



Lifting our gaze

Making broader outcomes a reality in the delivery of major infrastructure projects

January 2020

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1 Introduction: Lifting our gaze

New Zealand faces a choice. Our country is seeing historically high levels of investment in major infrastructure projects, with the Government spending taxpayer dollars on infrastructure in every corner of New Zealand. At the same time, our construction sector, housing stock and the environment are all under significant pressure from underinvestment and limited incentives for public sector agencies to use infrastructure as a means of delivering wider public outcomes (including social, cultural, economic and environmental outcomes).

The Government has recognised this and has shown a desire to steer the public sector to consider how it can help deliver these wider public benefits. This has been motivated by initiatives such as the Construction Sector Accord (the 'Accord'), Living Standards Framework, and new Government Procurement Rules. What is missing is an infrastructure investment approach (described, for example, in Budget and business case processes) that empowers agencies to plan and deliver wider outcomes from their own projects with funding support from elsewhere in the public sector. At present, most individual agencies appear to focus solely on how their infrastructure projects will deliver outcomes specific to their sector, rather than to all New Zealanders.

As a result, New Zealand agencies are leaving money on the table. The New Zealand Infrastructure Commission – Te Waihangā (the 'Commission') has published a pipeline of planned infrastructure projects with an estimated value of \$21.1bn, spanning 15 public sector agencies and more than 500 projects.¹ On the basis that each of these projects could help deliver a set of wider public outcomes – for example, improved skills in the local construction industry, reduced waste-to-landfill and greater use of Māori and Pasifika suppliers – every additional 1% of net project value that the Government could invest in these projects (either through increased contractor margins or direct Government spending) could accelerate more than \$200m of additional wider public outcomes that would not otherwise have been delivered.

It is time to start putting these ideas into practice. The New Zealand public sector, construction industry and infrastructure community need to collectively lift our gaze and view infrastructure as not only an enabler of economic growth, but as a catalyst for delivering the social, economic, and environmental benefits that are now required under the new Government Procurement Rules. This paper explores several key issues and routes to expanding the role of infrastructure investment, and includes case studies and examples of how initiatives such as the Accord can be used to deliver wider public outcomes.

1. <https://infracom.govt.nz/projects/pipeline-analysis/>



What is driving our current outcomes?

New Zealand's infrastructure investment framework is currently dominated by three core features that seek to maximise public value and de-risk specific infrastructure investments on a project-by-project basis.

Project and governance arrangements

When preparing to deliver major infrastructure projects², New Zealand public sector agencies often establish dedicated project teams to plan and execute the investment process on behalf of the Government.

Traditionally, the role of the project team is to develop a business case, engage with the market and deliver the project within an agreed budget. Project teams are rewarded depending on how they manage within budgets and de-risk project delivery, which often encourages agencies to take a “blinkers on” approach to planning and delivering major projects. Budget constraints and short-term metrics/incentives can cause projects to be viewed solely within the silo of their own procuring agency.

Typical governance and management structures created for the project team often measure success based on delivering a predefined solution on-time and within budget. Benefits realisation analysis, where present, typically focuses on agency- or sector-specific outcomes, with the delivery of broader public benefits often ignored or undervalued.

Business case framework

The Better Business Case framework standardises investment decisions so that they are easily comparable for decision makers. It explicitly requires procuring agencies to make trade-offs to identify a preferred project option that meets that agency's objectives and delivers public value. In almost all cases, public value analysis is exclusively related to *what* the project will deliver, without giving much regard for *how* it will be delivered and the potential cross-sector implications.

At present, Treasury's business case guidelines do not offer procuring agencies an effective means of capturing wider public outcomes that can be achieved within the process of delivering the project. They do not provide a clear mandate to consider these outcomes more broadly, value them explicitly, or empower agencies to leverage their preferred commercial model as an opportunity to deliver these outcomes.

2. The term “project” is used in this paper to refer to portfolio, programme, or project investments.



Vote mentality and appropriations

Budget processes incentivise agencies to squeeze the most value from their immediate and finite Budget appropriations. The direct outcome of this project-specific funding constraint is that agencies are not incentivised to seek opportunities to achieve enhanced public outcomes from their projects. As a result, large public risks – such as the sustainability of the NZ construction sector – can accrue.

For example, an agency delivering a new hospital within the Vote Health budget may be reluctant to pay a premium to support research and development (R&D) in the local construction industry, despite the obvious benefit to future projects in the same region. Such investments are, by definition, public good investments, however they do not fit squarely within the confines of current Budget or Better Business Case frameworks. Providing agencies with a mandate to align the wider benefits of infrastructure investments to different funding streams would increase the likelihood of realising these benefits.

There is no question that investing in wider public outcomes is the right thing to do from an “NZ Inc.” perspective and would achieve a range of positive outcomes for the country as a whole. Conversely, there are real costs involved with delaying investment in these wider outcomes, which simply postpones (and often amplifies) the underlying risks of underinvestment in these areas. However, under the current mindset there is little incentive for procuring agencies, operating within strict project-specific budget constraints, to invest in achieving these wider outcomes. An agency with a purely altruistic approach to pursuing wider outcomes would, under a fixed budget, directly compete with the objectives of the project itself, effectively trading off potential benefits from its own project against a set of wider public outcomes.

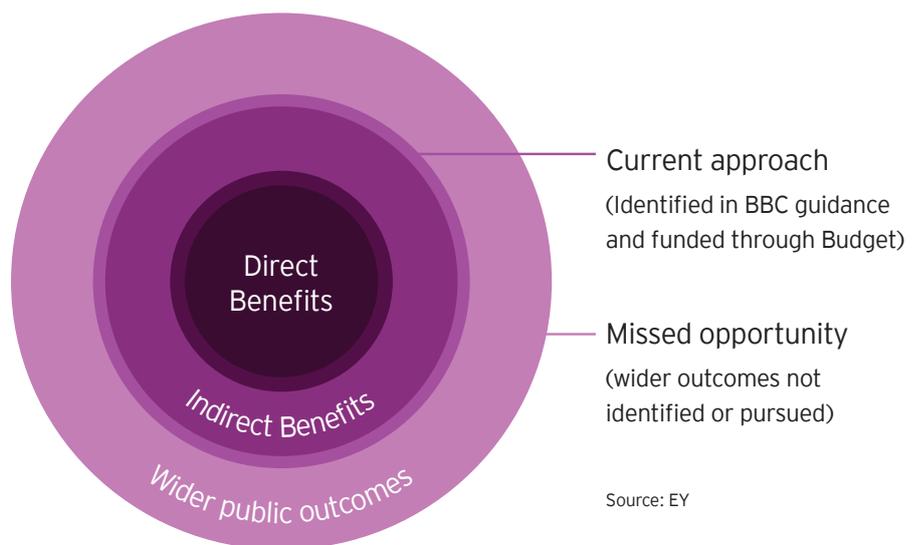
The current system therefore rewards narrow depictions of value that align to an individual investment. There is a clear opportunity to build on this approach and explore opportunities to broaden this value base in a way that maintains all that is good about the current system.

3 What is the opportunity?

This section outlines the potential opportunities available to procuring agencies to deliver wider public outcomes as part of their infrastructure investment decisions.

The role of infrastructure in enhancing economic and social value is well known. By definition, infrastructure connects: it sits at the heart of complex societal and economic interactions; it channels dispersed interests to maximise public good; it makes the complex, simple. It is therefore ironic that infrastructure investments are shaped by narrow investment decisions. What is best for a single project – or its procuring agency – often trumps what is best for New Zealand. Reshaping how we plan for and deliver infrastructure projects across New Zealand has the potential to unlock opportunities to maximise and capture long-term public value.

Figure 1: The missed opportunity to consider wider public outcomes





Moreover, there tends to be so much focus on *what* is being delivered that agencies often overlook the importance of *how* a project is delivered. The “how” can have substantial implications on the local community, workforce wellbeing, our construction sector, the environment and many other facets of New Zealand life. The decision (or not) to invest in these outcomes can have profound and long-term implications for the sector and our society – including our ability to effectively deliver the pipeline of future projects that will inevitably follow.

There is an opportunity to leverage investment in the delivery of major projects in New Zealand to:

- Support the advancement of the Government’s priorities and objectives
- Enhance the capability of the construction sector

A shift in thinking is required within New Zealand’s infrastructure investment framework to begin exploring how project costs and benefits can be addressed at a pan-Government level to achieve the Government’s wider priorities and objectives.

Deciphering terminology

The use of public procurement as a vehicle to realise positive public outcomes, beyond the core project delivery, is a topic of increasing interest in New Zealand and internationally. The Ministry for Business, Innovation and Employment (MBIE) refers to this as delivering *Broader Outcomes* through procurement, whilst some agencies explore these concepts under the term of social procurement. Terminology adopted internationally refers to the delivery of secondary policy objectives through procurement.

While there may be some academic nuances between these terms, the intent of this paper is to focus on the underlying concept sitting behind the terminology – i.e. that procurement can be used to realise wider public outcomes through delivering public benefit and mitigating public risks.

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How agencies deliver projects has implications on the community, the workforce, our construction sector, the environment and many facets of New Zealand life.



Exploring a missed opportunity: Advancing the Government's priorities and objectives

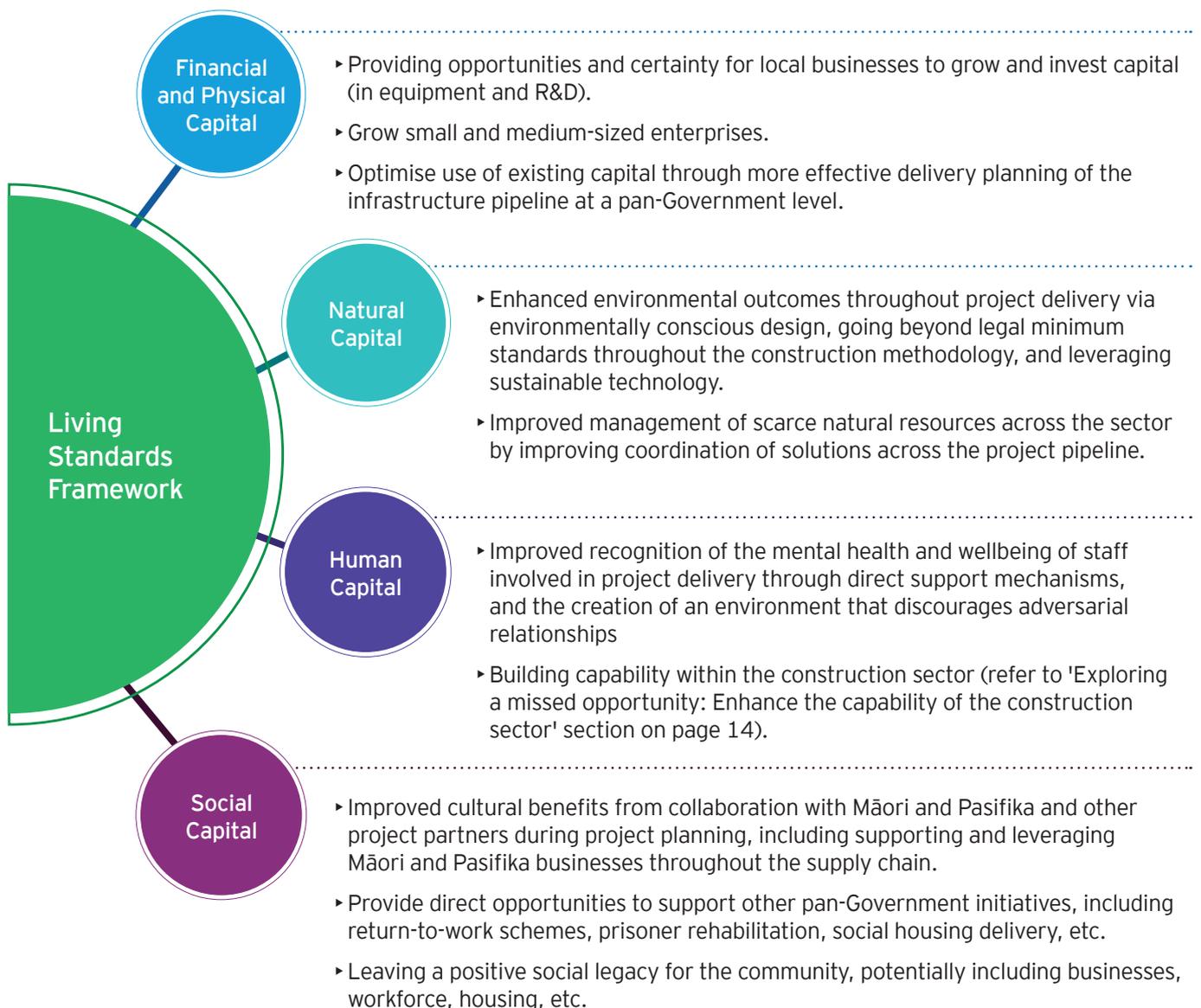
The wide-reaching implications of infrastructure delivery means that a project's outcomes are usually not constrained to a single organisation or sector. The challenge facing New Zealand is to reconsider what may be traditionally regarded as externalities from project delivery as areas of core influence that can be used to progress Government priorities and direction.

The Treasury's Living Standards Framework is one lens through which we can consider the broader public benefits of a major infrastructure project. Traditionally, infrastructure investment would be placed squarely in Financial & Physical capital within this framework. However, in considering the wider outcomes available to procuring agencies from these projects, it is easy to see how infrastructure investment can contribute meaningfully across all forms of capital (i.e. Natural, Social, and Human Capital).

The City Rail Link case study on page 12 outlines one example of how Government agencies have endeavoured to include wider outcomes in major infrastructure procurement.

In relation to delivering broader outcomes through procurement, MBIE has published a range of New Zealand agency experiences across various industries. Links to these case studies are provided in Appendix B.

Table 1: Summary of outcomes from infrastructure procurement across the Living Standards Framework



Source: The Treasury, EY



City Rail Link: Performance framework and Social Outcomes Strategy

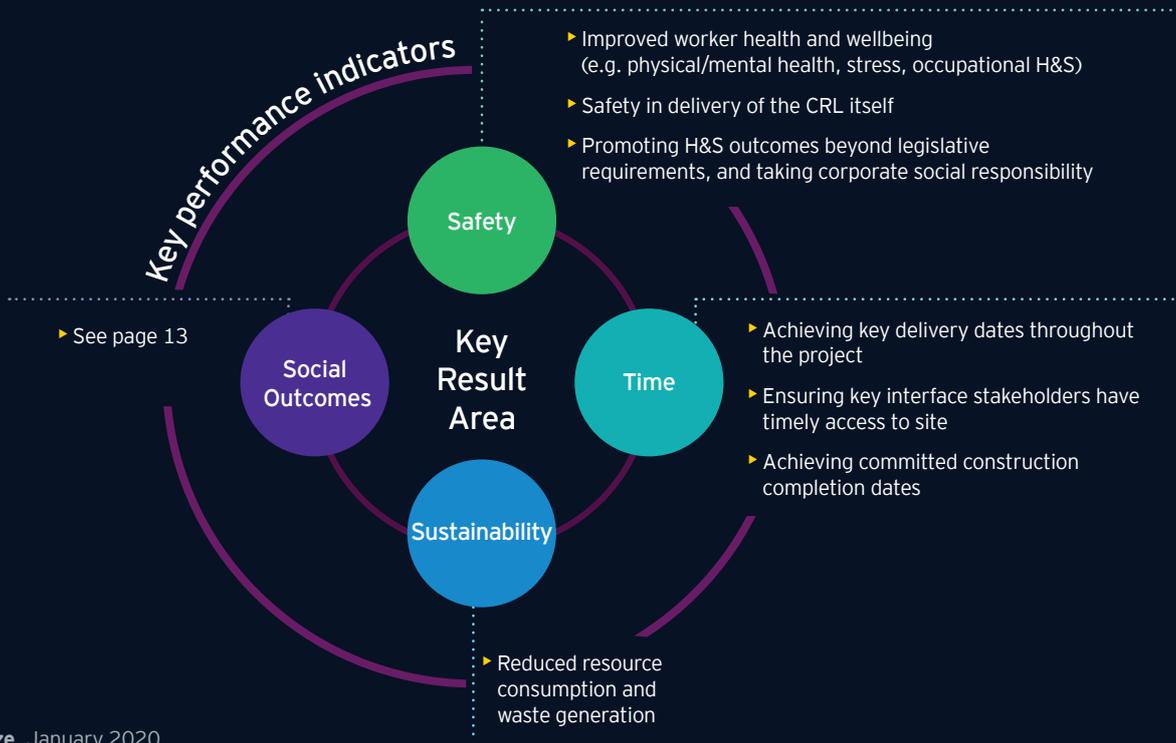
The City Rail Link (CRL) is a transformational 3.45km twin-tunnel underground railway link currently in development beneath the Auckland CBD.

It is expected to improve travel options and journey times across Auckland’s public transport network, and will double the number of Aucklanders within 30 minutes travel of the CBD. The sheer scale and influence of the CRL means the project has the opportunity to create a long-lasting positive impact on Auckland’s businesses and communities.

The largest package of the CRL – delivered under an Alliance model contract – included the design and

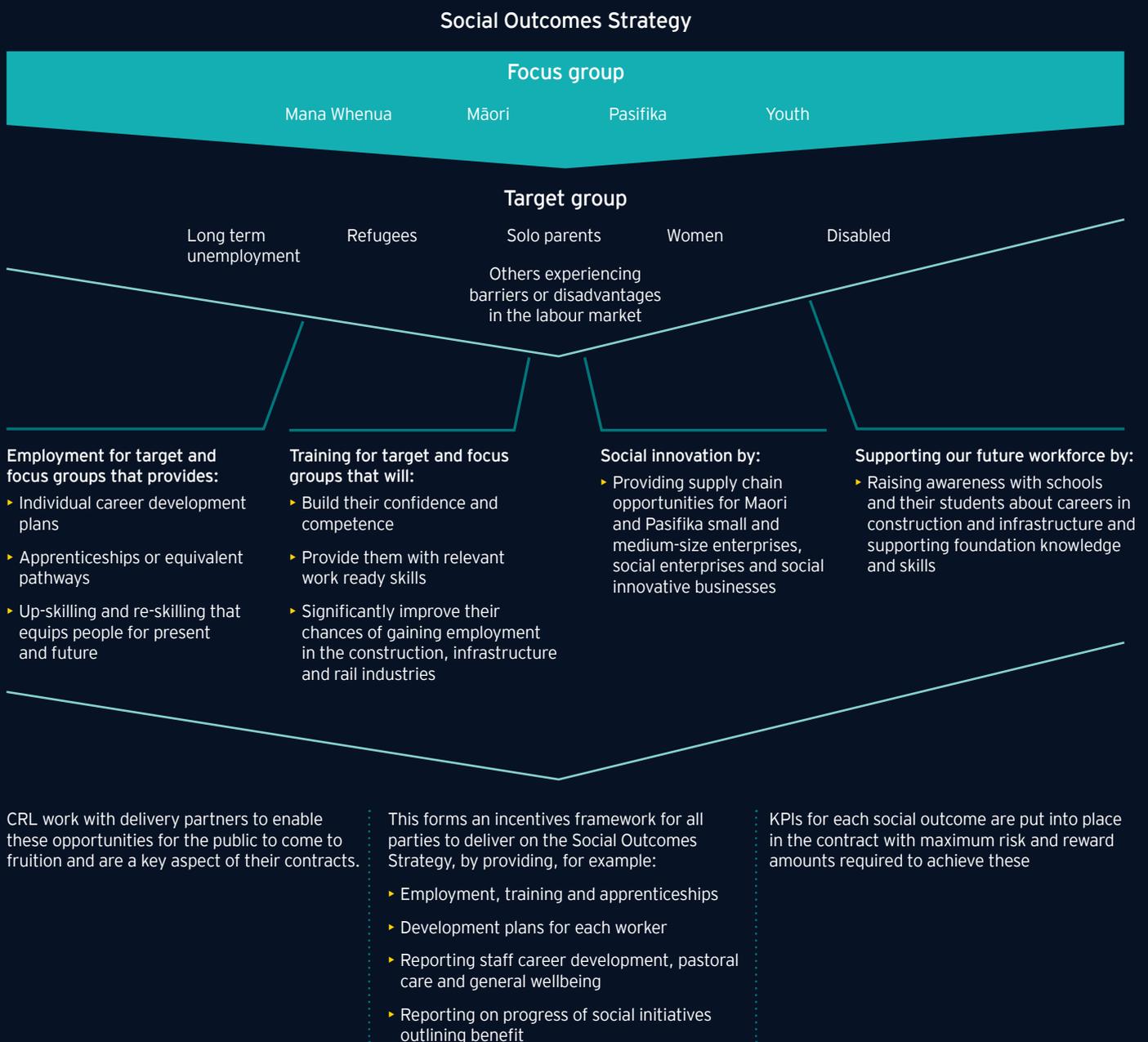
construction of the project’s stations, tunnels and associated rail systems. This collaborative form of procurement cultivated a culture of shared responsibility for the delivery of CRL’s project outcomes.

Several key result areas and performance indicators that extend beyond typical ‘on-time, on-budget’ concepts of success for a major infrastructure project were defined to measure the Alliance’s performance. Under this framework, CRL’s Alliance partners are financially rewarded for delivering exceptional performance in the following areas:

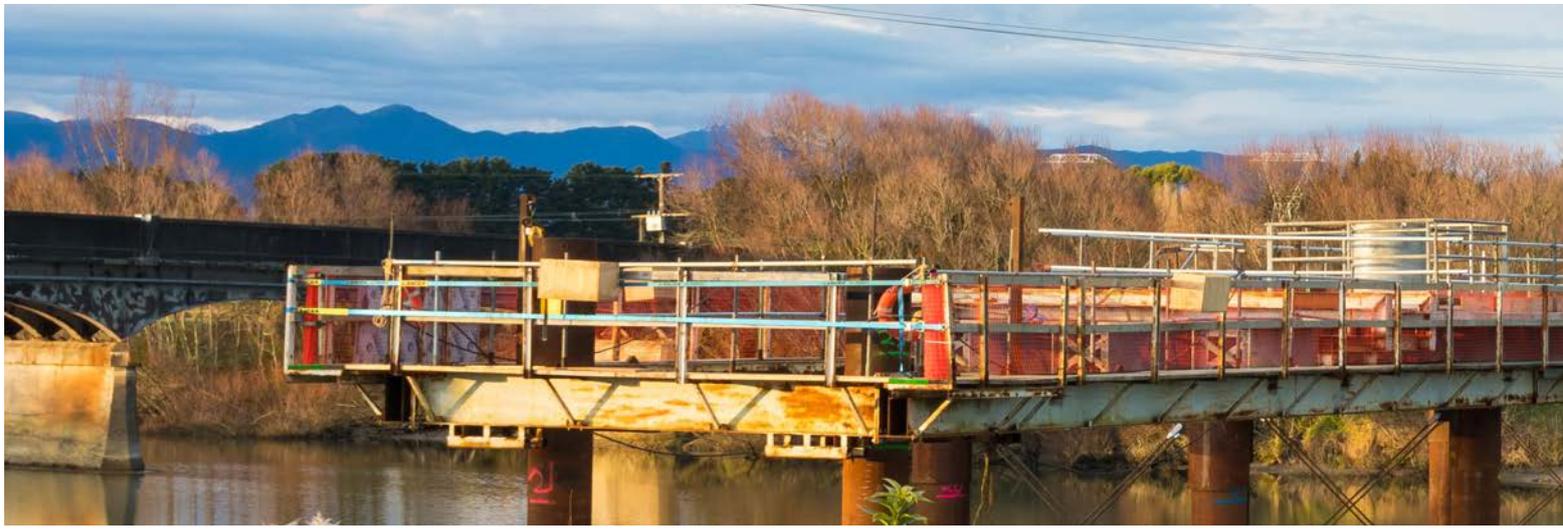


For one of the key result areas, CRL's delivery agency (City Rail Link Limited) established a Social Outcomes Strategy.³ This promoted the public benefits of the project, whilst responding to a number of the New Zealand construction industry challenges.

These include labour and skill shortages, the need for more trades and engineering graduates, and an ageing workforce. At its core, this Strategy is “about people and creating a diverse and inclusive workforce which will benefit Aucklanders and the communities they live in”. The Strategy is summarised in the diagram below.



3. <https://www.cityraillink.co.nz/crl-social-outcomes-approach>



Exploring a missed opportunity: Enhance the capability of the construction sector

Infrastructure should be considered as a pipeline of investments that enables economic and social outcomes. This pipeline should not just be a means for contractors to target the next job, it should represent an opportunity to lift the game of the whole sector – lessons learned, capital acquired, and skills developed in one project can be used to enhance the outcomes of subsequent projects.

The Accord sends a strong signal to the market about the Government's desire to work with the construction sector to improve the overall health and performance of the industry. Both the public and private sector have clearly recognised that the construction industry requires a reset, including to conduct a free and frank assessment of the issues that have led to the challenging conditions in the current market. To put the Accord's principles into practice, the stakeholders need to consider how these issues can be addressed and identify what both the Government and the industry can do to collectively achieve the Accord's goals of increased productivity, better capability, improved resilience and enhanced sector reputation.

The Government, as both a co-signatory to the Accord and one of the largest procurers of infrastructure in New Zealand, must be a driving force to ensure the principles of the Accord are deeply embedded in how agencies plan and deliver their projects from the outset.

Bringing the Accord to life – and hence giving agencies the mandate to explicitly pursue the Accord's goals in practice – will require substantial changes to the budgeting, evaluation and approval processes for New Zealand infrastructure projects. The current infrastructure investment framework is limited in its ability to effectively consider and value the wider public outcomes sought under the Accord. It is therefore difficult for agencies to identify (and hence justify paying for) these outcomes. Improving the health and performance of the construction industry cannot be an afterthought; it must be made a key consideration of the infrastructure investment decision-making process.

The upside is that many of the Accord's goals and principles are not difficult to achieve. The difficulty lies in shifting procuring agencies' thinking about who is responsible for improving the performance of New Zealand's construction sector – the answer, of course, is that as Government representatives, these agencies are themselves jointly responsible under the Accord. If given the right tools and budgetary flexibility to identify and value the wider outcomes sought under the Accord, procuring agencies can effectively achieve many of the Accord's outcomes without compromising their own investment decisions. The table to the right outlines some examples illustrating the approach that a New Zealand procuring agency could use to pursue some of the goals of the Accord within the typical business case and procurement process. These examples do not consider how Budget funding could be adjusted to invest in these outcomes – this discussion will flow naturally once the practical implementation is developed further.

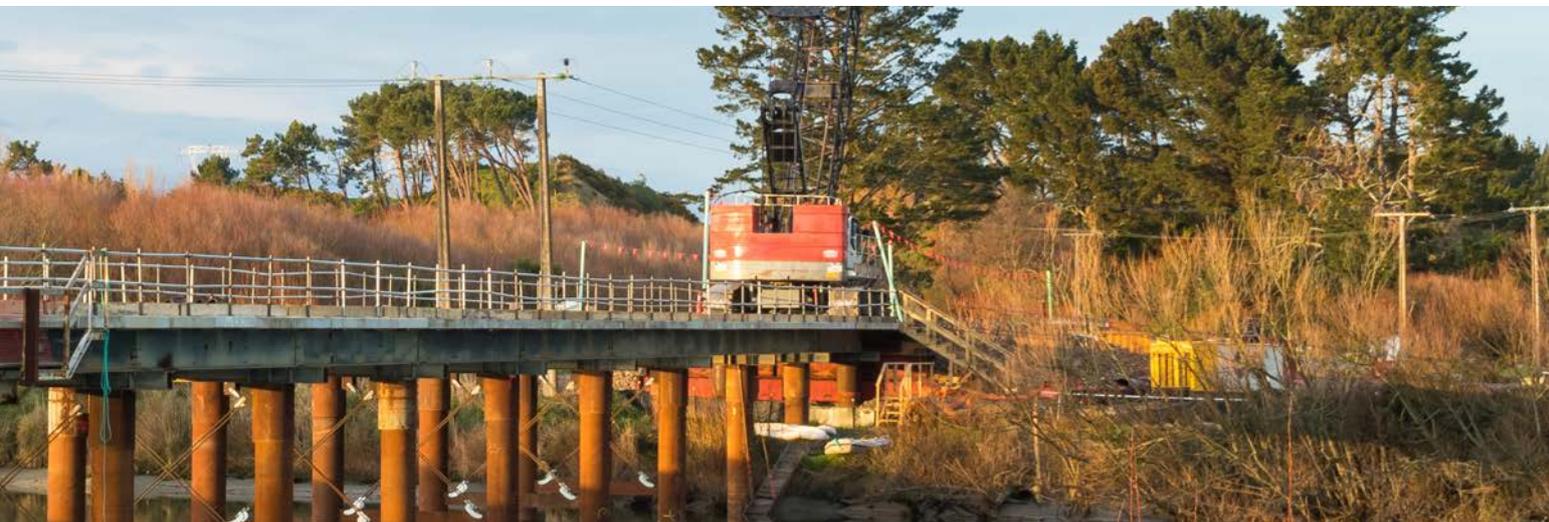


Table 2: Construction Sector Accord and generating broader public values

Shared goals of the Construction Sector Accord	How could a procuring agency achieve these goals?
<p>Increase productivity A productive, value-driven, and efficient construction sector able to produce more for each dollar spent.</p>	<ul style="list-style-type: none"> ▶ Require contractors to invest in R&D (either by paying higher margins or as a tender requirement) ▶ Encourage innovation through collaborative behaviours, early involvement in the design and planning process, or through bid evaluation ▶ Less focus on “lowest-price wins” to encourage quality solutions and higher value outcomes ▶ Increased emphasis on safety-in-design and H&S practices to improve morale and productivity ▶ Collaborative procurement models encourage shared approach to risk management and efficiencies (time, cost, labour, supply chain)
<p>Raise capability A skilled and capable workforce that meets New Zealand’s growing housing and infrastructure needs.</p>	<ul style="list-style-type: none"> ▶ Implement on-the-job training requirements ▶ Requirement to use apprentices ▶ Encourage use of local subcontractors and suppliers ▶ Encourage use of Maori/Pasifika suppliers ▶ Liaison with education providers (tertiary, training, secondary) to encourage education in certain key skills areas
<p>Improve resilience Strong, sustainable businesses with the capacity to innovate and adapt to change and disruption.</p>	<ul style="list-style-type: none"> ▶ Less focus on “lowest-price wins” to allow contractors to earn sufficient margin and avoid insolvency risk ▶ More appropriate and fairer risk allocation ▶ Improve health of subcontractor market (via open-book contracting, appropriate risk transfer, consistent contract terms) ▶ Work with Government and the Commission to provide certainty of pipeline that allows the construction sector to invest in growing resources (labour, plant, technology, management) ▶ Provide contractors with incentives to provide the optimal, and not simply the cheapest, contributions to improve environmental, social and economic outcomes.
<p>Restore confidence, pride and reputation A high-performing, transparent and trusted sector we can all be proud of.</p>	<ul style="list-style-type: none"> ▶ Encourage diversity ▶ Offer longevity and certainty of pipeline of work ▶ Less focus on “lowest-price wins” to encourage quality solutions and reduce adversarial behaviours

Revised Government Procurement Rules

On October 1, 2019, the fourth edition of the Government Procurement Rules was released.⁴ The update includes substantive revisions aimed at bringing to life the Government’s goal of leveraging procurement to achieve wider public outcomes for New Zealand. The new Government Procurement Rules strongly complement the goals of the Accord.

Additionally, this paper aligns with the intentions of the revised Government Procurement Rules, and emphasises the importance of considering public benefits as early as possible, including during (and prior to) the business case process. Of the substantive revisions to the Government Procurement Rules, the table below provides examples of how the Government is starting to integrate broader outcomes into the procurement phase of projects.

Table 3: Elements of changes to Government Procurement Rules reflect focus on wider public outcomes

Rule 16	Rule 17	Rule 18	Rule 19	Rule 20
Consideration of broader outcomes (social, environmental, cultural, or economic) that arise as a result of procurement and delivery of a project	Increase access for New Zealand businesses to procurement opportunities and encourages agencies to involve Māori, Pasifika and regional businesses as well as social enterprises	Suppliers expected to contribute to growth of construction skills and training, to support the expended capability and capacity of the construction workforce	Improving conditions for New Zealand workers, such as protecting workers from unfair and unsafe behaviour and labour practices	Transitioning to a net-zero emissions economy and designing waste out of the system to support a circular economy

4. Ministry of Business, Innovation and Employment (2019). Summary of substantive changes to the Rules of Sourcing.

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This paper aligns with the intentions of the revised Government Procurement Rules, and emphasises the importance of considering public benefits as early as possible.





What are the potential barriers and challenges?

This section explores the additional considerations facing the Government and procuring agencies when determining how best to reshape existing Budget and business case processes to pursue wider public outcomes.

The analytical burden

Exploring and identifying infrastructure investment opportunities is complex, often spanning multiple sectors, public agencies, stakeholders and assumptions. Individual project teams, as they are typically resourced, are unlikely to have the capacity to fully explore the public opportunities available. Moreover, the capabilities required to consider wider public outcomes extend beyond the experience and skill-sets of traditional procurement professionals – the job description is effectively being rewritten.

There are well defined guidelines to help determine the direct benefits that arise from investment in a specific project (e.g. Economic Cost Benefit Analysis: public transport investment will improve travel time by X minutes resulting in \$Y savings per person). However, defining the wider public opportunities that can be created by tailoring how the project can be delivered is largely uncharted territory for typical New Zealand public agencies.

Without defined guidelines outlining the extent to which wider public opportunities should be explored (at the project level), right-sizing the analytical efforts will be challenging. The effort and energy for each project must be commensurate with the public opportunities likely to arise.

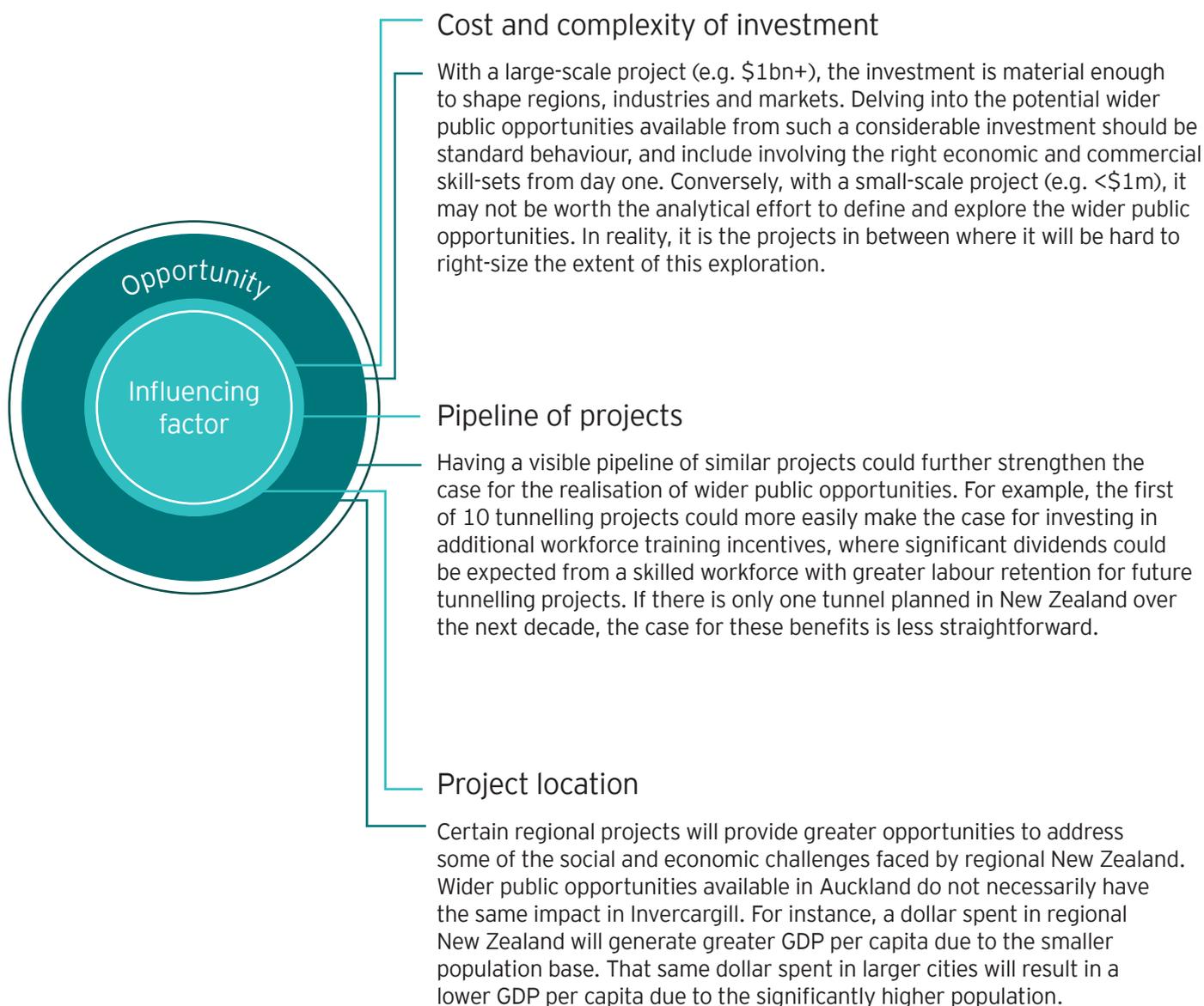
Complexity quickly develops when project teams seek to analyse the marginal opportunities available. Take the example of skills development through a major project – there is some ‘base case’ level of training required regardless of delivery approach, however there is also an opportunity to incentivise greater skill development by increasing training initiatives, which will benefit the future pipeline of projects.

Attributing the cost premium of the training, identifying the value delivered beyond the immediate project, and attributing public benefits between beneficiaries are complex tasks requiring the involvement of a diverse mix of skillsets to explore properly (including commercial and economic analysis).

To determine how far to take the analysis, it is important to look at the potential influencing factors and barriers (set out in Table 4 to the right). Understanding how these apply to a specific project is critical to establishing specifications and focusing the procuring agency's effort on the available public opportunities.



Table 4: Potential factors to consider when analysing wider public benefits/outcomes





Aligning incentives and funding

New Zealand has an opportunity to pivot from considering infrastructure investment on a project by project basis, where achieving wider outcomes is not the responsibility of any single agency and therefore investing in these outcomes is inefficient...

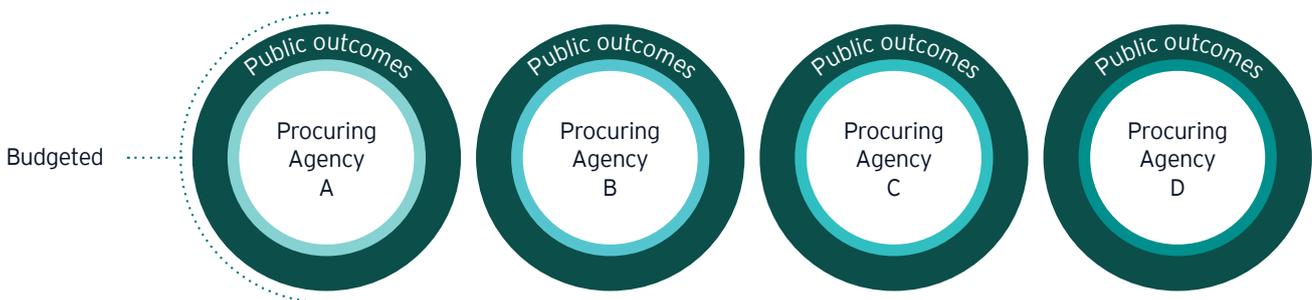
Figure 2: Procuring agencies adopting a “blinkers on” approach



Source: EY

...to an approach where individual agencies are empowered with the opportunity and fiscal resources to deliver these outcomes.

Figure 3: Procuring agencies empowered to deliver wider public outcomes



Source: EY



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Who should pay the 'social premium' necessary to deliver the wider public benefits from an infrastructure project?

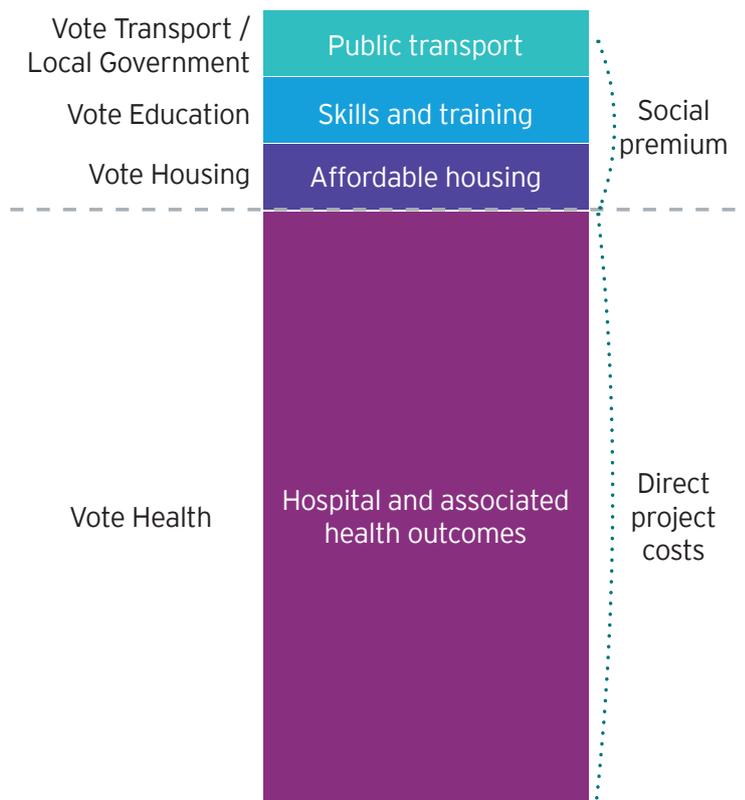
So, who pays the “social premium” necessary to deliver the wider public benefits from an infrastructure project?

Procuring agencies are unlikely to want to fund these wider outcomes themselves, especially if this is at the expense of their own projects. There needs to be a mechanism where funding that would otherwise be allocated to delivering these public benefits, but lacks the sufficient critical mass or an appropriate route-to-market for delivery on a centralised “NZ Inc.” basis, could be prioritised and implemented as part of an individual agency’s investment process. While individual infrastructure projects essentially catalyse this spending and provide an efficient way of directing Government expenditure towards achieving these wider outcomes, in general, the funding of these wider outcomes will need to come from outside the agency responsible for a given infrastructure investment.

The decision on who should pay the cost premium to deliver wider public benefits on day one will likely require amendments to existing Budget and business case processes. Seeking cross-agency funding from Vote teams for projects outside their core sector is likely to be a contentious process. However, to achieve wider outcomes agencies’ thinking needs to evolve from a constrained, project-specific perspective to a pan-Government approach to delivering on the Government’s priorities.

Implementing the right policy changes to allow a transparent, fair, and accountable cross-agency funding process will be a key step in enabling agencies to use their infrastructure projects to deliver wider public outcomes.

Figure 4: Hypothetical Budget allocations to fund wider outcomes on an example hospital project



Source: EY



How could these opportunities be realised?

This section considers a potential approach to planning and delivering wider public outcomes through infrastructure investment. Achieving wider public outcomes requires a mix of incentives, policy coordination and flexibility.

Consideration at a business case level

As part of the revised Government Procurement Rules, all procuring agencies must consider broader outcomes when planning procurement activities. MBIE's guidance on 'Implementing Broader Outcomes'⁵ provides a framework for considering how the procurement of a project can capture broader outcomes. In reality, these considerations are fundamental parts of infrastructure investment that should be considered as early as possible within the project business case process.

This section outlines how a business case could integrate the consideration of broader outcomes and how this aligns with the three key phases identified within MBIE's Implementing Broader Outcomes guidance – Context, Prioritisation and Delivery.

Table 5: Steps for considering broader outcomes in a project business case

Context

- 1 Set objectives that cover the range of project-specific and wider outcomes the project can influence

Prioritisation

- 2 Explore the public opportunities and benefits the project can support

- 3 Analyse and prioritise the public opportunities available

- 4 Inform your procurement model assessment with this knowledge

Delivery

- 5 Explore the public opportunities and benefits the project can support

- 6 Analyse and prioritise the public opportunities available

Source: MBIE

5. Ministry of Business, Innovation and Employment. (2019). *Implementing broader outcomes*.



Context

1 Step 1: Setting Tailored Objectives

The current Better Business Case framework supports agencies to identify the best delivery pathway for a project using a set of objectives that generally fall into one of two categories: (1) investment objectives which focus on the end state (the what) and are met by delivering the preferred option regardless of the delivery approach adopted (the how); and (2) commercial objectives that usually represent general measures such as “fit for purpose”, “cost certainty” and “market capacity” used to differentiate certain aspects of procurement models.

What’s missing? Acknowledgement that how the project will be delivered can shape long-term public outcomes extending beyond the direct sector of investment. By neglecting these considerations, agencies will continue to make procurement decisions that focus on a narrow set of outcomes responding solely to project-specific objectives.

Consider the following commercial objectives that might be adopted for major projects:

- ▶ Enhance the capability and resilience of our construction sector
- ▶ Create a safe and positive working environment for all parties involved in delivery of the project
- ▶ Leave a positive legacy for the people and businesses of the region
- ▶ Move New Zealand forward in areas of environmental sustainability and health & safety

It is important to have the right resources and key decision makers engaged during this step to:

- ▶ Ensure robust objectives are developed that align with agency, Government, and wider initiatives
- ▶ Ensure they are involved as early as possible to provide them with deep understanding of the plans to pursue wider public outcomes.



Procuring agencies need to consider the key areas of influence of their project and how these might impact our economy and society.

Prioritisation

2 Step 2: Explore the public opportunities and benefits the project delivery can support

Since every project will enable a different range of potential public outcomes, procuring agencies need to consider the key areas of influence of their project and how these might have flow on implications into other parts of our economy and society.

Some public benefits will command a cost premium to deliver broader public outcomes. For example, labour costs will be incurred on any project, but agencies would likely need to pay a premium to require contractors to employ a number of previously unemployed workers in their delivery team. While this might not directly benefit the specific project, it builds the capability of the construction sector for future projects and potentially creates public cost savings elsewhere (e.g. through reduced unemployment benefits incurred by the Ministry of Social Development).

Measuring contribution and attribution for these public benefits can be very challenging, particularly when third-party agencies and Vote teams are being asked to contribute funding to a project outside their core sector. Establishing a process for how public outcomes are attributed will be a core part of any revisions to current Budget processes.

3 Step 3: Analysing and prioritising opportunities for the project

Individual infrastructure projects cannot be a silver bullet to achieving all the Government's desired public outcomes. However, they can be very effective at catalysing specific public outcomes so that, in aggregate, the wider New Zealand infrastructure pipeline helps to accelerate a wide range of these societal benefits. As such, the range of potential public outcomes from a given infrastructure investment will need to be analysed and prioritised in order to determine how a particular project can most effectively deliver these outcomes – this will involve the following two steps:

- **Analyse.** Agencies must evaluate how their project can deliver the outcomes identified. For example, if a project presents an opportunity to increase skills and training in the construction workforce, the agency should understand the specific public need and therefore potential benefit potential of a skilled workforce; the size/target number of people to train; and the resources required to meet this opportunity.
- **Prioritise.** Based on the analysis above, procuring agencies should work with stakeholders to rank the opportunities in terms of their importance, achievability and feasibility. Using an economic analysis can support the decision but gets complex quickly. One option could be for agencies to implement disciplined decision-making by using a fixed budget allocation (i.e. if a 10% social premium is being considered, how would it best be allocated?).

These steps will enable the public opportunities of a project to be scaled and will provide decision makers with a deeper understanding of the value and risks that could arise from pursuing wider public outcomes.





4

Step 4: Assess potential delivery approaches against criteria that promote public outcomes

Step 1 above highlighted that wider public outcomes are often neglected when considering which procurement model is optimal for a given project, meaning the opportunity to influence these outcomes through the choice procurement model is missed.

There is considerable potential for a specific procurement approach to help deliver wider public outcomes. For example, agencies could consider using procurement models with increased collaboration as a means to help deliver a fairer risk allocation with the private sector, or implement a specific performance framework that directly incentivises the industry to achieve the social, economic or environmental outcomes prioritised above.

This step seeks to expand the typical set of commercial objectives to also consider broader public objectives along with traditional criteria when assessing procurement models. Agencies would be encouraged to develop “public-benefit driven” commercial objectives that are unique to the project, plus some objectives that may be uniformly implemented across different business cases and sectors.

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It is important to consider wider public outcomes as early as possible, providing a cohesive and consistent case for investment that ensures key decision makers are brought along the journey.



Delivery

5 Step 5: Develop an implementation plan including an incentives framework

As with achieving optimal risk allocation on a project, there are certain parties who are best placed to manage the delivery of specific opportunities within each unique project. Developing an implementation plan to identify the best party – whether private or public sector – to take responsibility for each opportunity can ensure that these outcomes are executed optimally.

However, the commercial reality is that some parties may be hesitant to take responsibility for delivering certain outcomes given the associated costs, complexity, size and risks. To overcome this barrier, encouraging collaboration and implementing an incentives framework can be effective ways of delivering these outcomes. For example, to encourage skills and training development in the construction industry workforce, the procuring agency and its stakeholders could work together to structure a particular project's commercial model to:

- ▶ Increase publicly-funded trade programmes
- ▶ Mandate any contractor to train a specified number of people throughout the programme
- ▶ Incentivise the contractor through a payment bonus per newly trained person
- ▶ Enter a joint agreement for Government and the contractor to delivery specified training outcomes

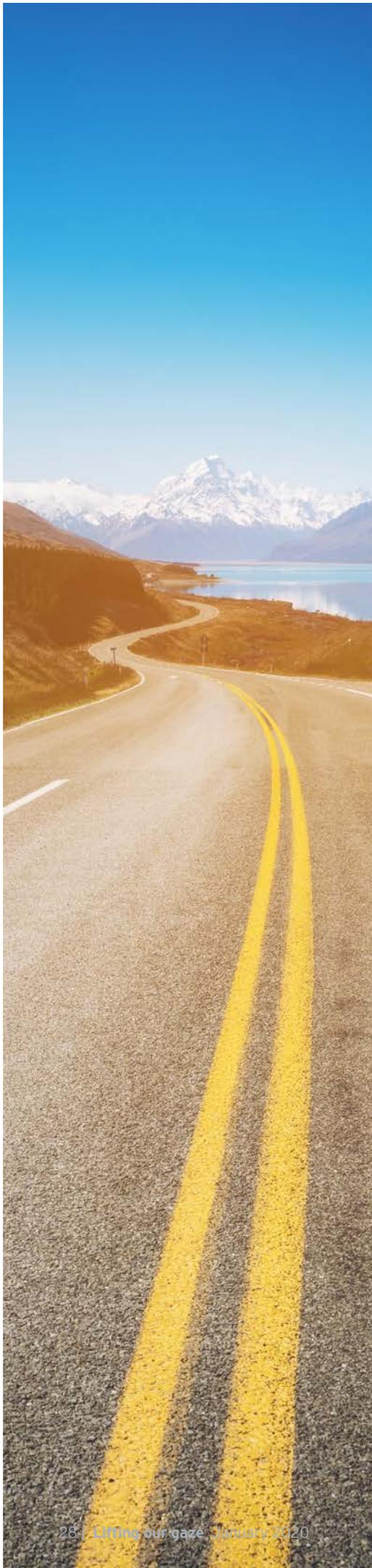
It is important during this phase to explore who is best placed to deliver the opportunity in practice, and what is needed to establish arrangements that facilitate these outcomes. This naturally flows into commercial aspects such as risk allocation, contractual arrangements and governance – fundamental things we need to get right to maximise the opportunities available.

6 Step 6: Revisit other aspects of the business case

Pursuing broader public outcomes within a project will have implications on other key aspects of the business case beyond the Commercial Case. For instance, the following could be influenced:

- ▶ Strategic Case – the potential scope of the investment, including the problems being solved and benefits being delivered.
- ▶ Economic Case – the investments included within the options and the monetisable benefits, costs and risks.
- ▶ Financial Case – the project budget, including any costs directly attributable to achieving public outcomes (and potential funding sources).
- ▶ Management Case – the implementation plan (including incentives framework) that could be adopted to achieve the outcomes and how the delivery structure (including governance and project team) may need to adapt to provide suitable oversight. Critically, the need to resource the project with staff that bring the skills and experience to carry forward the wider public outcomes should be made clear.

The breadth of these implications indicates the importance of considering public outcomes within the business case as early as possible. Early contemplation of these potential outcomes will help to provide a cohesive and consistent case for investment that ensures key decision makers are brought along the journey from inception through to project delivery.



Including wider outcomes within the Better Business Case framework

To effectively improve public outcomes, the approach to adopting an “NZ Inc.” perspective needs to be actively considered throughout project delivery planning. This requires consideration of how agencies can be incentivised and supported to consider these outcomes

The most obvious vehicle for guiding procuring agencies through this process is Treasury’s Better Business Case guidance. An update to the guidance could more explicitly direct agencies to explore how the delivery of their projects will shape the public outcomes delivered. As detailed above, the heart of this discussion may well sit in the Commercial Case but will have flow on implications into other business case areas. Given the analytical effort required in this process, there could be an opportunity to implement hurdle criteria in the business case process, where a project’s size, value or political sensitivity may determine the extent to which agencies are required to explicitly consider and pursue the wider public outcomes available from their projects. This would be similar to existing guidance relating to when agencies are required to explore PPP options within business cases.

Encouraging discussion with the Commission should be a standard part of the analytical process, creating a central knowledge base accessible to various procuring agencies.



An update to Better Business Case guidance could more explicitly direct agencies to explore how delivery of their projects will shape public outcomes.

Pan-Government initiatives

Some opportunities may not be specific to a single project – identifying initiatives (including policy) that could be progressed at a national level to support delivery of the pipeline more broadly.

Consider targeted wage subsidies as an example - a common tool used in an effort to deepen the labour market and target specific groups. New Zealand already uses these subsidies in a limited capacity, but in the US and South Africa they are more common. In the US they are used to move ex-felons and former welfare recipients into work, often in specific sectors (e.g. construction). In South Africa they are used to increase the diversity of the workforce. In both cases, the lessons have been similar: the more targeted the incentive the less effective it is. It appears that highly targeted wage subsidies actually create a level of stigma for job seekers and employers.

Incentives that target programmes to retrain workers and facilitate moves into highly constrained sectors have been more successful. These subsidies are often combined with job retraining programmes – sometimes additionally targeting geographic disadvantage (e.g. in the US Empowerment Zone model) – leading to a reduction in risk in training employees, and higher employment rates. The effects of these incentives are threefold: they deepen the labour market overall because many employees are out of work, they increase regional investment, and they increase overall vocational training levels.

International progress on broader outcomes

A 2015 OECD report, Recommendation of the Council on Public Procurement, recommended more explicit consideration of broader outcomes, including a recommendation for adherents to “develop an appropriate strategy for the integration of secondary policy objectives in public procurement systems”.

A 2019 OECD report presents the progress made in Reforming Public Procurement. This report showcases substantial progress globally in moving forward public procurement processes to go beyond the purchase of goods and services.

The paper outlines a number of international successes in adopting strategies to integrate broader outcomes in procurement, for example:

- ▶ Norwegian procurement processes include new provisions for contracting authorities to improve sector outcomes by specifying a maximum number of subcontractor levels in the supply chain or mandating the use of apprentices.
- ▶ Australia’s Indigenous and Procurement Policy requires Australian Commonwealth entities to award 3% of their contracts to indigenous businesses.
- ▶ The Canadian federal CPB, Public Services and Procurement Canada (PSPC) requires suppliers and their first-tier subcontractors to certify that they comply with a list of eight fundamental human and labour rights principles each time they bid.



6 Has this been done elsewhere?

This section explores how wider outcomes have been successfully incorporated into infrastructure investment processes in other jurisdictions.

New Zealand procuring agencies are starting to consider how to address the issues outlined in this paper, with some agencies well ahead of the curve in incorporating specific “social procurement” policies in their procurement processes. While there is no doubt that these policies are being adopted with positive intentions, the strategic drivers for their adoption are seldom supported by analytical evidence.

For instance, New Zealand has recently seen a number of construction contracts that include incentives (contractual obligations or KPIs) to support training outcomes.

However, the magnitude of the training requirements in these contracts is often arbitrary and the objectives it is intended to support ill-defined. A consistent and coordinated approach would improve the visibility between action and outcomes, supporting more balanced investment decisions. The Victoria State Government has recently adopted a framework that is similar in nature to the one contemplated in section 5. The case study to the right outlines the Value Creation and Capture (VCC) framework and how it integrates with the business case process.

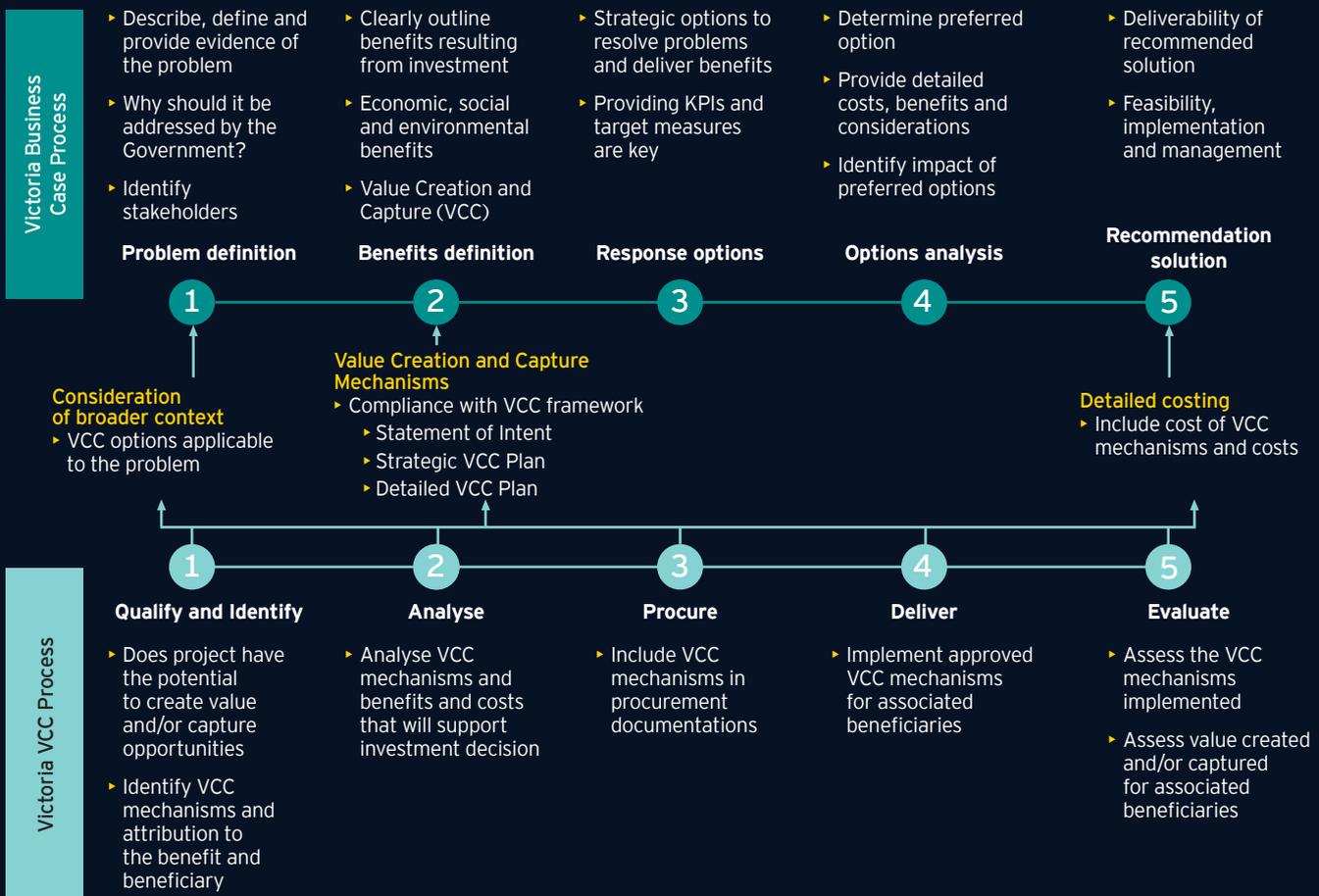


Victoria Value Creation and Capture framework

Victoria's VCC framework was launched in late 2016 and seeks to encourage government project sponsors to maximise environmental, social and economic value. This is achieved by requiring agencies to consider VCC opportunities that maximise public value beyond the core scope of the project, while also ensuring that the selected opportunities remain secondary to project needs.

The framework was developed by the Department of Premier and Cabinet (DPC), which helps to provide guidance, is responsible for identifying which projects must comply with the framework and is involved in the approval process.

The framework seeks to cultivate value creation opportunities that respond to identified needs, extend the focus of individual project objectives, and deliver net benefits that are both feasible and financially sustainable.^{6,7}



6. Department of Treasury and Finance Victoria (2019). Long form business case template.

7. Victoria State Government (2019). Victoria's Value Creation and Capture Guidelines.



Ultimately, the framework should be aimed at incentivising procuring agencies to make value-enhancing commercial and economic decisions.

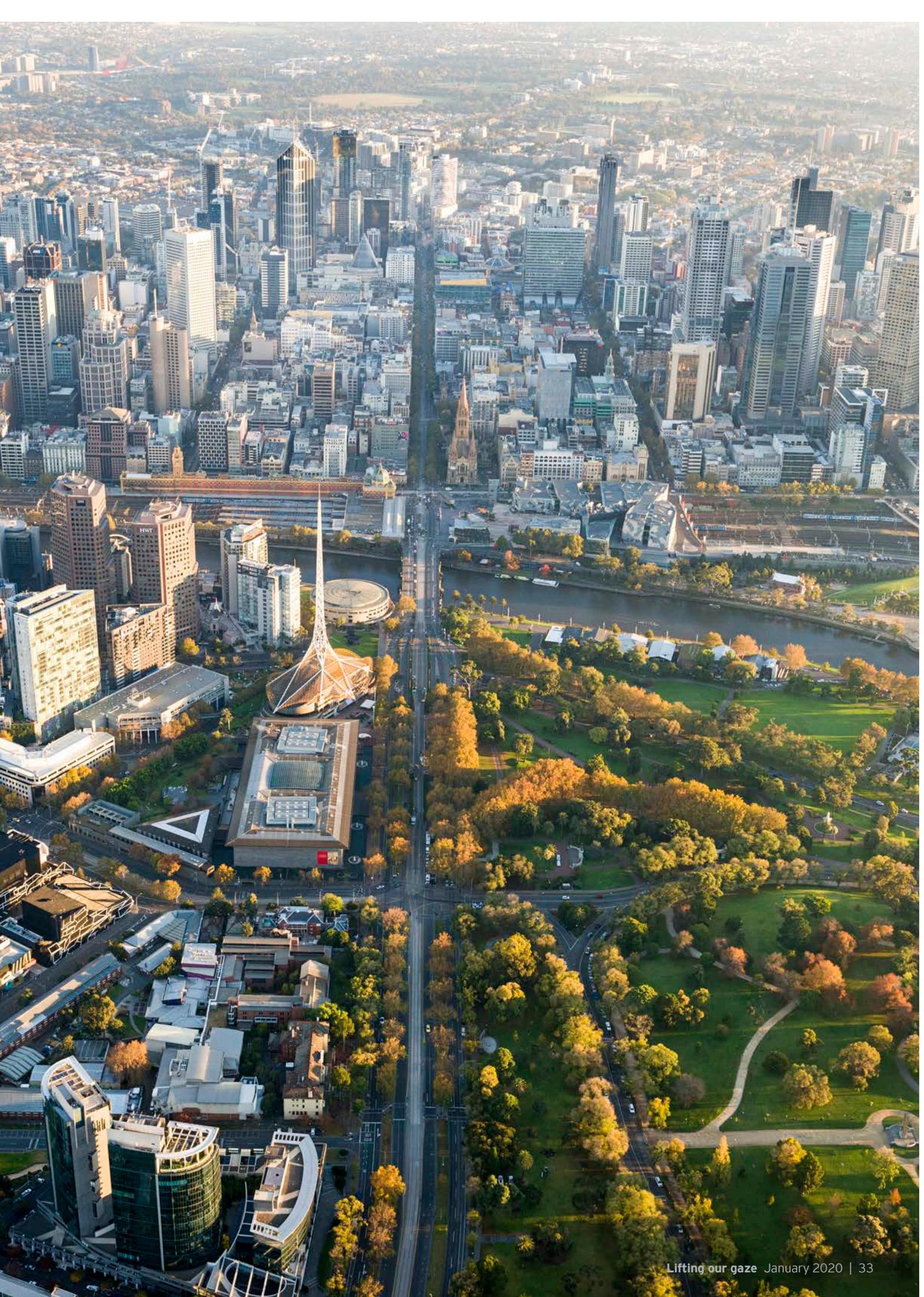
The VCC framework promotes the involvement of commercially-minded individuals from day one of the project planning. It also relies on implementing a highly consultative process across agencies to inform the original development, refinement and ultimately the allocation of delivery responsibilities. These are desirable characteristics that New Zealand agencies should seek to replicate when considering how to pursue wider public outcomes within New Zealand infrastructure investment.

There are some areas where the VCC framework differs from what is being contemplated in this paper. For example:

- ▶ The VCC framework does not distinguish the “what” from the “how” in project delivery, and therefore would not capture a number of the benefits (and disbenefits) contemplated in this paper, particularly relating to construction sector outcomes.
- ▶ The wider public outcomes considered in this paper are broader than the commercial outcomes typically explored in value capture. Therefore, the involvement of a wider pool of specialists may be involved in these early discussions (including economists, sector experts, etc.).
- ▶ The form of the VCC framework means the opportunities are considered in parallel to the business case process. This paper proposes adoption of these principles within the business case framework to encourage increased alignment and improved behaviours within the core project team.

One of the challenges in implementing a successful framework for considering wider outcomes is the need to ensure it is not seen as simply a compliance exercise, where procuring agencies tend to adopt a tick-box approach. Ultimately, the framework should be aimed at incentivising procuring agencies to make value-enhancing commercial and economic decisions – requiring that the right people be involved and the right questions be asked throughout planning and delivery. This means a focus on changing behaviours and cultures, rather than a focus on standardised solutions to diverse project challenges.

It is clear that when implemented well, a framework for assessing and delivering wider public outcomes can be integrated tightly with – or form a core part of – the business case process. Exploring the potential for New Zealand’s Better Business Case framework to explicitly consider wider public outcomes is a key next step in investigating how New Zealand procuring agencies can use their infrastructure projects to deliver these outcomes.





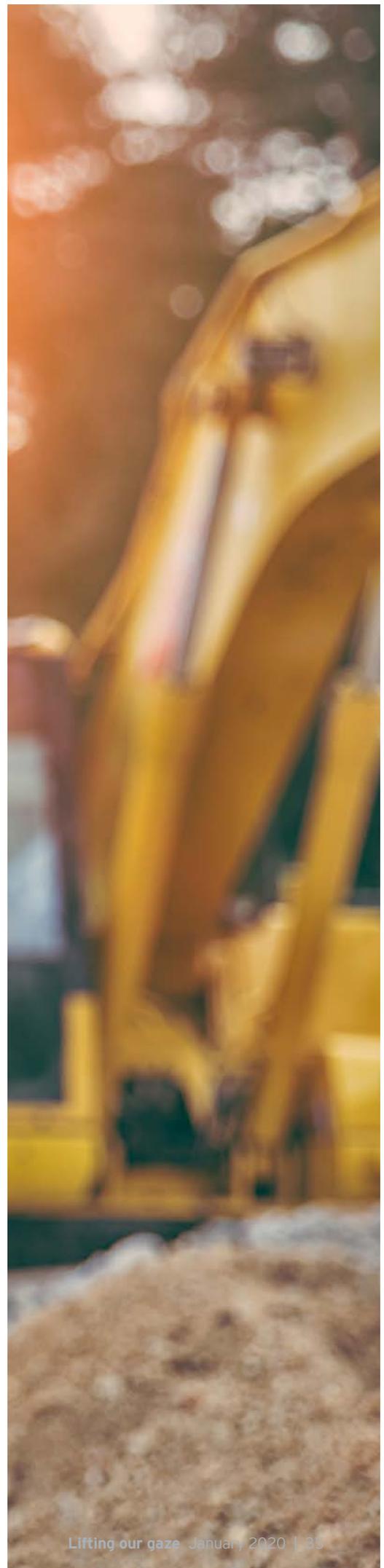
7 Next steps

Lifting the gaze of New Zealand procuring agencies will require a combined effort across Government, the construction industry and the wider infrastructure community.

The shift in mindset required to consider infrastructure investment from a pan-Government perspective will likely require a substantial challenge to the current Budget and business case processes through which infrastructure is planned and funded.

The first step is to begin engaging with the major players in the sector (e.g. the Accord Steering Group, Treasury (including the IMAP and Vote teams) and major construction industry participants) to better understand their perspectives on how delivering wider public outcomes can be effectively folded into the infrastructure delivery process. Later consultation could be expanded to include large capital-intensive procuring agencies, MBIE, local government, etc.

The potential size of the opportunity – i.e. the wide range of public outcomes that could be delivered faster and more efficiently through major infrastructure procurement – is significant enough to get the attention of the public and private sectors. There is simply too much value being left on the table through New Zealand's current project-specific approach to infrastructure investment.



Appendix A

New Dunedin Hospital case study

The New Dunedin Hospital project is currently being planned by the Ministry of Health (the 'Ministry') and involves a complete rebuild of the largest tertiary hospital in the Southern District Health Board's region.⁸ With an estimated capital cost of \$1.4bn, the project is New Zealand's largest ever vertical construction project and will be a significant disruptor to the Southern District health system, the New Zealand construction sector and the wider Dunedin economy.

During recent engagement with the construction industry as part of developing the New Dunedin Hospital business case, there was consistent feedback from construction contractors and subcontractors on the shortcomings of current public-sector procurement and delivery practices on major projects in New Zealand. It is not surprising that many of these concerns – including adversarial contracting relationships, inappropriate risk transfer to the private sector, unsustainably low profitability and limited visibility on pipeline – have also been recognised by the Government and are captured within the guiding principles of the Accord. By taking steps to achieve the shared goals outlined in the Accord, the Ministry has the potential to not only address some of the issues raised by the construction industry, but create a contracting environment in which the New Dunedin Hospital can help deliver a wide range of social, economic and environmental outcomes that are otherwise unavailable under the status quo.

Building a large hospital in a relatively small city was always going to have significant implications for Dunedin. In addition to the direct health outcomes attributed to the New Dunedin Hospital, introducing a significant construction workforce to the city will impact everything from housing to tourism to traffic congestion to school rolls to the local hospitality industry, and will have wide-reaching effects on the national construction pipeline as a result of the project's drain on resource and supply chain capacity.

However, many of the core benefits and disbenefits of delivering the project are realised more or less independently of the Ministry's choice of procurement strategy and should already be considered as part of an economic assessment under Treasury's Better Business Case guidance. To access the wider outcomes available from delivering a project of this magnitude – including those outcomes that are explicitly sought under the Accord, the new Government Procurement Rules and the Government's wellbeing framework – the Ministry has the opportunity to consider how the project's commercial framework (e.g. collaborative procurement models, performance measures and governance structures) can be used to leave a strong positive legacy for the construction industry and the people of Dunedin.

8. <https://www.newdunedinhospital.nz/>

Examples of the broader outcomes which could potentially be supported by the New Dunedin Hospital project:

- ▶ Increased collaboration between Government and market to encourage transparency, trust, reduced conflict and reduced legal challenges
- ▶ More efficient and effective risk allocation, enhancing sector stability and sustainability
- ▶ Incentivising better construction sector performance – productivity, H&S, innovation, asset longevity and quality, etc.
- ▶ Encourage social procurement – for example environmental outcomes, training, Maori/Pasifika employment
- ▶ Build regional capability to support the future infrastructure pipeline
- ▶ Provide positive impacts to the local community (and protecting from adverse impacts), for example in the housing market

Consider the following two hypothetical pathways for how the New Dunedin Hospital might be delivered and the outcomes it could achieve, which are described in further details on the following pages.

- ▶ **Pathway 1: A “blinkers on” approach to project delivery:** The first is where the new hospital is delivered under a traditional (construct only, or design & build) procurement model that focuses only on achieving direct health outcomes and core benefits from the new facility.
- ▶ **Pathway 2: Adopting a broader outcomes mindset to project delivery:** The second is where the Ministry pursues a collaborative contracting model that, in addition to delivering the hospital itself, allows it to identify, price and influence a set of wider public outcomes that improve the performance of the construction industry and are aligned with Government priorities.





Hypothetical Pathway 1: A “blinkers on” approach to project delivery

The following represents a fictional scenario describing how the New Dunedin Hospital could be delivered under traditional procurement without actively considering wider outcomes.

Off the back of the IBC, which set an indicative programme and budget for the project, work continues to refine the design of the hospital facility. The Ministry appoints a well-qualified Design Team to develop a solution that meets its clinical needs. As the largest procurer of health infrastructure in New Zealand, the Ministry is confident that it is well placed to own the design right through to completion, at which stage it will procure a contractor to build the facility. The Ministry’s Design Team continues to progress design right up to the end of Detailed Design, with input from Southern DHB.

In parallel, the Ministry works with its legal advisors to develop a standard form contract for the project, including a number of special conditions that ensure the Government’s interests are protected from as much risk as possible, with little consideration of which party is best placed to mitigate them. The proposed risk allocation reflected within the contract is the same as previous hospital builds – which all attracted multiple bidders.

As design is completed, the Detailed Design and contract are issued to the market and a two stage competitive process is run. While some of the Ministry’s ambitions for aspects of sustainability, H&S, innovation, etc. are considered within the evaluation process, delivering the project on-time and on-budget is communicated as the most important measure of success.

The market is surprised by the scale and timing of the tender, and with such short notice some bidders are unable to compile a competitive bid. However, a short-list of two lead contractors is successfully identified to proceed to the RFP phase. The contractors also work in the background to secure firm commitments from local subcontractors and suppliers. To protect against these subcontracts being given to new market entrants, the locals sign up to relatively low prices and unmanageable risk positions.

A preferred bidder is selected based on a compelling fixed price. As delivery of the project goes from a possibility to a certainty, there is a temporary but large influx of workers and resources into Dunedin to complete the largest vertical construction project in the country. These workers are mostly from other regions in New Zealand and overseas, where the experience in delivering hospital projects lies.

Subcontractors entering the Dunedin market act quickly to buy and rent local houses for their workers for the duration of the project – house prices rise quickly and soon much of Dunedin’s housing supply is over-priced for local purchasers and renters.



The contractor is focused on getting started and reaching the first of the key construction milestones. It continues utilising familiar supply chains and construction methodologies as there is insufficient lead time to employ innovative building techniques such as pre-fabrication. Similarly, goals around sustainability and environmental outcomes, while considered in the RFP process, remain a secondary consideration to delivering the construction works on-time and on-budget.

Shortly into the construction phase, many of the consultants within the Ministry's Design Team hit the caps of their fixed price contracts and withdraw key personnel from the job. Meanwhile, the contractor is finding much of the design documentation to be incomplete and lacking in practical buildability. Subcontractors ultimately find themselves having to complete the documentation which leads to a strain on the project budget and programme.

Project contingencies quickly become depleted. Contractors begin losing margin and disputes emerge between the Ministry and the contractor about the ongoing quality of documentation and the alignment with the agreed risk transfer. These adversarial relationships create tension on the site and delay payment requests, with cash flow issues begin to weigh on contractors and subcontractors.

Upon the completion of the new hospital, much of the workforce leaves Dunedin to return to either their home city or the location of the next 'mega project', taking their experience and learnings with them and leaving Dunedin with no legacy or improvement in skills. House prices and rents plummet, leaving those that remained in the market out of pocket – particularly hurting recent first home buyers.

At the time of completion, the next programme of works is announced in the Otago region, including major projects by the University of Otago, Ministry of Education and Dunedin City Council. Without any earlier certainty of these projects, the local subcontractors again find themselves underinvested and without the skilled workforce required to deliver these projects on a standalone basis in the region. The procuring agencies experience RFP submissions with high bid prices and extended delivery programmes as a result of the lack of market depth in the region and need for additional imported skills.

Hypothetical Pathway 2: Adopting a broader outcomes mindset

The following represents a fictional scenario describing how the New Dunedin Hospital could be delivered under more collaborative procurement with active, cross-agency consideration of how the project can achieve wider outcomes.

The Ministry recognises the scale of the New Dunedin Hospital project and the significant pipeline of projects planned in the wider region. In response to this, the Ministry uses the business case process to identify and analyse broader public benefits that can arise as a result of the new hospital.

The Ministry works with other procuring agencies and the construction sector to identify skill gaps, develop detailed resourcing requirements, and invest in skills development programmes (apprenticeships, on-the-job training, university and polytechnic programmes, etc.). Engaging with relevant organisations at this early phase provides an opportunity to build partnerships and inform long-term planning decisions.

The analysis indicates some labour will be required from outside the region and the Ministry identifies value in providing worker accommodation to protect the local property market from major price swings. Conversations with the Ministry of Housing and Urban Development (HUD) reveal that part of its strategic plans are to invest in high-density accommodation in the Dunedin CBD, close to the hospital site. A Memorandum of Understanding (with cost share agreements) is signed whereby the Ministry agrees to develop accommodation buildings in parallel to foundation works, using them as an opportunity to train the hospital's foundation works local construction workers. Subsequently, the Ministry uses the buildings to house workers for the duration of the hospital's main works contract.

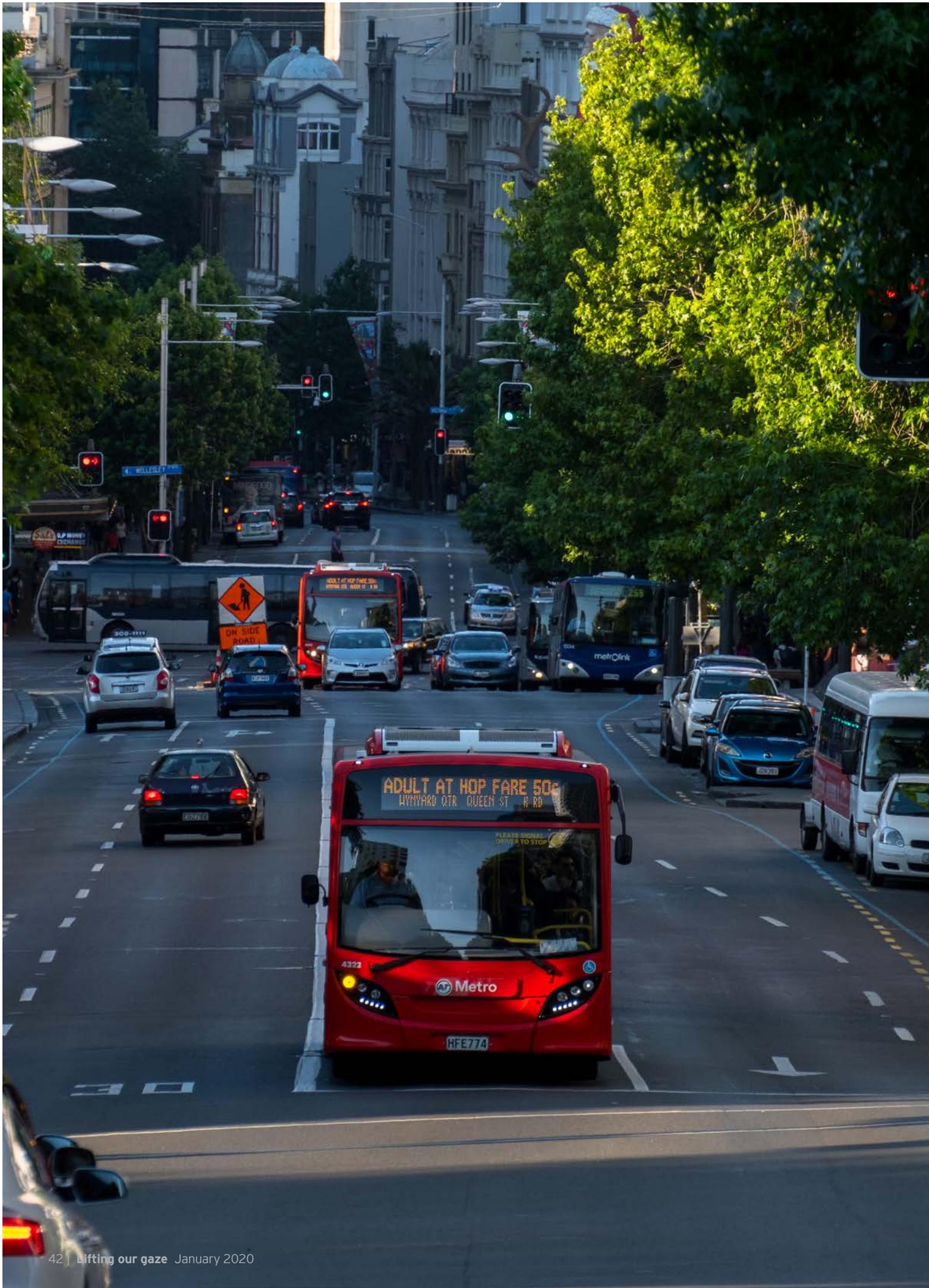
When planning its procurement process, the Ministry adopts a collaborative approach to leverage the expertise of the private sector, encourage innovation and proactively address risk allocation. This includes early involvement from industry to inform the design and construction methodology. Underpinning the process is a performance framework which creates shared goals for the client, the Design Team and the contractors.

The market is given notice of the procurement process and feedback is sought advance notice on the intent and deliverables of each procurement phase to enable the Ministry to refine its approach. The market is eager to meaningfully collaborate with the Ministry to influence and develop a robust solution for all parties.

The Ministry encourages transparent subcontracting arrangements and pricing – acknowledging that it is willing to pay a premium if bidders illustrate a commitment to improving productivity by investing in skills, training, innovation and promoting better contract practices. Investment in these commitments benefits industry (and the public sector) in the long-term due to greater sector stability and capability.

When the contractor is appointed, there is in-built lead time before work is scheduled to start on site. The contractor uses this time to work with the Ministry to progress some of the ideas raised in the competitive procurement process, including to leverage prefabrication solutions that spread capacity requirements beyond the region and initiatives to reduce environmental impacts.





It also works to begin mitigating some of the project's key risk areas – building a skilled workforce and developing housing solutions that align with HUD plans.

The contractor is incentivised to integrate with the local community (including Māori and Pasifika) and adopt an approach that appropriately respects and advances the region. KPIs are used to encourage innovative approaches to environmental, H&S, cultural and social outcomes.

A small Māori owned business, historically overlooked for large contracts due to its lack of capital equipment, is appointed early in the delivery programme to work with the contractor to scope up the project needs. The programme duration and certainty of work enables the business to invest in the necessary equipment for this project – also positioning them to bid competitively on future projects and continue to grow organically.

Moving through the construction phase, a “one team” approach is adopted for project decision-making. Transparent sharing of risks and rewards fosters trust between the Ministry and construction industry and creates a common incentive to minimise costs. Decisions are made on an informed basis, with trade-offs between various financial and non-financial outcomes a standard component of change requests.

Before completion of the project, procuring agencies coordinate and communicate the forward-looking pipeline of infrastructure projects. Local contractors and their staff, who have gained experience from the new hospital, can apply these skills and learnings to future projects. Some experienced personnel choose to remain active in the local Dunedin market while other specialist subcontractors are attracted to the Ministry's projects in Christchurch and Nelson.

At project completion, the high-density housing developed to support worker accommodation is handed over to HUD. This enables HUD to retire obsolete stock elsewhere, improving the living environment provided to in-need families.

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Glossary

Agency or Procuring Agency	A public sector entity (e.g. Government Ministry, Department, Crown entity, non-public service Department, local Government entity, etc.) that is responsible for the procurement of a major infrastructure project; specifically, those staff involved in the development and internal approval of the project business case and procurement process. May refer to multiple entities if the delivery of the project is a joint mandate or partnership.
Broader Outcomes	Defined in the Government Procurement Rules as the secondary benefits which are generated due to the way goods, services or works are produced or delivered. They include economic, environmental, social, and cultural outcomes.
Business Case	A management document that supports decision-making for an investment, such as an infrastructure project. It sets out the case for investment in a specific project, considers alternative solutions, identifies assumptions, constraints, benefits, costs, and risks and sets out potential funding structures and commercial arrangements.
Commission	The New Zealand Infrastructure Commission – Te Waihanga
Government Procurement Rules or the Rules	Standards of good practice for Government procurement as published by the Ministry of Business, Innovation and Employment, many of which are mandatory. The 4th edition published in October 2019 contained substantive revisions aimed at bringing to life the Government's goal to leverage procurement to achieve wider public outcomes for New Zealand. https://www.procurement.govt.nz/procurement/principles-and-rules/government-procurement-rules/
Infrastructure	Fixed, long-lived structures that facilitate economic performance and wellbeing. Infrastructure includes buildings and physical networks (principally: transport, water and energy), social assets such as hospitals and digital infrastructure such as mobile and broadband infrastructure.
MBIE	Ministry of Business, Innovation and Employment
Procurement	All aspects of acquiring and delivering goods, services and works. It starts with identifying the need and finishes with either the end of a service contract or the end of the useful life and disposal of an asset.
R&D	Research and development



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