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TITLE:	Implementing the Early Intervention Investment Framework: A Report to the Victorian Department of Treasury and Finance
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SERIES:	ANZSOG Research Insights
NUMBER:	23
DATE:	May 2022
PUBLISHER:	Australia and New Zealand School of Government
ISSN:	2653-7281
DOI:	10.54810/STBQ7161
CITATION:	ANZSOG. *Implementing the Early Intervention Investment Framework: A Report to the Victorian Department of Treasury and Finance: ANZSOG Research Insights No. 23*. Melbourne: Australia and New Zealand School of Government, May 2022.

ANZSOG RESEARCH INSIGHTS

Implementing the Early Intervention Investment Framework

Australia & New Zealand School Of Government

ANZSOG

Implementing the Early Intervention Investment Framework

A report to the Victorian Department of Treasury and Finance

10 May 2022

1. INTRODUCTION

The Victorian Department of Treasury and Finance (DTF) is implementing and refining the Early Intervention Investment Framework (EIIF), a new budgeting tool designed to guide investment in early intervention initiatives with rigorous quantification requirements. The EIIF seeks to facilitate a robust evidence base for better decision-making and collaboratively developed, quality proposals that deliver avoided costs and better outcomes for Victorians. DTF has engaged the Australia and New Zealand School of Government (ANZSOG) to develop a research and practice paper to aid in the refinement and implementation of the EIIF.

This paper considers what the most effective features are for the EIIF to support budgetary decision making on long-term social services investments, and what is required to realise this. It does so with a focus on the feedback loop that exists between the technical aspects of the EIIF – the systems and tools within the budgeting process and broader government – and organisational and individual behaviours and attitudes, as well as the changes that will support the implementation of the EIIF and continue to build it long-term.

We have drawn on the government and budget experiences of ANZSOG staff, findings from a high-level review of practitioner and scholarly literature (at Appendix 1) and interviews from senior officials[1] from the Commonwealth Department of Finance, Victorian Department of Treasury and Finance, New South Wales Department of Treasury and Office of Social Impact Investment (OSII), and New Zealand Department of Treasury who have direct knowledge, experience and insight in how programs with similar objectives have been implemented (albeit not at the same funding scale facilitated through EIIF). This evidence base broadly concludes that cultural and behavioural factors such as shared purpose, trust, and accountability are central to successful cross-boundary collaboration and long-term budgeting.

This paper aims to generate discussion and learning within DTF and, in turn, the Victorian Public Service (VPS), encouraging individuals to consider the work still do be done to steward the successful and sustainable implementation of the EIIF. This paper draws out practical next steps for DTF that will have the greatest impact in improving processes and behaviours to bring about better outcomes through more effective application of the EIIF and better allocation of resources.

2. THE EARLY INTERVENTION INVESTMENT FRAMEWORK

A conventional view of budgeting processes tends to focus on department-specific initiatives, rather than initiatives that span multiple departments, with an emphasis on addressing acute, immediate problems. This view contributes to inefficiencies like duplicated effort with a lack of consideration of cross-departmental impacts with programs assessed on a department-basis

[1] A methodological limitation of our paper and its findings is that our interviews were solely with officials from central financing agencies. Consequently, we strongly recommend that any next stage in refining and implementing the EIIF involve engagement with line agencies to facilitate understanding of their perspectives on the EIIF, peer-to-peer discussion and mutual learning.

rather than their overall merit. Additionally, it misses opportunities for pre-emptive, integrated responses which seek to prevent the issues becoming acute

This aspect of inefficient fiscal management is exacerbated by a lack of relevant and agreed information needed to make informed decisions about the effectiveness of a program, one of the critical elements needed to inform decision making to prioritise funding for initiatives with the greatest impact for citizens and the service system.

Other factors, such as the fiscal impact of the COVID-19 pandemic stimulus and a pre-existing trend towards acute costs growing above population, can further enhance the need for both greater efficiency and services that address the acute impacts of a range of societal problems.

A well-designed mechanism is a necessary precondition to addressing these two situations. The EIIF is one such mechanism. Announced in the 2021-22 Budget, the EIIF is being implemented to guide the Government's budget consideration of early intervention programs. The EIIF operates on the principle that effective early intervention services can lead to better client outcomes and reduce the need for acute downstream services, meaning avoided costs in the future. The EIIF links investment with the quantifiable impacts of an intervention program. When making a case for EIIF funding, line agencies are required to quantify the impacts of an initiative in terms of:

- **Improved outcomes:** the quantified impacts across select outcome measures on the lives of service users and their families, the broader community, and the service system e.g. increased workforce participation, reduced recidivism rates, increased social connectedness; and

- **Avoided costs:** the monetised value for Government of the expected reduction on future acute service expenditure compared to the expected trajectory if an early intervention initiative did not take place e.g. reduced emergency department presentations, reduced hospital bed days, reduced demand for housing assistance.

The EIIF has created a change in the way DTF and line departments engage. DTF is working with line agencies to identify and refine outcome measures and annual targets, ensuring that they are well-defined, based on a variable that can be monitored and measured, and demonstrate a causal link between action and outcome. This reaffirms that a central financing agency's role is not just to say no to proposals, but to promote better policymaking and proposals that ultimately provide greater benefits for citizens.

DTF has also made considerable progress in developing avoided cost budget guidance to assist agencies in setting the parameters and framework for avoided cost estimation under the EIIF. These include defining the proposed cohort, specifying how the initiative will impact the lives of this cohort, and estimating the cost of initial and downstream reduction on service demand. This is a collaborative process that facilitates the production of reasonable and more consistent measurement across EIIF initiatives.

Agencies provide regular reports on the progress of EIIF funded initiatives against outcome measures and annual targets. This information on the effectiveness will help guide reinvestment and support the growth of investment in early intervention.

Setting and tracking the impacts of EIIF-funded initiatives will help the Victorian Government understand what is being achieved and the most effective and efficient strategies for improving outcomes for Victorians. In this way, the EIIF can be seen as a better budgeting process and an investment in the evidence-led decision-making capability of the VPS. While this is being initiated in a tight fiscal environment, the principles and practices of the EIIF apply equally in times of growth as the framework is fundamentally concerned with intervening at a point which is both more effective for service users and more efficient, thus reducing the call on budget capacity, and providing greater confidence in investments.

In recognition of the intersectional nature of social services, where benefits and costs are diffused across multiple portfolios, the EIIF adopts a benefit sharing approach. Benefits from avoided costs are shared across agencies as ongoing EIIF dividends, reflecting where avoided cost are estimated to accrue – with agencies retaining any upside risk associated with reduced service use, such as reduced pressure on services enhancing workforce attraction and retention.

Operating with discretional power, the Expenditure Review Committee (ERC) will ring-fence EIIF dividends to respective agencies to allow them to be reinvested in future early intervention initiatives through the budget process. This model operates on the principle that benefit sharing will incentivise agencies to develop more EIIF initiatives and increase the fiscal return and funds available to ERC to invest in future early intervention initiatives.

3. BUDGET PROCESSES AND THE ROLES OF CENTRAL AND LINE AGENCIES

A way to gain insight into the budget process is to think about it in terms of the Tragedy of the Commons. The Tragedy of the Commons is an economic theory that refers to a situation where individuals with access to a shared resource act in their own self-interest, and not in the common interest of all users, leading to the depletion of the resource.[2]

A budget process functions to allocate a common pool of financial resources across stakeholders. During the budget process in government, line agencies develop and propose initiatives that they will implement and be responsible for, and which will draw from that common funding pool over a short-to-medium term timeframe. Each line agency has specific foci, goals and responsibilities, proposing initiatives to meet them. In this way, the process incentivises line agencies to secure a maximum allocation of resources to pursue their own specific objectives, rather than balance the needs of the broader commons.

Without the budget process applying certain limits, shared financial resources may easily be overexploited, which is a risk all commons face. Political economist Elinor Ostrom outlined a set of rules for managing the commons. These include clearly defined boundaries around who is entitled to access and to what, the need for collaborative decision making, and continued transparency and accountability around processes and performance.[3]

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[2] Garrett Hardin, "The Tragedy of the Commons," *Science* 162, no. 3859 (1968): pp. 1243–48.
[3] Elinor Ostrom, *Governing the Commons: The Evolution of Institutions for Collective Action*. Cambridge: Cambridge University Press, 1990.

The roles of central financing and coordination agencies, such as DTF and the Department of Premier and Cabinet, are to manage their jurisdiction's financial commons. These agencies take a whole-of-government approach, providing economic, financial and resource management advice and tools to help the Government deliver policies and common services for the public. In this way, DTF can be seen as the steward of the commons. This is a role that seeks to resolve issues through the passage of annual appropriation legislation. It also involves long-term considerations and planning to ensure sustainable budgeting and the optimisation of fiscal resources to achieve value-for-money outcomes. Line agencies, by way of contrast, are primarily concerned with how they can secure resources, working under the instruction of Ministers who want them to maximise allocations and spend them well to help more members of the public. In some instances, roles overlap where central and line agencies proactively work together to developed cross-portfolio solutions and strengthen businesses cases in collaboration.

Accordingly, during the budget process, DTF must sit in judgement, making recommendations to Government based on how reasonable estimates are, which proposals should receive funding, and which programs are underperforming and should be abandoned. Essentially, the central financing agencies act as gatekeepers into the commons, and the fence-builders within it, by determining which parts of the financial commons the line agencies can access to pursue their goals. These fundamental roles will remain irrespective of the budget process.

While the budgeting process averts a broader tragedy of the commons, there is still a 'Budgetary Tragedy of the Commons' where the shared financial resources are not utilised in a way that optimises outcomes for citizens. One challenge of the budgeting process is that it discourages collaboration between siloed departments, which means missed opportunities to invest in valuable cross-portfolio early intervention initiatives.

As Lord Andrew Adonis observes, "pooling budgets between government departments is probably more difficult than negotiating international treaties."[4] This is particularly true in social policy areas, where potential interventions and their associated beneficial outcomes stretch across multiple line agencies. Another challenge is that the budgeting process, when combined with the electoral cycle, encourages short-term thinking across government. This can mean early intervention initiatives that will realise opportunities for savings and reinvestment over the longer-term, are not funded adequately.

Questions to consider.

- What steps can be taken to address the Budgetary Tragedy of the Commons?
- What practices from other areas (e.g. negotiating international treaties or protecting the environmental commons) could be drawn on to support the implementation of the EIIF?

[4] Lord Andrew Adonis, National Community Budgets Conference, London, 29 November 2012.

4. IMPLEMENTING THE EIIF WITHIN THE BUDGET PROCESS

We view the EIIF as a means to help address the Budgetary Tragedy of the Commons. Not only does it provide more flexibility across the budgeting process – essentially removing and altering some of the fences that line agencies can access in the commons – it also encourages line agencies to focus on the common good and longer-term planning when developing budgetary initiatives.

This conception of the EIIF aligns with how the budgetary officials interviewed as part of this project saw their role. Collectively, they viewed the role of central financing agencies as not just gatekeepers and fence-builders of the commons, but the stewards who promote better use of shared resources over the longer term. A central financing agency's role is not just to say no to proposals, but to promote better policymaking and proposals that ultimately provide greater benefits for citizens. There was a consensus among the interviewees that a feedback loop exists between the technical aspects of the budgetary process and behavioural and attitudinal forces. A central financing agency may very well create new tools and processes; however, the right behavioural and attitudinal changes are also required to create a culture that drives demand for these technical solutions.

To balance the technical and adaptive challenges that interviewees identified when implementing a mechanism such as the EIIF, we suggest that DTF consider the Adaptive Leadership Framework. The Adaptive Leadership Framework was developed by Ron Heifetz and Marty Linksy of the Harvard Kennedy School. Heifetz and Linsky distinguish between technical problems and adaptive challenges. As outlined in Figure 1, technical problems have a clear problem definition and clear solution that can be provided by an authority figure who possesses the appropriate knowledge, skills or resources. Adaptive challenges have an unclear problem definitions and solutions that require learning by the relevant stakeholders instead of the authority figure. Most problems are not neatly packaged as technical or adaptive, but rather are a mix of both elements being intertwined.[5]

Figure 1. Distinguishing technical problems and adaptive challenges

Kind of challenge	Problem definition	Solution	Locus of work
Technical	Clear	Clear	Authority
Technical and adaptive	Clear	Requires learning	Authority and stakeholders
Adaptive	Requires learning	Requires learning	Stakeholders

From: Heifetz, Grashow and Linsky, *The Practice of Adaptive Leadership,* p. 20

We can apply the adaptive leadership model to examine ways of bringing about change. Where technical change generally occurs through incremental adjustments and applying existing expertise and problem-solving processes, adaptive change deals with systemic problems that require organisations and individuals to challenge their beliefs and behaviours,

[5] Ronald Heifetz, Alexander Grashow and Marty Linksy, *The Practice of Adaptive Leadership: Tools and Tactics for Changing your Organisation and the World.* Boston: Harvard Business Press, 2009, pp. 19-20.

develop new competencies, and work collectively. Through a process of repetition, changes at the behavioural and cultural level inform technical aspects and implementation, as new standards and values are baked into practice.[6]

Heifetz argues that the most common leadership failures are produced by treating adaptive challenges as they are technical problems. In such situations, people generally seek out technical tweaks or turn to an authority figure to provide a solution.[7] That technical solution might provide temporary relief, but it fails to address the underlying problem by avoiding the necessary adaptive work.[8]

Take, for instance, a family member who approaches you with a request to borrow $1,000 to pay off a bank loan they will default on tomorrow. You could view this as a clear problem definition (the person needs $1,000) that has a clear technical solution (you, the authority, give the person $1,000). However, this may only address the problem in the short term, with the family member returning to you in a month seeking more money. Alternatively, you could view it as an adaptive challenge where there needs to be learning by the family member, yourself and possibly others to define the problem and generate a solution. In this scenario, you might explore why the family member is defaulting on the loan, and what behaviours or attitudes they need to change to prevent them from ending up in this situation again.

We view the implementation of the EIIF as a situation where there are both technical problems and adaptive challenges present. DTF has made significant progress in advancing the technical aspects of EIIF, including growing internal capability to quantify outcomes and avoided costs and the positive incentive generated from a reinvestment approach.

The fact that these have not been straightforward tasks, with DTF having developed a new fiscal tool that does not necessarily fit within the standard parameters of the budgeting process and fundamentals of cost benefit analysis, can obscure how much remains to be done to maximise the prospect of its adoption.

At the current stage of implementing the EIIF, DTF faces some complex choices. There is a risk of diminishing returns in focusing on further technical refinements, when instead the threshold should be that both central and line agencies have verified the tools and trust the outputs. It is due to the significant progress which DTF has made in advancing the technical aspects that the bulk of the discussion below focuses on the adaptive changes that are still required.

The implementation of the EIIF is not something ANZSOG can refine with certain prescriptive solutions. Instead, this paper poses questions and tests identified features of the EIIF against the practical experiences of other jurisdictions to model potential paths that DTF may take, particularly by applying the adaptive leadership model to the areas of outcomes measures, risk sharing, and incentives. Our aim in doing so is to support DTF's own learning and

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[6] Ronald A. Heifetz and Donald L. Laurie, "The Work of Leadership," *Harvard Business Review* 75, no. 1 (1997): pp. 124-134.
[7] Ronald Heifertz, *Leadership Without Easy Answers.* Cambridge: The Belkap Press of Harvard University Press, 1994, p. 69.
[8] Heifetz and Laurie, "The Work of Leadership," p. 133.

encourage internal leadership of the adaptive work required to optimise the potential and impact the EIIF.

Questions to consider:

- How do different stakeholders view the EIIF and the challenges surrounding its implementation? What learning needs to occur at DTF, line agencies and with other stakeholders to successfully implement the EIIF?
- What technical problems exist in implementing the EIIF? What adaptive challenges exist in implementing the EIIF?

4.1 Outcome Measures

Considering the design of social policy interventions and their second order effects do not typically fit within Treasury's cost benefit analysis model, as the second and third order effects of an initiative lack tangibility, particularly in terms of quantifying long-term impacts. The EIIF seeks to bridge this divide, using impact measures to model a trajectory for second and third order effects within the budgeting process. With this comes a clear and quantified understanding of the anticipated impact of a program and a greater level of certainty upon which DTF can provide advice to Government to make its investment decision.

Across the jurisdictions interviewed, there was a consensus that proponents of initiatives should adopt a technical mindset – ensuring sufficient rigour to maximise the likelihood of success. Developing the right tools and processes is fundamental to encouraging this approach. New Zealand Treasury's *Living Standards Framework* and NSW Treasury's *Outcome Budgeting* business planning model, for instance, have been useful in framing evaluation as central to the work of government. Budgeting officials found that these tools have helped line agencies shift their thinking towards a technical focus, carefully considering how best to articulate avoided and distributional costs when making a program budget proposal, how to align spending with outcomes, and reform existing programs.

While well-designed tools are certainly important in the implementation of the EIIF and similar programs, they cannot be separated from the respective roles of central and line agencies and how this will inform the perceived purpose of outcome measures.

With DTF's established role of judging and recommending, line agencies are inclined to view outcome measures as a compliance activity, with initiatives facing increased scrutiny and the threat of punitive cuts. Accordingly, line agencies may overestimate avoided costs to maximise funding for reinvestment opportunities or seek exceptions to protect their allocations. This would generate a high degree of uncertainty and scepticism within DTF, with a tendency to view measures as lacking credibility and unlikely to deliver savings. If not addressed, this behaviour would threaten the technical aspects of the EIIF, with neither DTF nor line agencies trusting one another to accept the validity of the outcomes model. For these reasons, it is crucial that DTF continues its proactive collaboration to ensure reasonableness of estimates and maintains a review capability for cases where collaboration is not possible.

It stands that before technical features can be successfully and sustainably implemented, line agencies must shift their thinking about outcome measures from a compliance activity to an activity that is key to ensuring effective and efficient programs. This involves adaptive change in the areas of framing and function.

The literature examining cross-boundary working finds that engagement is key to closing links between differing parties and promoting participant buy-in. This is most effective when driven from the top-down, as leadership ultimately sets the tone and values throughout an organisation.[9] The Suffolk Lowestoft Rising project offers a useful example of leadership that effectively models collaboration. The Suffolk Lowestoft Rising project focused on pooling resources to promote a whole systems approach joining up local social services – a Sponsoring Group of chief officers from the five partners provides leadership, strategic decision-making on resource allocation and work streams. The Sponsoring Group reaffirmed their commitment to collaboration and a common objective through the Support Team, consisting of at least one staff member from each participating organisation to lead work streams and engage with staff from each of the other participating organisations.[10]

With its established record in social impact bonds and outcomes-focused budgeting, NSW's observations provide particularly useful insight into the adaptive change required to successfully implement programs like the EIIF. The NSW Treasury officials observed an evolution from a mindset among agencies that outcome focused business plans were simply a compliance activity enforced by Treasury towards being key to ensuring the delivery of effective and efficient programs. There is now an agreed upon cycle of framing project proposals and outcome measures, regular reporting, and reform and refinement in response to outcome measures. It must be acknowledged that the evolution observed in NSW has been a measured one that faced some initial opposition among line agencies. Overwhelmingly, NSW Treasury officials noted the importance of genuine and engaged communication between Treasury and line agencies in facilitating this evolution. These interactions provide opportunities to understand the different contexts and interests at play, fostering long-term relationships that are built on a foundation of trust.

The NSW Treasury officials also observed that these interactions provide an opportunity to clarify and reinforce the role of outcomes measures. They have made a concerted effort to frame outcome measures as a tool for ensuring that funding is being allocated based on merit and what will deliver the greatest public good. This allows Treasury to communicate to agencies that it is not strictly concerned with savings, but also service delivery for the public good and better budgeting processes. Outcomes-based funding is, as one NSW Treasury official observed, "an alliance with the public service to drive good decision making."

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[9] *Collaboration Between Sectors to Improve Customer Outcomes for Citizens of NSW*. Research Report Prepared for the NSW Public Service Commission, Nous Group (2013), p. 18; *Collaboration – Build, Support and Sustain a Culture of Collaboration between and within Government and the Community Services Sector*: *Literature Review Report*. Supporting Communities Forum, Western Australian Government, 2019, p. 12.

[10] Jeremy Lonsdale, Daniel Schweppenstedde, Christian van Stolk, Benoit Guerin, and Marco Hafner, *One Place, One Budget – Approaches to Pooling Resources for Public Service Transformation*, RAND Corporation, 2015, pp. 21-22, 61.

Among NSW Treasury officials, both purposeful messaging and trust building are seen to have helped outcome measures gain purchase. Higher levels of trust and clarity have made line agencies more likely to engage fully and with good faith in the agreed cycle of designing an outcomes-based project, agreeing upon measures, providing regular reporting, and enacting reform in response to outcome measures.

Greater opportunities for collaboration may also protect against a fundamental feature of economic thinking – the preference for large datasets and simplified models that tend to reduce the complexities of existing economies and societal forces.[11] Certainly, large datasets provide useful insight into cohorts and trends in service use. However, they do not necessarily substitute the deeper work that agencies do. One senior official from Commonwealth Finance observed the need for mandated institutional structures to join up the capabilities of central and line agencies.

The incorporation of agencies' specialist knowledge about a portfolio – what is needed to address complex problems (e.g. local solutions and empowering individuals and communities), what information is being measured and if it is the correct and most useful information – facilitates the design of more sophisticated proposals with better outcome measures.

4.1.1 Considerations for DTF

The next practical step in refining and implementing the EIIF is ensuring that the rationale for improved outcomes and avoided costs is well defined and understood by stakeholders. NSW and New Zealand treasury officials suggest that an outcomes framework, similar to their own, may prove a useful tool in helping line agencies learn and adapt. It is important to recognise that existing structures and reporting processes, particularly those which are public, will drive behaviours and culture and could cut across more nuanced and valuable EIIF measures.

DTF should be prepared for opposition in the first years of EIIF's rollout – including scepticism or mistrust among some line agencies and a reluctance to report on what initiatives have not worked – and the need to commit to a sustained campaign of collaboration and communication with line agencies to incrementally build trust in the EIIF. DTF has already made some headway in this area, having developed avoided cost budget guidelines, and working collaboratively to quantify impacts for new EIIF proposals with line agencies including: estimating avoided costs, identifying outcome measures and helping to set targets for potential budget bids. The development of mandated institutional structures may continue to support this collaborative approach. A consideration for DTF is what form these may take, and how best to implement them.

Overwhelmingly, the literature and interview findings suggest that line agencies should be treated as partners rather than a vulnerability. For DTF, this would involve continuing to acknowledge that line agencies bring with them specialist knowledge about complex problems and appropriate and available performance information that can augment what EIIF is trying to achieve. Opportunities for engagement across various portfolios and levels of seniority will

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[11] Simon Torracinta, "Bad Economics," *Boston Review,* 9 March 2022, https://bostonreview.net/articles/bad-economics/.

be valuable in this process, providing DTF opportunities to consider the different knowledge, guidance, and tools required to align purpose both horizontality and vertically.

DTF is still in the initial stages of crafting the overall messaging around the EIIF and outcomes measures. A foundation of frankness will lend credibility to the outcomes-focused rationale of the EIIF and increase its long-term viability. This requires DTF to balance aspiration with reality in its messaging around the EIIF.

The EIIF is a more-informed budgeting process and investment in the decision-making capability of the VPS to facilitate more effective and efficient social services. However, at times – including now – it is also a better savings process. This latter feature would certainly be apparent to line agencies, and a failure to acknowledge this will only generate suspicion that DTF is not acting in good faith, leaving line agencies less likely to engage. DTF would do well to acknowledge that the EIIF is useful in periods of both budgetary growth and savings, and clear in its expectation that it will work with line agencies to identify both inefficiencies as points for savings and effective strategies for increased future investment.

In thinking about the messaging surrounding outcome measures, it may also be useful to consider expanding those involved in determining success beyond central and line agencies to include service providers and service users. This broader engagement will maximise the focus on the ultimate outcomes being sought, and increase buy-in.

A final consideration for DTF around how the EIIF is communicated is how the framework relates to vertical pressures and the gravitational pull of broader Government processes. For instance, Budget Paper No. 3: Service Delivery (BP3) outlines the Government's new funding decisions, how these support the Government's strategic objectives, and performance measures. There is a risk that EIIF funded initiatives will be distorted by the gravitational pull of BP3 measures, which have a stronger emphasis on compliance. Accordingly, DTF may wish to consider how best to align EIIF and BP3 to demonstrate a clear line of sight between EIIF initiatives and Government objectives, preventing potential downstream barriers to an effective and sustainable EIIF.

Questions to consider:

- What steps can DTF take to develop trust in the EIIF and associated budget process?
- How can the EIIF and its purpose be communicated effectively?

4.2 Managing Risk

The systemised, outcomes-focus of the EIIF flows into questions surrounding risk management. Mechanisms like the EIIF involve risk sharing across agencies and services. These stakeholders each have varying objectives and risk appetites, meaning that how DTF articulates ownership of risk will inform line agency engagement with the EIIF model.

In the case of the EIIF, DTF holds a significant proportion of the risk. There is the obvious first order risk of responsibility for funding an initiative. A central financing agency must also consider the second order risks, such as an intervention proving ineffective and failing to deliver savings.

The EIIF itself is also a risk, with line agencies' discretion over core funding allowing the distribution of allocations internally that may lead to underfunding for delivery of EIIF initiatives, or the potential that line agencies will 'game' the system by overestimating avoided costs. Indeed, budgetary officials we interviewed have observed a resistance among line agencies to report information about what has not been effective and why. This behaviour speaks to a perception of outcome measures as a cost-cutting mechanism and concern that future allocations will be reduced. Of course, this is driven by the distinct role of line agencies and how they perceive budgeting principles, with Ministers who want their portfolios to maximise allocations.

A common theme across the jurisdictions interviewed was the vertical pressures that central financing agencies face when activities are seen to fall beyond the traditional remit of cost benefit analysis. For instance, one senior official from the New Zealand Treasury observed that difficulties arose when the Auditor General perceived outcomes focused initiatives as unnecessarily high risk. As with BP3 measures, this points to the gravitational pull of existing rules and processes with which EIIF may be competing.

How then can DTF gain enough confidence to take on higher levels of risk and better fund more and more effective early intervention initiatives?

Budgetary officials from the Commonwealth and NSW championed a risk management model that targets change at the line agency level. Within this model, line agencies are required to approach the central financing agency with a technical mindset and robust outcome measures framework that communicates what an initiative is seeking to achieve and addresses issues of scale. With tools to routinely monitor maintenance of effort, a central agency has greater insight into how resources are being spent and can operate with greater certainty that an initiative will deliver social benefits and avoided costs.

Robust outcomes frameworks and regular reporting can facilitate multidirectional transparency and confidence building. For instance, one official from the OSII noted the importance of regular briefings with the Treasurer and Premier, outlining the successes, risks and failures experienced. This level of transparency lends credibility to outcome measures and, in turn, promotes a deeply invested senior leadership. Additionally, a consistent record of reporting over time is a useful tool for building trust in and across departments in the long-term.

Useful as the approaches of NSW and the Commonwealth are in terms of quantifying risks and delivering technical responses, they remain imperfect. Both jurisdictions acknowledged reluctance among line agencies to engage fully in the evaluative model. The challenge, they observed, is ultimately a cultural one that involves encouraging agencies to approach them with a problem rather than a predetermined solution. These observations speak directly to the Adaptive Leadership Framework, which warns against deriving a solution to a problem and trying to 'sell' it to the intended audience. Rather, the more appropriate course of action is collectively considering the dimensions of a problem and solution, and assessing who needs new competencies or resources to develop, understand, and implement the solution.[12]

An alternative model to risk management involves negotiation and the devolution of power. This model draws on the 'reform deal' proposed by Lonsdale et al. In the context of pooled budgeting and local-central government relations, the reform deal seeks to offer greater flexibility at the local level, while providing the central government with reassurances that public money is being managed responsibly. Commitments from central government to devolve responsibilities are traded for corresponding commitments to governance, transparency, and accountability from local governments. At the central level, these commitments are grouped into the four categories of funding, collaboration, regulation, and support, while at the local level they are grouped into focus on outcomes and efficiency, taking an evidence-based approach, governance and capability, and accountability. The possibility of sanctions remains as a recourse for behaviour that lacks transparency.[13]

One New Zealand Treasury official offered a comparable example, observing that the most effective approach in long-term, outcomes-based funding is for the central finance agency to accept that it holds most of the risk. With this comes a clear signal of trust in line agencies, granting them greater autonomy to innovate with solutions which, in turn, promotes greater buy-in. A comparable approach to funding is the EIIF's benefit sharing approach, where the ring-fencing of EIIF dividends guarantees a minimum level of new early intervention funding for reinvestment as part of subsequent budgets.

As in the reform model, this increased trust and autonomy comes with increased responsibility. While funding is guaranteed, expenditure reviews and contingencies for changed circumstances remain, allowing insight into how public funds are being managed and where inefficiencies might exist. Treasury expects agencies to work alongside it in this process, providing regular progress reports and identifying points for short- and long-term savings.

4.2.1 Considerations for DTF

The management of risk is a key consideration for DTF, one that gets to the heart of the challenge of implementing an effective and sustainable EIIF. A successful model for risk management is yet to be identified in the literature or among the jurisdictions interviewed. Nevertheless, there are useful lessons to be observed.

A robust outcomes framework is the primary tool for managing risk, providing DTF with confidence that interventions will result in positive outcomes and a reduction in acute service usage. This technical tool can be augmented by the messaging that DTF adopts around EIIF and positive and negative incentives to manage risk. DTF may wish to lay out the softer aspects of the EIIF, returning to the messaging of an evidence-based, more cooperative budgeting process that produces better policy outcomes and a safe pathway towards growing

[12] Heifetz and Laurie, "The Work of Leadership," p. 133.
[13] Jeremy Lonsdale, Daniel Schweppenstedde, Christian van Stolk, Benoit Guerin, and Marco Hafner, *One Place, One Budget – Approaches to Pooling Resources for Public Service Transformation*, RAND Corporation, 2015, pp. 27–31.

early intervention, as a shared goal, rather than solely applying a hard savings approach premised on estimated avoided costs.

However, this comes with the necessary caveat that to protect against the possibility of the system being gamed, DTF will continue to work collaboratively to input to new EIIF business cases to ensure their reasonableness, and maintain a central review capability to review for those submitted without collaboration with DTF beforehand. Building and maintaining the trust required to make this approach practicable will be an iterative process, relying on commitments from all parties to a more open dialogue about the successes and failures of investments.

A further consideration for DTF, should it adopt a collaborative approach, is the supporting tools. For instance, a risk sharing framework that sets out common terminology, expectations around accountability, and regulatory protections. Such a tool not only establishes clear expectations and responsibilities, but also promotes alignment of purpose.

The changeability of the public service creates key person risks if support for the EIIF rests with a select few people or within a single agency. A further consideration for DTF is securing an authorising environment that provides legitimacy and multidirectional buy-in to protect the EIIF long-term. This involves being attuned to how changes in priorities or leadership might influence DTF's objectives. A related consideration for DTF are the engagement activities required to instil confidence in the EIIF and sustain commitment. This may take the form of regular briefings of the Premier and Treasurer, as is the practice of the OSII. Whatever the form, these activities can help the DTF in its long-term planning and stewardship of the EIIF.

Combined, these interventions at both the technical and behavioural levels promote a more co-operative budget process driven by a sense of shared responsibility, ultimately offsetting scepticism among central agency officials that spending agencies may behave poorly.

A risk not identified in the literature or interviews, yet still pertinent to DTF, is the question of scale and growth. If the scale of the EIIF is too small, it will be ignored and fail to become the established basis for business case development; too large and the EIIF risks losing the discipline of its quantification if investment in early intervention outstrips the evidence base. In such a scenario, consistently ineffective initiatives will undermine the credibility of outcomes-focused funding and the long-term viability of the framework. Relatedly, the EIIF aims to increase investment in early intervention and as a better budgeting process, there is a reasonable case to do so quickly. However, the growth of the EIIF's share of new expenditure must be managed sustainably, or else risk resource allocation problems. The ring-fencing of dividends for reinvestment is one means of ensuring that the scale and growth of the EIIF are appropriate. DTF may wish to consider additional oversight processes and contingency plans.

As DTF continues to consider how best to identify and manage risk, a practical next step is the establishment of a community of practice (CoP). As evidenced throughout the interview component of this project, there is a community of individuals across multiple jurisdictions practicing on similar problems. A CoP would provide a valuable opportunity for frank peer-to-peer discussion and mutual learning.

Questions to consider
- What is the most appropriate scale for the EIIF?
- What risks do line agencies see existing with the EIIF?

4.3 The Role of Incentives

The role of incentives is an important final case study in the feedback loop that exists between individual and organisational behaviours and cultures and the technical aspects of implementing the EIIF.

The material incentives of the EIIF rest on the benefit sharing approach, whereby the monetised benefits to government of reduced demand on acute services are applied as EIIF dividends. These dividends are ring-fenced by ERC for future investment in EIIF programs, incentivising line agencies to develop more EIIF initiatives and, in turn, reinforcing a cycle in which the EIIF becomes the established basis for costing activities in scope.

However, line agencies must believe the EIIF model if they can be expected to be compelled by incentives and participate fully. This speaks to the risk of overemphasising technical considerations without due consideration for how individuals might respond and the effect this will have on implementation. Simon Torracinta, reflecting on the work of economist Diane Coyle, captures this feedback loop. He writes that, by embracing elegant, inflexible models and the role of an objective observer,

> economists in many applied domains – especially public policy – fail to account for their own agency within the system. Policymakers don't just observe the world; they intervene in it. And since the real economy is replete with feedback loops and two-way causality, models that don't factor in the role of policymakers – and how people might respond to their interventions – are destined to be misleading.[14]

Torracinta observes that these models often conflate the "descriptive and predictive uses of models with their prescriptive role in public policy". The model then, should be brought more in line with real world realities, factoring in the behaviour of complex problems and individuals.[15]

In the case of the EIIF, this involves considering the nature of social policy, where there will always be an unmet need perpetuated by deeper structural inequalities. For example, there is an almost infinite capacity for intervention in early education to improve downstream outcomes. Similarly, advances in health technologies mean that as what becomes medically possible expands the need for rationing will grow. This is exacerbated by the risks and limitations of avoided cost estimation, where there is an inherent uncertainty in modeling future events and fear among line agencies that demand reduction may not occur, but savings will nonetheless be taken. Accordingly, if line agencies fear this imagined loss, they may not find EIIF incentives compelling enough to participate fully, either pursuing funding outside of the EIIF or seeking to game the system.

[14] Torracinta, "Bad Economics."
[15] Torracinta, "Bad Economics."

An additional real-world consideration is how agencies will perceive the distribution of benefits across portfolios. Take for example a Department of Justice and Community Safety initiative addressing prison recidivism through drug and alcohol misuse programs. In addition to reducing reoffending, this initiative may also deliver reduced downstream demand for housing assistance services and savings for the Department of Families, Fairness and Housing. In cases such as this, where there is an institutional misalignment between investment and where benefits accrue, any crude application of savings solely to 'bidding department' may result in a likely a sense of competition among line agencies and reticence to engage in a model that rewards inactivity may develop. This may lead line agencies to seek funding through the usual budgeting process rather than EIIF, placing the growth of the EIIF and early intervention investment at risk. For these reasons, a rigorous approach to quantifying impacts and returning ring-fenced funds to where benefits accrue will need to remain features of the EIIF.

One senior New Zealand Treasury official spoke to similar challenges in the recent piloting of budget clusters, which sees agencies grouped together for budgetary collaboration and multiyear funding. The official observed difficulties around maintaining engagement with a model when an agency observes an initiative being funded that fails to deliver outcomes in their individual portfolio, or funds spent in one portfolio detracting from another. The proposed remedy, although not yet operating successfully, is the promotion of a shared vision for government funding with wraparound impacts that cut across portfolio silos.

4.3.1 Considerations for DTF

To achieve sustained and genuine engagement with the EIIF, it is paramount that line agencies believe in the rationale of the model and its incentives structure. In considering how to build this credibility and trust, we have given particular attention to the importance of framing impact measures as a tool for building public service capacity to determine successful initiatives and scale up investments in early intervention.

When approaching messaging around the role of incentives, DTF may wish to consider how best to position the EIIF as both a service reform exercise and savings exercise. Rather than a tool for redirecting funds, the focus should be on how the EIIF model will remove fiscal pressure on Government, improve decision-making and – through the ring-fencing of EIIF dividends – reinvest to scale up initiatives that work. Both the literature and interviewee observations suggest that this kind of purposeful messaging can help line agencies appreciate that evaluation and impact reporting will lead to greater allocations via further investment in successful, innovative initiatives. The larger an initiative's outcomes and avoided costs, the more meritorious it is likely to be viewed and the greater the amounts returned to departments for reinvestment in new early intervention proposals.

This incentive structure also has flow on effects for risk management. By rewarding line agencies for efficiency and the provision of better, more useful impact or outcome information, DTF is provided with greater certainty that initiatives will deliver downstream savings.

As DTF seeks to address the challenges apparent in the distributive nature of benefits sharing, it would do well to adopt a concerted effort to promote a whole-of-system approach to budgeting, one that prioritises inter-agency relationships and their shared purpose, rather than looking at the constituent parts of a system.[16] The technical tools for promoting interagency alignment and increased opportunities for engagement and cooperation that have already been discussed in this paper are important enablers of this whole-of-systems outlook.

Avoided cost estimates can only provide an approximate indication of the scale and distribution of the expected reduction in acute service usage across portfolios. DTF has taken many important early steps in acknowledging the estimation risks of the EIIF and preempting how line agencies may respond. This includes the design of a framework that incorporates a degree of conservativism to manage this estimation risk. The balanced approach to benefits sharing - with dividends that are lower (only a portion of avoided costs) yet still adequate to meaningfully increase funding available to ERC for future investment in early intervention - incentivises line agencies to develop more EIIF initiatives.

While these are certainly impressive early steps, DTF would do well to consider if additional adaptive changes and incentives are required to offset fear among line agencies that demand reduction may not occur, but savings will nonetheless be taken. Should a CoP or similar network be established, DTF would be provided with a valuable network of peers whose insight could be drawn upon.

Questions to consider

- What other incentives, particularly those that are non-financial, could support the implementation of the EIIF?
- In what ways are individuals or line agencies currently disincentivised to engage with the EIIF?

5. CONCLUSION

The EIIF is a new budgeting tool designed to guide and grow the Victorian Government's investment in early intervention initiatives. The EIIF is a better budgeting process, investing in the evidence-informed decision-making capabilities needed to assess the effectiveness of a program and allocate resources where they will have the greatest impact for citizens and provide a clearer line of sight between investment and its impacts. It is, at times, also a better savings process that guides the responsible allocation of resources that directly links to reducing the need for acute downstream services and costs to Government.

This research and practice paper has sought to aid the DTF in the refinement and implementation of the EIIF, examining the conditions necessary to realise a framework that effectively supports budgetary decision making on activities within scope. In doing so, we have conceived of the EIIF as a means to address the Budgetary Tragedy of the Commons. It is a tool for supporting greater flexibility across the budgeting process and encouraging line agencies to consider longer-term planning and the optimisation of shared financial resources for the common good, facilitating the safe scale up of initiatives that work through quantification requirements and yearly outcome reporting.

[16] Emily Miles with William Trott, *Collaborative Working: How Publicly Funded Services can take a Whole System Approach*, InsideOUT Series, Institute for Government, 2011.

Certainly, a central financing agency may develop new tools and processes and shore up technical features, however, we have found that the right behavioural and attitudinal changes are required to create a culture that drives demand for and deep investment in these tools. To address this feedback loop, this paper has adopted the Adaptive Leadership Framework, focusing on the changes required to ensure both central and line agencies have verified the tools and trust the outputs. This paper has tested identified features of the EIIF against the practical experiences of other jurisdictions. We have examined the likely challenges that DTF will face in progressing implementation of the EIIF and the learning required across the areas of outcomes measures, risk sharing, and incentives. A common theme emerging across each of these areas is that **a sense of shared purpose, trust, and accountability are central to adaptive change and the successful implementation of the EIIF**. This will be an iterative process, likely over a period of several years, and will require a sustained campaign of collaboration and careful stewardship by DTF to incrementally build the legitimacy of the EIIF.

A challenge that has emerged throughout this paper is DTF's dual role, being both the architect of the EIIF – with a vested interest in its success and continued growth – working collaboratively with departments on the business case, as well as advising Government on which EIIF proposals are meritorious for funding through the budget process. This duality is not easily navigated, and potential solutions are beyond the scope of this paper. Nevertheless, this may inform an agenda for future research and internal discussion.

In this paper, we have sought to generate discussion and creative thinking within DTF, rather than provide prescriptive solutions, with our hope being that we can support DTF's own learning on the adaptive leadership required to optimise the potential of the EIIF. The next step for DTF is to determine the priority areas and actions among those identified in this paper and what learning and by whom will deliver the greatest impact.

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APPENDIX 1: REVIEW OF THE LITERATURE

Introduction

Announced in Victoria's 2021-2022 budget, the Early Intervention Investment Framework (EIIF) is an innovative social services funding mechanism designed to link government investment with the quantifiable outcomes of early intervention programs. These outcomes are organised into two categories: the impacts on the lives of services users, their families, and the broader Victorian community, and the avoided costs to government from reduced need for acute services. The overarching goal of the EIIF is to balance budgetary reform with budgetary savings to deliver initiatives that are efficient and improve the lives of Victorians.

The first EIIF package – a total of $324 million over 4 years – supports Victorians from a range of cohorts, with complex policy issues and avoided costs that fall across several portfolios, including child protection, housing, health, and crime prevention. The EIIF reflects a broader trend in the public service away from budget and accountability silos towards a focus on whole systems approaches, greater fiscal sustainability and innovative budget management systems that support a wider set of outcomes.

While the EIIF and similar government funding mechanisms encourage cross-portfolio collaboration and greater autonomy to innovate and manage resources, considerable implementation challenges exist. These challenges are largely attitudinal and structural in nature, including the distinct roles and responsibilities of central and line agencies and the flow on effects for negotiating shared benefits and risks. This review draws on academic and practitioner literature to provide a high-level assessment of the barriers to and the enablers of long-term and intersectional government budgeting.

This literature review begins with an overview of the mechanics of government collaboration and the importance of developing a sense of shared purpose. The review then explores social impact bonds (SIB), as the closest comparator to the EIIF. The mindsets, tools, and processes that support collaboration are examined through SIBs literature and case studies. The review closes with a consideration of the relationship between central and line agencies, and proposed models for greater autonomy to facilitate trust and budgetary innovation.

The Mechanics of Government Collaboration

Collaboration is key to the delivery of government programs in which benefits and risks are distributed across portfolios. However, as the literature notes, collaboration is difficult to implement when contending with different priorities and operating environments.[17] This is particularly true of intersectional and long-term budgeting programs where benefits are diffused across multiple agencies. While these kinds of programs break down budgeting silos, encouraging innovation and greater efficiency, there are a lack of incentives when program risks and benefits are owned by another agency.[18] The challenge is an attitudinal one, Emily Miles and William Trott observe, in which governments must adopt a whole systems approach that prioritises the relationships between agencies and their shared purpose, rather than looking at the constituent parts of a system as if they operate independently from one

[17] John M. Bryson, Barbara Crosby, and Melissa Middleton Stone, "Designing and Implementing Cross-sector Collaborations: Needed and Challenging," *Public Administration Review* 75, vol. 5 (2015): pp. 647-63, https://doi.org/10.1111/puar.12432; *Collaboration Between Sectors to Improve Customer Outcomes for Citizens of NSW*. Research Report Prepared for the NSW Public Service Commission, Nous Group, 2013, pp. 9, 19-20.

[18] *Early Intervention: Smart Investment, Massive Savings. The Second Independent Report to Her Majesty's Government.* Cabinet Office, Government of the United Kingdom, 2011, pp. 1-9; Peter Willis and Matt Tyler, "Implementing a Social Outcomes Fund in Australia," *The Mandarin*, 3 September 2018, https://www.themandarin.com.au/97738-implementing-a-social-outcomes-fund-in-australia/.

another.[19] Three broad enablers of this whole systems approach were identified in the literature: shared purpose and benefits, trust, and effective and supportive leadership.

The literature shows in abundance that shared purpose is required for successful collaboration. A focus on desired outcomes from the outset is useful in developing a shared purpose and sense of shared ownership of both risks and benefits. In their overview of resource pooling at the local government area level, Lonsdale et al. found that a focus on jointly negotiated outcomes promoted a common understanding of an issue, overall objectives, and the standard of evidence needed to determine if objectives had been met.[20]

Leadership traits and mindsets – both at the individual and systems level – also play an important role in promoting shared purpose and driving altitudinal change. Strong leadership that consistently and repeatedly emphasises a shared vision and explores opportunities for cross-boundary working sets the tone throughout the participating organisations.[21] In the case of the Suffolk Lowestoft Rising project – which focused on pooling resources to promote a whole systems approach joining up local social services – a Sponsoring Group of chief officers from the five partners provides leadership and strategic decision-making on resource allocation and work streams. The Sponsoring Group reaffirmed their commitment to cross-boundary collaboration through the Support Team, which consists of at least one staff member from each participating organisation to lead work streams and engage with staff from each of the other participating organisations.[22] Groups such as these signal a common objective and a commitment to cross-collaboration.

However, more than simple signaling is necessary to facilitate effective government collaboration. Purpose-build tools and processes are also required from the outset to establish trust and close any links between agencies. As different agencies have varying objectives and regulatory structures, they will likely view the management of risks and benefits differently. The literature suggests that early engagement that is driven by strong leadership is central to understanding the different contexts and interests at play and, where possible, seek alignment. Alignment is best achieved through well-designed mechanisms, such as governance structures and risk frameworks, which set out common terminology, balance and allocate risk between parties, and provide guidelines for the management of resources.[23] In the case of shared budgets, this may take the form of a shared accountability structure for each agency to promote transparency in how allocations are spent.[24] As Lonsdale et al. note, “such tools provide the basis for considering strategically the overall objectives that all partners are seeking to achieve, and help to link individual contributions to the wider initiative.”[25] Moreover, they establish common operating guidelines that are relevant to all participants and offset any fear that individual agencies will behave in a way that threatens the objectives of other

[19] Emily Miles with William Trott, *Collaborative Working: How Publicly Funded Services can take a Whole System Approach*, InsideOUT Series, Institute for Government, 2011.
[20] Jeremy Lonsdale, Daniel Schweppenstedde, Christian van Stolk, Benoit Guerin, and Marco Hafner, *One Place, One Budget – Approaches to Pooling Resources for Public Service Transformation*, RAND Corporation, 2015, pp. 17-21.
[21] *Collaboration Between Sectors,* p. 18; *Collaboration – Build, Support and Sustain a Culture of Collaboration Between and within Government and the Community Services Sector*: *Literature Review Report*, Supporting Communities Forum, Western Australian Government, 2019, p. 12.
[22] Lonsdale, Schweppenstedde, van Stolk, Guerin, and Hafner, *One Place, One Budget*, pp. 21-22, 61.
[23] “Factsheet: Understanding and Managing Shared Risks,” Department of Finance, Commonwealth Government of Australia, 2020, https://www.finance.gov.au/sites/default/files/2020-11/comcover-information-sheet-understanding-and-managing-shared-risk.docx; *Collaboration – Build, Support and Sustain a Culture of Collaboration*, pp. 9-10.
[24] David McDaid and A-La Park, *Evidence on Financing and Budgeting Mechanisms to Support Intersectoral Actions between Health, Education, Social Welfare and Labour Sectors,* Health Evidence Network Synthesis Report 48, WHO Europe, 2016, p. 23.
[25] Lonsdale, Schweppenstedde, van Stolk, Guerin, and Hafner, *One Place, One Budget*, pp. 20.

agencies. The ideal result is high buy-in among participants and a sense of shared responsibility to one another and for the management of risks and benefits.

Social Impact Bonds: Challenges and Enablers

The last decade has seen an increased focus on developing new funding approaches for delivering social impact. There has been a drive towards reform within the public service, moving away from a spending mindset that responds to the consequences of a crisis towards spending that seeks to lessen the consequences of a crisis.[26] One such mechanism are social impact bonds (SIBs), a type of pay for success contract between government and private or philanthropic investors in which repayment on investment is linked to agreed measurable social outcomes. The EIIF draws on the best parts of the SIBs model – quantification and rigorous program evaluation linked to government payments – and scales it up. As the closest comparator to the EIIF, the lessons learnt from SIBs are highly relevant.

Social outcomes funding has been commended in the literature as an innovative approach that delivers the following benefits:

- More efficient use of public funds: the cost and benefits of a program are assessed on merit, while early intervention programs prevent poor social outcomes and, in turn, reduce future social service expenditure.
- Improved accountability: with funding based on achieving measurable targets, there is an increased incentive to generate rigorous program performance data.
- Accelerated uptake and sharing of best practice: responsible agencies use performance data to make evidence-based deliberation, allowing them to test new models of delivery about the best way to reach individual targets and promote scaled up implementation.[27]

The world's first SIB was the United Kingdom Justice Ministry's contract with Social Finance to provide a package of intensive support services designed to prevent reoffending among 3,000 prisoners at Peterborough Prison. The Justice Ministry agreed to make repayments on Social Justice's £5 million investment if the reoffending rate among prisoners released from the prison fell by at least 7.5 percent relative to the recidivism rate in a comparison group. The greater the reduction in reoffending rates beyond 7.5 percent, the larger the repayments, with a maximum return to investors of 13 per cent. The Peterborough Prison pilot, which operated between September 2010 and June 2015, resulted in a reoffending rate 9 per cent lower than the control group and was commended among stakeholders.[28]

Despite early success, SIBs remain a relatively new field of research and practice. As such, the evidence base underpinning the effectiveness of SIBs remains relatively limited. There is still much to test and refine and a sound agenda for future research. What can be gleaned from the literature are the challenges and conditions for success when implementing SIBs and similar mechanisms.

[26] *Early Intervention: Smart Investment, Massive Savings,* pp. 1-2.
[27] Jeffrey B. Liebman, *Social Impact Bonds: A Promising New Financing Model to Accelerate Social Innovation and Improve Government Performance*, Centre for American Progress, 2011, pp. 10-14; Jim Clifford and Tobias Jung, "Social Impact Bonds: Exploring and Understanding Emerging Funding Approach," *Routledge Handbook of Social and Sustainable Finance*, ed. Othmar M. Lehner (Oxfordshire: Taylor & Francis, 2016), pp. 161-176; Matt Tyler and Ben Stephens, "Paying for Outcomes: Beyond the Social Impact Bond Buzz," *Inside Story*, 28 October 2016, https://insidestory.org.au/paying-for-outcomes-beyond-the-social-impact-bond-buzz/.
[28] "Evaluating the World's First Social Impact Bond," *Rand Corporation*, 18 December 2015, https://www.rand.org/randeurope/research/projects/social-impact-bonds.html#key-lessons; Jake Anders and Richard Dorsett, *HMP Peterborough Social Impact Bond - Cohort 2 and Final Cohort Impact Evaluation*, National Institute of Economic and Social Research, 2017, pp. 13-14.

The literature identifies structural factors particular to the public service that make SIBs and other performance-based funding schemes difficult to implement. Chief among these are political and ethical drivers to focus on acute crises as they emerge and the flow on effect this has for funding certainty. This is exacerbated by the fact that SIBs take several years to deliver results. Accordingly, guarantees are required that policy changes and crisis response within central government will not lead to the diversion of funds. This generally takes the form of explicit mandates over a mid to long-term timeframe.[29] To provide additional certainty, Peter Willis and Matt Tyler have suggested that the expectations of both the public and government should be managed to ensure results are understood contextually. This includes avoiding messaging that "successful programs will 'pay for themselves'", instead placing an emphasis on sustainability and combining fiscal responsibility with improved lives.[30]

For SIBs to be feasible, they must be founded on credibility. Outcome measures and the regular collection of program performance data are primary tools for ensuring this. Outcome measures provide a clear and quantified understanding of the anticipated impact that a SIBs program will deliver for the community and the service system. The literature notes the complexity of identifying appropriate and reliable outcome measures. Measures must be clear and well defined, credible over the course of a program, particularly given the long timelines of preventative funding. They must also be based on a variable, ideally a method for assessing predicted outcomes in the absence of the program. Measures that are weakly correlated with program outcomes or only measure narrow components may distort performance data and erode trust.[31] In the case of one of Australia's first SIBs – the NSW Government's Benevolent Society Social Benefit Bond, which provides an intensive support program designed to prevent children entering out-of-home care – three outcome measurements are used to monitor the scale of impact. These are out-of-home care entries, Child Protection Helpline Reports, and the number of safety and risk assessments. Each outcome is weighted to provide a final performance percentage which determines repayment rates. The performance percentage is compared against a control group and independently certified, ensuring the credibility of the program.[32] While setting and monitoring outcome measures promotes accountability, it is a time consuming and analytically complex process. Accordingly, practitioner literature underscores the importance of planning for the time and capabilities required to ensure successful program implementation.[33]

A focus on outcomes not only lends credibility to SIBs, it also incentivises buy-in and evidence-based decision making through the allocation of risks and benefits. Service providers are generally unable to provide sufficient capital upfront to fund long-term program. They are also unable to absorb the entire risk of failing to deliver on outcomes targets. SIBs allow private investors to absorb most of the risk, as well as perform a quality control role, as service

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[29] *Early Intervention: Smart Investment, Massive Savings,* pp. 13-19; Willis and Tyler, "Implementing a Social Outcomes Fund in Australia"; Matt Tyler and Peter Willis, *Improving Outcomes in Social Services: Modernizing Australia's Social Infrastructure,* Final Report for the Australian Labor Party, 2017, pp. 51-52.
[30] Willis and Tyler, "Implementing a Social Outcomes Fund in Australia".
[31] Liebman, *Social Impact Bonds*, pp. 3-4, 13-14.
[32] Emily Gustafsson-Wright, Sophie Gardiner and Vidya Putcha, *The Potential and Limitations of Impact Bonds: Lessons from the First Five Years of Experience Worldwide*, Global Economy and Development Program, Brookings Institute, 2015, pp. 121-22; "The Benevolent Society Social Benefit Bond," Office of Social Impact Investment, NSW Government, https://www.osii.nsw.gov.au/initiatives/sii/the-benevolent-society-bond/.
[33] Lonsdale, Schweppenstedde, van Stolk, Guerin, and Hafner, *One Place, One Budget*, pg. 18; "NSW Social Impact Investment Policy: Statement of Progress 2015," Office of Social Impact Investment, NSW Government, https://www.osii.nsw.gov.au/assets/office-of-social-impact-investment/files/Statement-of-Progress-2015.pdf; "OSII Releases 2016 Statement of Progress," Office of Social Impact Investment, NSW Government, https://www.osii.nsw.gov.au/news/2017/07/07/2016-statement-of-progress/; "NSW Social Impact Investment: Statement of Progress 2018," Office of Social Impact Investment, NSW Government, https://www.osii.nsw.gov.au/assets/Statement-of-Progress-2018.pdf.

providers must be able to reasonably demonstrate that they can deliver outcomes. This risk allocation is only viable if benefits satisfy investors. A common feature of SIBs are payments to investors that are tiered, with higher interest rates tied to higher overall improvements in outcomes.[34] By linking benefits to measurable outcomes, investors understand that improved program outcomes will result in higher-level returns. Service providers similarly understand that a failure to meet outcomes will result in funding being terminated or reduced, placing the continuation of a program at risk. This model incentivises transparency and rigorous evaluation, as both parties seek to find the most effective and efficient way of delivering services.[35]

Leadership that encourages and facilitates collaboration is a common feature among successful SIBs. For example, the NSW Office of Social Impact Investment (OSII) – launched in 2015 following successful SIBs piloting – is overseen by the Social Impact Investment Steering Committee. The governance group consists of executives appointed from the NSW Treasury, NSW Department of Communities and Justice, NSW Department of Education, NSW Department of Premier and Cabinet, including Aboriginal Affairs, and NSW Ministry of Health.[36] After identifying the need for improved capabilities in identifying and measuring outcomes, the Social Impact Investment Steering Committee oversaw the development of the Technical Guide for Outcomes Measurement. This guide assists providers in identifying their population, counterfactuals, and outcomes, and select appropriate methods for measuring the effectiveness of interventions.[37] The OSII has also sought to improve the quality of and access to performance data, including removing barriers to data sharing across agencies. OSII reports that these steps help streamline processes and make for more credible, comprehensive assessments of how programs are performing.[38] With repayments tied to performance, participants are positively incentivised to engage in collaborative efforts, make use of available tools, and identify and share examples of factors that have contributed to success.

Models for Greater Budget Flexibility

Long-term government budgeting initiatives that rely on the quantification of a broader range of impacts necessitate a degree of flexibility in the budgeting process. This marks a trend away from the traditional command-and-control system in which central financing agencies closely inspect and regulate the financial behaviours of line agencies.[39] While flexibility and devolved power are beneficial, they cannot be without limits. There are inherent differences in the budgeting principles of central and line agencies and certain rules must be upheld to ensure accountability around how public resources are allocated, spent, and transferred and who has authority to permit these actions.[40] Some work has been done to identify a balance between enhancing the flexibility and autonomy of line agencies and maintaining the rules of budget control that ensure public money is managed with accountability.

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[34] Gustafsson-Wright, Gardiner and Putcha, *The Potential and Limitations of Impact Bonds,* pp. 55-129.
[35] *Liebman, Social Impact Bonds*, pp. 1-4, 22, 43.
[36] "About Us," Office of Social Impact Investment, NSW Government, https://www.osii.nsw.gov.au/about-us/about-us-2/.
[37] "Technical Guide for Outcomes Measurement," Office of Social Impact Investment, NSW Government, https://www.osii.nsw.gov.au/tools-and-resources/technical-guide/.
[38] "NSW Social Impact Investment Policy: Statement of Progress 2015"; "OSII Releases 2016 Statement of Progress"; "NSW Social Impact Investment: Statement of Progress 2018"; Lonsdale, Schweppenstedde, van Stolk, Guerin, and Hafner, *One Place, One Budget*, pp. 17-18.
[39] Allen Schick, "The Changing Role of the Central Budget Office," *OECD Journal on Budgeting* 1, vol. 1 (2001): p. 9, https://doi.org/10.1787/budget-v1-art3-en.
[40] Peter Wilkins, John Phillimore and David Gilchrist, *Working Together: Evidence on Collaboration from the Reports of Independent Watchdogs*, Australia and New Zealand School of Government, 2015; Robyn Keast, "Joined-up Governance in Australia: How the Past can Inform the Future," *International Journal of Public Administration* 34, vol. 4 (2011): pp. 397-419, https://doi.org/10.1080/01900692.2010.549799.

One such model is the 'reform deal' proposed by Lonsdale et al., which is predicated on a link between performance and greater flexibility. In the context of pooled budgeting and local-central government relations, the reform deal seeks to offer greater flexibility at the local level, while providing the central government with reassurances that public money is being managed responsibly. Commitments from central government to devolve responsibilities are traded for corresponding commitments to governance, transparency, and accountability from local governments. At the central level, these commitments are grouped into the four categories of funding, collaboration, regulation, and support, while at the local level they are grouped into a focus on outcomes and efficiency, taking an evidence-based approach, governance and capability, and accountability. For instance, central governments may provide funding with a multi-year mandate to allow upfront investment to focus resources on complex needs, demand reduction and improve outcomes in the longer term. In return, local governments would be required to commit to clear and specific outcomes, with obligations attached to funding. One such obligation may be annual reporting requirements on program performance, ensuring the credibility of programs and building trust between the central and local government.[41] Michael Di Francesco and John Alford's model for earned autonomy builds on the reform deal through the inclusion of teared incentives and regulatory protections. Earned autonomy operates as a scaled incentive mechanism, where a line agency's performance against predetermined minimum financial management requirements is rated, compared, and either rewarded or sanctioned.[42]

While there is no single model for governing the allocation of risks between parties, both the reform deal and earned autonomy are useful in the context of the EIIF. Both models are grounded in considerations of the distinct roles of central and line agencies, and how this constrains action and relationships within the budgeting process. Importantly, both models suggest that there is the potential for a degree of latitude if higher levels of trust are built. This is a delicate balance between mutual obligations and regulatory protections, which, if executed correctly, will offset any paranoia within the central agency that spending agencies may behave poorly. The concept of earned autonomy, in particular, raises the potential for collective earned autonomy, in which a high level of buy-in across departments promotes greater autonomy than low buy-in, thereby acting as a shared incentive for aligning budgeting processes, building trust, and sharing risks and benefits.

The key point taken from the literature is that trust is dynamic; trust and the greater autonomy it offers can easily be eroded by behaviors that lacks transparency or are unexpected. For DTF and the implementation of the EIIF, building and maintaining trust will be an iterative process that relies on commitments from all parties and embracing a more open dialogue about the successes and failures of investment performance.

[41] Lonsdale, Schweppenstedde, van Stolk, Guerin, and Hafner, *One Place, One Budget*, pp. 27-31
[42] Michael Di Francesco and John Alford, "Balancing Budget Control and Flexibility: The Central Finance Agency as 'Responsive Regulator'," *Public Management Review* 19, vol. 7 (2017): pp. 979, 983-4, https://doi.org/10.1080/14719037.2016.1243812.

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