- the structure of the Crown entity; and
- the Crown entity's strategic objectives.

4.9   Crown entities told us that some monitoring departments did not have a thorough understanding of their issues or their business. Several Crown entities said that limited understanding was one of the biggest challenges of working with their monitoring department.

4.10   We accept that some Crown entities fit more naturally with the scope and mandate of their monitoring department than others. However, in our view, a critical part of the monitoring department's role is to build relationships with the Crown entity and understand the context it is working in. Crown entities might equally benefit from better understanding the scope and mandate of their monitoring department.

4.11   We strongly encourage monitoring departments and Crown entities to work together to build this knowledge and understanding. In our view, having secondments or joint induction sessions (where staff from each organisation have an opportunity to share information) is likely to be useful.

Better quality performance information is required

4.12   We expected that monitoring departments would have a good understanding of their Crown entities' key performance measures. We expected that monitoring departments would collect and analyse a range of information to develop an understanding of Crown entity performance and the likelihood of each Crown entity achieving its strategic objectives. We expected that monitoring departments would use this understanding to advise the responsible Ministers.

4.13   When performance objectives were not being met, we expected that there would be agreed escalation processes in place. We expected that the monitoring departments would provide advice to responsible Ministers about what options were available to improve performance.

4.14   We also expected that monitoring departments would also form a view about the effectiveness of Crown entity governance by, for example, requesting that Crown entity boards carry out regular reviews of their performance.

4.15   We reviewed monitoring reports of nine Crown entities written between 2019 and 2021 (29 reports in total). We found that, generally, the reports:

- lacked independent analysis and relied too heavily on information provided by Crown entities;

- did not report enough about the risks each Crown entity is facing in delivering its outcomes or whether Crown entities were adequately managing risks;

- did not report about the performance of Crown entity boards in a timely way; and

- offered limited advice about actions that the responsible Minister could take when Crown entities were not meeting expectations.

Reporting to responsible Ministers lacks analysis

4.16   We expected that monitoring departments would use the information reported by the Crown entity, combined with information from other sources, to assess a Crown entity's operational and strategic performance. We also expected to see:

- an assessment of whether the performance information adequately provided a picture of current performance;

- clear identification of any areas of poor performance, with reasons provided; and

- a summary of any actions being taken to improve performance.

4.17   In our view, this is the minimum level of information required to provide advice to responsible Ministers.

4.18   In the monitoring reports we reviewed, a red-amber-green scale was applied to different aspects of the Crown entity performance information, such as financial performance and progress towards performance expectations. Guidance from Te Kawa Mataaho in *It Takes Three* recommends that monitoring departments make their own assessment of these same aspects of a Crown entity's performance. However, we found this assessment was usually based on, or relied heavily on, a self-assessment by the Crown entity.

4.19   All the monitoring departments we surveyed told us that they use other sources of information as well as the information that Crown entities provide. However, we did not see evidence of how monitoring departments use this other information in the monitoring reports that we reviewed. In most cases, the

monitoring reports appeared to largely repeat the information a Crown entity provided without adding significant insight to it.

4.20   Few reports and briefings we reviewed were forward looking. Monitoring departments rarely drew information together in briefings to reach conclusions about significant issues facing a Crown entity or environmental changes that could affect a Crown entity's future performance.

4.21   In our view, monitoring departments need to provide an independent assessment of the information from Crown entities. It might be helpful if monitoring departments tested the information from Crown entities against information from other sources, such as customers and stakeholders, or compared the information with that from other entities.

4.22   There is likely to be information that the Crown entity already holds that could provide more comprehensive performance advice to responsible Ministers. This could include audit and risk committee reports, risk registers and frameworks, or workforce planning and other capability strategies.

4.23   Monitoring departments should have a good understanding of the range of information a Crown entity holds. In our view, monitoring departments should review these sources to ensure that they are consistent with externally reported performance information. We expect Crown entities to be open and transparent about this information with their monitoring departments.

4.24   Information sharing is an integral part of Crown entity monitoring. In our view, information sharing works better when monitoring departments and Crown entities work together to develop their monitoring framework, and establish clear expectations of one another and their roles and responsibilities (see Part 2).

Monitoring reports do not include adequate information on risk

4.25   We expected monitoring reports to include a robust assessment of a Crown entity's risks. Where risks are clearly identified, responsible Minsters should be advised about how effectively these are being managed and mitigated. Te Kawa Mataaho's *It Takes Three* states that the monitoring department should "seek information to identify risks to the entity, to facilitate risk monitoring and response" as well as "scan for and act on emerging risks that may require a response". We did not see evidence that these activities were regularly happening.

4.26   Monitoring reports we reviewed typically included:
  • a summary of the Crown entity's activities for the quarter;
  • financial information describing whether the Crown entity is on budget;

- non-financial performance information, including information setting out how many of the Statement of Performance Expectations measures are on target; and

- a summary of risks the Crown entity faces.

4.27   However, monitoring departments do not appear to have a routine method for gathering information on risk from, or about, Crown entities. We saw monitoring departments rely on an individual's knowledge of the sector and relationships with the Crown entity to understand potential risks.

4.28   Relationships with people working in the sector can provide useful information about a Crown entity's performance. However, relationships alone are not a reliable method for identifying the risks a Crown entity faces.

4.29   Ideally, the monitoring department would have its own framework for thinking about the risks that Crown entities face. The monitoring department should also use its regular engagement with the Crown entity and review of relevant documents to monitor and record key risks over time. This would assist the monitoring team in determining whether the risk is increasing or decreasing. It would also help the monitoring team decide when to raise a risk for discussion with the Crown entity, when to keep their own leadership informed, and when it might be necessary to brief the responsible Minister.

It is not clear whether mechanisms to address performance issues are effective

4.30   Responsible Ministers have a range of ways to influence the performance of Crown entities. These are sometimes called "performance levers". Monitoring departments advise responsible Ministers on the most appropriate levers to use. *It Takes Three* identifies several levers available for Ministers to use, including:[11]

- meeting with staff or board members;

- writing a letter of expectations;

- requesting information;

- directing the board chairperson to a particular action;

- leading a process to amend legislation;

- altering the monitoring regime;

- commissioning a review of the Crown entity's performance; and

- changing board members.

4.31   The most common lever we saw responsible Ministers use was the letter of expectations. Generally, the responsible Minister would use this letter to inform

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11   The full list of performance levers available to responsible Ministers is available at publicservice.govt.nz.

the Crown entity that they expect performance targets to be met, if the Crown entity had not met the target the previous year.

4.32   We did see examples of other performance levers being used. In one example, a Crown entity faced significant financial pressures. The monitoring department advised the responsible Minister about the levers they could use for addressing this issue. The levers included more intensive monitoring and new performance measures.

4.33   One responsible Minister told us that telling the Crown entity to improve generally works (in their view, instructing the Crown entity worked about 80% of the time). In the other instances, they would have a direct conversation with the board chairperson. When asked what they would do if the direct conversation did not work, the Minister said they were not sure because so far it has always worked.

4.34   However, staff from both Crown entities and monitoring departments told us that the current levers are ineffective. We heard that when a Crown entity is not performing, the monitoring department feels it can only inform the Crown entity to improve performance either through a letter or in a meeting as other levers are perceived as too drastic. In our view, monitoring departments should consider what other actions are appropriate to help the Crown entity address the cause of poor performance.

4.35   Where there are disagreements between monitoring departments and Crown entities, we did not see a clear escalation process for how those issues would be addressed. Only 43% of Crown entities surveyed said they had an agreed process with their monitoring department for resolving any issues or disputes.

4.36   Most of the monitoring departments we spoke to could not identify a clear escalation process to resolve an issue or dispute. In some cases, monitoring departments were not clear about when an issue should be escalated to responsible Ministers.

4.37   For example, in one situation we heard that neither the board nor the monitoring department advised the responsible Ministers of bullying and harassment complaints in a Crown entity until they were reported in the media. This is despite the board and the monitoring department acknowledging that they were aware of these issues for some time. Although it is not the responsible Minister's role to deal with employment matters, they do have an interest in understanding the risk this could present to the performance of the Crown entity and the reputation of the public sector.

4.38   In our view, there would be value in monitoring departments and Crown entities having more discussions about how to escalate risks rather than waiting for poor

performance to trigger an intervention. These could involve senior management having more discussions with Crown entity chief executives, Ministers' offices, or even central agencies, where appropriate.

Information on board performance is not routinely provided to responsible Ministers

4.39   Understanding and managing risks to the Crown entity is important for effective governance. Monitoring departments need to gather information to understand whether governance in the Crown entity that they are monitoring is being carried out effectively. They should report this information to the responsible Minister.

4.40   A well-functioning board is critical to good Crown entity performance. We expected that board evaluations would be carried out regularly to understand whether it is functioning effectively and to identify improvements in board performance.

4.41   Te Kawa Mataaho recommends that both internal and external evaluations should be carried out by Crown entities. We expected that monitoring departments would use the results of these evaluations to keep responsible Ministers informed about board performance.

4.42   Two-thirds of Crown entities we surveyed had carried out a board review, and most of these were done in the last two years. More than half were external reviews. In our view, this is positive.

4.43   However, we could not see evidence that the results of board evaluations were consistently reported to responsible Ministers. In the monitoring reports that we reviewed, we found little reference to board evaluations. We saw advice about individual board member performance, but these were generally raised during reappointment processes (about once every three years).

4.44   It appears that unless the Crown entity volunteers the information, poor performance of a Crown entity board or an individual board member can continue for a significant length of time without the responsible Minister being aware, and without the issue being addressed.

4.45   Monitoring departments should regularly ask Crown entities to carry out board evaluations. Information from these evaluations will enable them to form advice about whether the Crown entity's governance is effective.

4.46   As well as formal board evaluations, monitoring departments could assess the effectiveness of governance in other ways, including by:

- obtaining board papers to understand whether the board is being made aware of, and/or actively seeking, information about strategic risks;

- checking the quality of risk monitoring and mitigations; or

- ensuring that internal risk and assurance plans are in place (without overstepping the governance role of the board).

Advice to responsible Ministers is integral to their understanding of Crown entities' performance

4.47 Crown entity boards are primarily accountable for Crown entity performance. However, advice from the monitoring department is important for Ministers to adequately understand how a Crown entity is performing.

4.48 Responsible Ministers need to be aware of the risks a Crown entity faces and the effects this might have on meeting strategic goals or on operational performance. Responsible Ministers should also have a clear understanding of how board members are contributing to the performance of a Crown entity. Without this knowledge, it can be difficult for a responsible Minister to know if a Crown entity board is effectively delivering on strategic objectives.

Recommendation 4

We recommend that monitoring departments improve the quality of performance reporting about Crown entities, ensuring that reports to Ministers provide an independent view on:

- a Crown entity's strategic and operational performance;

- how the Crown entity is managing risk;

- the potential impact of risks on both performance and outcomes; and

- the results of regular board evaluations in a timely way.

Building monitoring capability

<div style="text-align: right">**5**</div>

5.1 In this Part, we discuss:
- the inherent tensions in the Crown entity monitoring system;
- maintaining monitoring capability in monitoring departments;
- the need for strong system leadership; and
- the need for regular reviews of how monitoring arrangements are operating.

Summary of findings

5.2 When we spoke with people who were directly involved in Crown entity monitoring arrangements, we observed a clear desire to improve the effectiveness of these arrangements. This included improving transparency and accountability to responsible Ministers and providing better advice and support for Crown entities so they can provide more effective services to New Zealanders.

5.3 Nevertheless, there was a perception that little progress had been made to address the recommendations from our 2009 report, *How government departments monitor Crown entities*.

5.4 There are tensions that responsible Ministers, Crown entities, and monitoring departments must manage. Monitoring departments will sometimes need to challenge Crown entities while respecting the arm's-length nature of Crown entity governance and maintaining a constructive working relationship. Monitoring departments describe this tension as a "critical friend" relationship.

5.5 In our view, if the right balance is not achieved, the quality of the monitoring activity is undermined. Currently opportunities for monitoring departments to properly understand Crown entities' business and provide meaningful advice and support to improve Crown entities' performance are being missed.

5.6 Compounding these difficulties, monitoring departments can find it challenging to retain staff with monitoring capability. We regularly heard that staff turnover was an issue. Because monitoring relies on an individual's knowledge and connections with the Crown entity, the monitoring department's long-term relationship with a Crown entity can be undermined if those individuals leave.

5.7 Stronger system leadership could help address these challenges. Although guidance published by Te Kawa Mataaho is used widely, monitoring departments and Crown entities told us they need further support to implement this guidance, particularly for developing and maintaining the "critical friend" relationship.

5.8 Responsible Ministers, Crown entities, and monitoring departments should review monitoring arrangements regularly to ensure that they remain fit for purpose.

There are inherent tensions in the Crown entity monitoring system

5.9   At the core of the Crown entity monitoring system are inherent tensions. For example:

- Monitoring departments and Crown entities need to work closely to develop monitoring frameworks and common expectations. However, a monitoring department must retain enough independence to take an objective view of the Crown entity's performance.

- To be an effective "critical friend", monitoring departments must be prepared to challenge the information that Crown entities provide. However, at the same time, they also need to respect the arm's-length relationships a Crown entity has with its responsible Minister.

- Crown entities highlighted that one of the main challenges in the monitoring arrangement was that monitoring departments lack understanding of the Crown entities' context and business. Despite this, some Crown entities were reluctant to share too much information because they were concerned that the monitoring department would micromanage their business.

- The primary oversight and monitoring relationship for a Crown entity is with its governance board. However, part of a monitoring department's role is to provide advice to the Minister about whether board governance is effective. To form this judgement, the monitoring department might need to see some similar information as the board to assess whether the board is carrying out effective oversight.

- The board of a Crown entity receives information about the performance of a Crown entity that is more detailed and up-to-date than the information a monitor receives. We accept that it can be challenging for monitors to provide a totally accurate and up-to-date assessment of entity performance. However, this is why ongoing dialogue between monitors and Crown entities is important.

5.10   Ministers we spoke to acknowledge the complexity in balancing these tensions. They told us that a framework that enables Crown entities to operate at arm's length is good and emphasised that their relationship with the board chairperson is the primary source of assurance about a Crown entity's performance.

5.11   The difficulty in balancing these tensions appears to be a barrier to monitoring departments and Crown entities working together to actively improve their monitoring relationship. For example, monitoring departments routinely accept information provided by Crown entities and report it to responsible Ministers without substantively challenging the information. We saw instances where both monitoring departments and Crown entities appeared indifferent to the

continued use of inadequate performance measures (see paragraph 3.29). We also heard from some monitoring departments that the levers to address poor performance by Crown entities were ineffective (see paragraph 4.34).

5.12 Some monitoring departments do not appear to prioritise the monitoring function. In our survey, people who worked at the monitoring departments highlighted a range of challenges, including that:

- the monitoring departments they worked in lacked understanding of the monitoring function;
- monitoring teams lacked resourcing;
- people with specialist skills were hard to recruit and retain;
- the work was largely reactive, which made it difficult to take a strategic focus; and
- structures in some monitoring departments did not support the capability required to monitor effectively.

Maintaining monitoring capability is difficult

5.13 We heard that, for monitoring teams to work well, they need to have:
- strong relationship management skills;
- the ability to understand complicated organisations quickly;
- knowledge of risk management and investment logic; and
- attention to detail and analytical ability.

5.14 Some monitoring departments have long-serving and experienced monitoring staff. These staff members have extensive knowledge of the sector and strong relationships with the Crown entity.

5.15 However, people with these skills and experience are relatively few. Every monitoring department we spoke to said they face challenges in maintaining fully effective monitoring capability.

5.16 We identified two main challenges to maintaining capability:
- People we spoke to said that staff regularly move away from monitoring, resulting in a loss of skills and relationships. For example, one Crown entity told us they had five different monitors in five years.
- Monitoring staff told us that they feel they lack influence. Crown entities also told us they felt monitors could not always influence chief executives and responsible Ministers to make required changes to support improvements (for example, changing how funding is allocated to achieve outcomes).

5.17 Staff from monitoring departments said that if there was a clear career development pathway for monitoring staff, it could help attract and retain more people. From the interviews we carried out, it was clear that this pathway did not exist.

There is a need for strong system leadership

5.18 Monitoring departments and Crown entities primarily use guidance published by Te Kawa Mataaho. In our survey, every monitoring department stated it uses guidance from Te Kawa Mataaho, such as *It Takes Three*, in its monitoring role. The same survey found monitoring departments rated the guidance documents that Te Kawa Mataaho produces as the most useful for monitoring activities.

5.19 Although the guidance is good quality, comprehensive, and widely used, some monitoring departments told us they would find more examples of good practice useful. Monitoring departments and Crown entities also told us they felt that Te Kawa Mataaho could have a greater role in helping monitoring departments with this.

5.20 In the Performance Improvement Framework reviews it carried out, Te Kawa Mataaho also identified challenges to effective monitoring, including:

- encouraging monitoring departments to collaborate with Crown entities to build monitoring approaches together;
- supporting approaches that better reflect the individual Crown entities being monitored; and
- improving sector co-ordination across Crown entities on relevant issues affecting the wider sector.

5.21 Te Kawa Mataaho has an opportunity to explore how it provides more support for, and greater oversight of, the Crown entity monitoring system. This includes providing advice on how to develop the "critical friend" relationship. Although this relationship will be unique to each monitoring arrangement, Te Kawa Mataaho is well placed to offer support.

5.22 Te Kawa Mataaho has recognised that there are areas where improvements to monitoring performance and capability are required. We have heard that it is planning to do more work to support this system. For example, it has recently appointed a director to scope its role in supporting appointments, governance, and Crown entity monitoring.

Recommendation 5

We recommend that Te Kawa Mataaho Public Service Commission continue to strengthen its support for, and oversight of, the Crown entity monitoring system. In particular, how it could:

- assist monitoring departments and Crown entities in creating and applying effective monitoring frameworks;

- promote good practice in monitoring departments and Crown entities, including supporting communities of practice and professional development for monitoring practitioners;

- set expectations with chief executives of monitoring departments about the priority that needs to be given to effective Crown entity monitoring;

- regularly assess the effectiveness of monitoring carried out by monitoring departments and hold departmental chief executives to account for meeting these expectations;

- support effective Crown entity governance, such as advice for succession planning, talent management, and good practice tools; and

- where monitoring is ineffective, provide additional advice and support to help monitoring departments and Crown entities improve.

5.23   In response to our findings, Te Kawa Mataaho has told us it has several initiatives under way that will address some of the challenges we have identified. We are encouraged by this and will maintain an interest in the progress of that work.

5.24   For example, Te Kawa Mataaho told us it is currently including monitoring performance in the performance measures for monitoring department chief executives.

5.25   It also plans to:
- work with relevant agencies to develop a post-graduate professional development pathway for monitoring staff;
- develop tools to support more effective and diverse boards, such as a public service competency framework for boards and an all-of-government board appointment data integration system; and
- update its guidance following the Public Service Act 2020 reforms and develop more practical, hands-on guidance to support monitoring departments.

5.26 The Treasury administers Part 4 of the Crown Entities Act 2004, which covers Crown entity reporting and financial obligations. In our view, the Treasury should also consider its role in supporting Te Kawa Mataaho and the Crown entity monitoring system.

5.27 We acknowledge that our findings do not specifically reference Māori-Crown relationships or te Tiriti o Waitangi. In part, this reflects the fact that these are not referenced in the Crown Entities Act or *It Takes Three*.

5.28 The Ministers of Finance and the Public Service, through the Treasury and Te Kawa Mataaho respectively, issue an enduring Letter of Expectations that applies to all Crown entities. In the current letter, both Ministers indicate that they expect Crown entities to support future-focused Māori-Crown relationships.

5.29 In our view, Te Kawa Mataaho should consider working with the Office for Māori Crown Relations – Te Arawhiti[12] to explore ways they can support monitoring departments and Crown entities to meet these expectations within their monitoring frameworks. There could also be an opportunity to consider reflecting these expectations more explicitly in other relevant guidance.

Regular review of how monitoring arrangements are operating would be valuable

5.30 Some monitoring departments agreed that regular reviews of monitoring arrangements were needed. They were not clear how often they should review monitoring approaches, what to measure, and how to assess if they are monitoring effectively. This means that monitoring departments cannot be fully confident that they are well placed to engage with Crown entities.

5.31 We saw examples of monitoring departments making changes to how they monitor. These changes were usually in response to a significant issue. Generally, changes focused on the frequency of reporting. For example, when one Crown entity was having significant financial issues, the monitoring department increased the frequency of financial reporting. However, it was not clear to us what steps the monitoring department took to better understand or help the Crown entity address the underlying cause of this issue.

5.32 Our survey supports this finding. We found that although half of monitoring departments surveyed had reviewed how they monitor their Crown entities in the last three years, only one did so as part of a regular scheduled review. More than 60% of monitoring departments that responded to our survey carried out the review themselves and did not involve Crown entities.

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12 The Office for Māori Crown Relations – Te Arawhiti is a Crown agency dedicated to fostering strong, ongoing, and effective relationships with Māori across Government. It provides support and guidance for relationships between Māori and the Crown, which, through effective partnership, realise the intentions of te Tiriti o Waitangi.

5.33   Chief executives of monitoring departments need a way to assure themselves that their monitoring approach is effective. Regular reviews allow monitoring departments and Crown entities to determine if the monitoring framework is fit for purpose or what needs to change to improve it.

5.34   In our view, monitoring departments and Crown entities should collaborate on these reviews to ensure that they both fully understand and buy into their monitoring frameworks.

5.35   Greater collaboration can also help to clarify expectations and appropriately reflect a Crown entity's circumstances. In turn, this can mitigate any perception that monitoring is imposed.

5.36   Monitoring departments should regularly ensure that responsible Ministers are satisfied with the quality and frequency of monitoring advice.

5.37   In our view, these reviews should take place at least after significant change in the size, role, risk profile, performance, or leadership of Crown entities has occurred.

Recommendation 6

We recommend monitoring departments, Crown entities, and responsible Ministers regularly review monitoring arrangements to ensure that they remain fit for purpose.

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