



# SageBush starter series

## Public sector finance 101

SageBush's starter series supports public sector leaders to understand and manage financial challenges.

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# Public sector finance 101

New Zealand's state sector financial management system aims to:

- help the government of the day translate its strategy into action
- focus spending on outcomes sought by the Government
- promote informed decision-making and accountability
- identify and actively manage fiscal and non-fiscal risks
- encourage a responsive, prudent, efficient and effective state sector.<sup>1</sup>

Sounds complicated ... and it is! This guide will provide you with the basics to understand how the system works and why you may need to input into various processes and to meet various reporting requirements over the year.

<sup>1</sup> Putting It Together: An Explanatory Guide to New Zealand's State Sector Financial Management System, The Treasury, September 2011, page 4.

# Constitutional structure (in a nutshell)

Understanding the state sector financial management system requires knowledge of the constitutional environment in which it operates.

Parliament (the legislature) is the supreme law-making authority in New Zealand. It consists of a single House of Representatives (the House) whose members are elected by the people of New Zealand and the Governor-General as representative of the Head of State.

The leader of the party (or of the largest party in a coalition) that has the confidence of the House is Prime Minister and head of the executive branch of the government. The government is accountable to Parliament.

The Prime Minister assigns one or more portfolios to each Minister, who will then lead the development of policy within the portfolio(s). Portfolio responsibilities also include control of public financial resources, oversight of state sector organisations and duties under relevant legislation. Individual Ministers are supported in their portfolios by one or more departments. Cabinet is chaired by the Prime Minister and is made up of senior Ministers. Cabinet makes all significant government policy decisions.

Select committees are Members of Parliament appointed by the House to consider and report on specific areas of government activity. On behalf of Parliament, select committees also scrutinise and hear public submissions on Bills (draft legislation), scrutinise proposed appropriations for each portfolio (Vote) and review the performance of state sector agencies.

## Accountability framework

The financial management system supports the government's accountability to Parliament by assigning roles and responsibilities for the use of public sector resources, setting clear performance expectations and then assessing performance against those expectations.

During the budget cycle, the government decides:

- its outcome priorities and which outputs it will purchase to achieve them
- the level of investment to be made in state sector organisations
- what departments will distribute or deliver on its behalf.

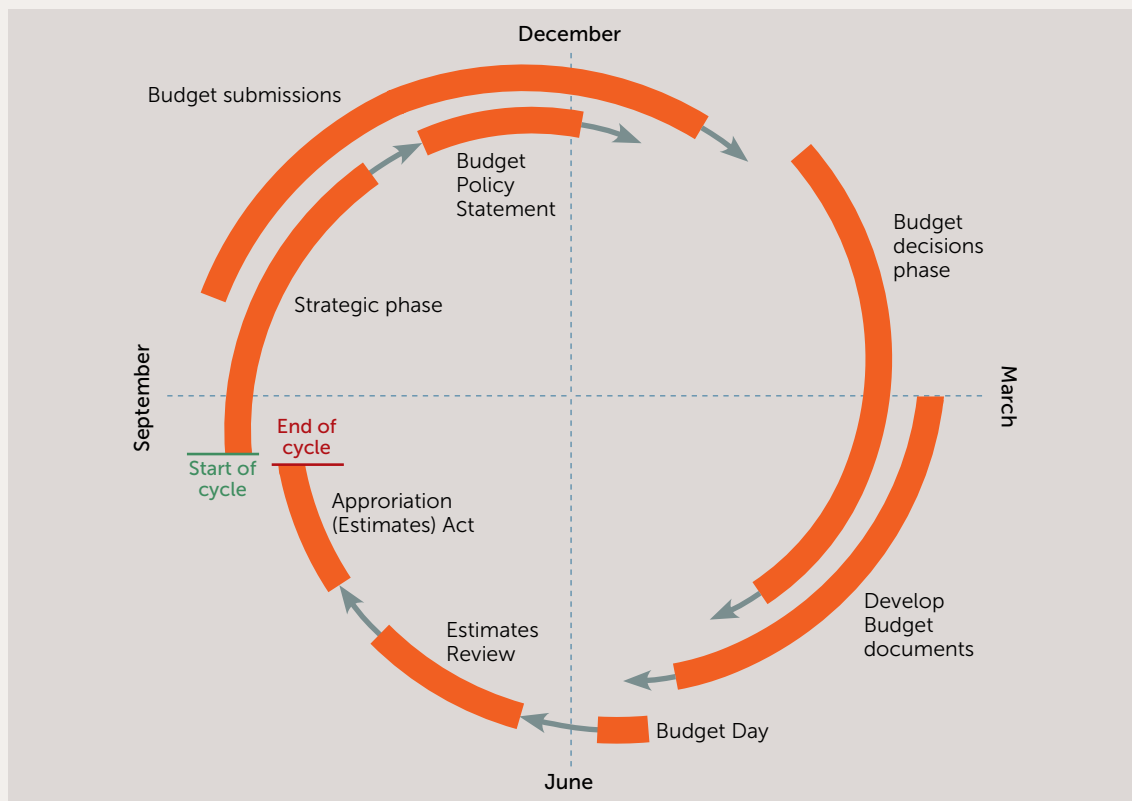
Responsibility for implementing these decisions is assigned to Ministers through their portfolios. Ministers delegate these responsibilities to departmental chief executives by agreeing chief executive performance agreements and output plans.

# Financial management cycle

The state sector financial management cycle is illustrated in the following diagrams:

- The government budget cycle, which determines the direction and priorities for the state sector.
- The departmental planning and reporting cycle, which sets out how a department will support the government's priorities, deliver services and report on performance.

## Government budget cycle



**Strategic phase** – the cycle starts in August/September when Cabinet develops its overall approach for next year's budget, including priorities, intentions and themes in light of fiscal and economic forecasts. A spending limit is set for the budget, parts of which may be ring-fenced for specific purposes or sectors.

**Budget Policy Statement** – the strategic phase culminates in the Budget Policy Statement, which is usually announced in November/December. It sets out the government's budget priorities, including both short-term and long-term fiscal objectives. Ministers identify the priorities for their Votes, which in turn guide the development of budget submissions and drive departmental planning.

**Budget submissions** – departments prepare budget plans that set out how a Vote will support government priorities; options to start, enhance, reduce or stop programmes; and risks facing the Vote and how these will be managed. Submissions must be agreed with Vote Ministers and may include bids for new funding.

**Budget decisions phase** – Budget Ministers meet over a 2–3 month period to consider and refine budget submissions and to develop a proposed budget package for the coming year. The budget package seeks decisions on funding for new initiatives and reprioritisation of spending within and across Votes and agencies. Cabinet agrees the budget package, and it flows into a range of budget documents.

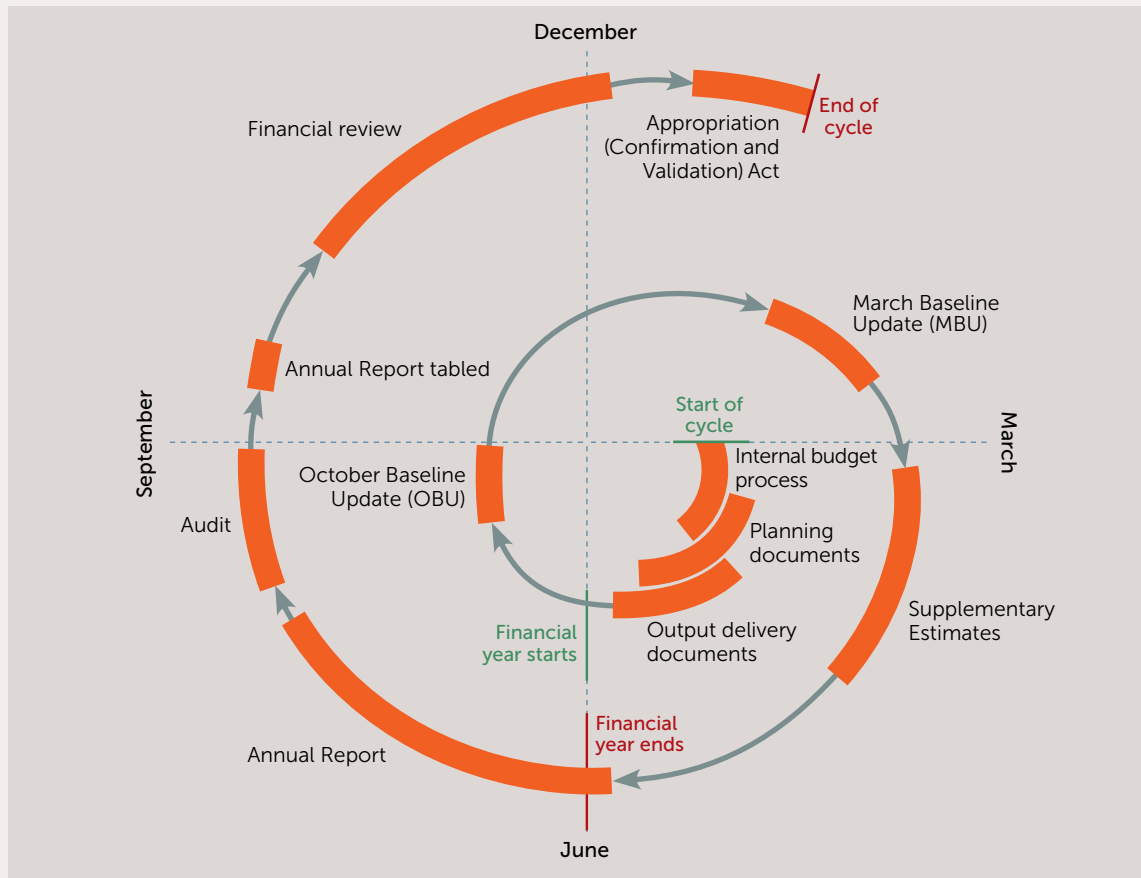
**Develop Budget documents** – departments and Treasury prepare documents to support the government budget. The key documents are the Estimates and Information Supporting the Estimates, which form the basis of the Appropriation (Estimates) Bill. The information in budget documents is treated as budget secret until it is announced on Budget Day.

**Budget Day** – the Minister of Finance presents the government budget to Parliament and the public on Budget Day (usually late May).

**Estimates Review** – select committees examine Ministers and departments about the appropriations that have been requested in the Appropriation (Estimates) Bill. They report back to the House within 2 months of the delivery of the Budget.

**Appropriation (Estimates) Act** – the government budget cycle concludes with the passing of the Appropriation (Estimates) Bill. By passing this Bill, Parliament approves the appropriations for the coming year, which authorises the government to spend public money.

## Departmental planning and reporting cycle



**Internal budget process** – departments prepare their internal operating budgets. These need to align with the draft Estimates documents, and the amounts allocated to business groups can be no more than the total appropriations sought.

**Planning documents** – departments prepare their key planning documents for the coming year, which include financial and non-financial forecasts. Documents include a four-year plan and statement of strategic intentions.

**Output delivery documents** – departments prepare documents that specify the outputs to be delivered, performance measures and standards, expected costs and monitoring and reporting arrangements. These are formalised in the output plan and the chief executive's performance agreement.

**October Baseline Update (OBU)** – this provides the first opportunity to update appropriations to reflect decisions made by Cabinet since the Estimates, to seek approval for fiscally neutral changes and to adjust forecasts.

**March Baseline Update (MBU)** – this provides a second opportunity to update appropriations to reflect decisions made by Cabinet, to seek approval for fiscally neutral changes and to adjust forecasts.

**Supplementary Estimates** – departments prepare documentation to support the Supplementary Estimates, which is the process by which the government seeks parliamentary approval for changes to the current year appropriations. Approval is sought by submitting an Appropriation (Supplementary Estimates) Bill to Parliament, and the changes are confirmed when the Bill is passed.

**Annual Report** – departments report their financial and non-financial performance in the annual report. This is a key accountability document and is used by select committees to scrutinise performance. (In addition to yearly reporting, departments also provide monthly reporting to their management teams and quarterly reporting to Ministers.)

**Audit** – the government auditor (Audit New Zealand) reviews the department's annual report to ensure it is complete and accurate and that public money has been spent for the purposes that Parliament authorised.

**Annual Report tabled** – the Minister responsible for a department (the Responsible Minister) tables the department's annual report in the House.

**Financial Review** – select committees examine Ministers and departments on performance and expenditure in the annual report against appropriations.

**Appropriation (Confirmation and Validation) Act** – the departmental planning and reporting cycle concludes with the passing of the Appropriation (Confirmation and Validation) Bill. This confirms any year-end changes requested under the Public Finance Act and validates actual expenditure for the previous year.

# Appropriations

Appropriations provide authority for the government to spend public money. In simple terms, Parliament says: “You are authorised to spend up to this amount ... You must spend it on these things ... and show us what you have done by achieving these targets.”

Appropriations are specified in terms of **amount** (how much can be spent), **scope** (what it can be spent on) and **period** (when it can be spent). These limits are legally binding. Responsibility for each appropriation is allocated to a Minister and is administered by a department on behalf of the Minister. The job of the administering department is to ensure that any expenditure is within the amount, scope and period of the appropriation.

If expenditure is incurred without an appropriation or is not in accordance with the amount, scope or period, unappropriated expenditure is said to have occurred. Unappropriated expenditure is unlawful, and there is a series of procedures that must be followed to legitimise the overspend.

Appropriations must be approved each year under an Appropriation Act and are subject to a process of parliamentary scrutiny. Without parliamentary authority, the government is unable to spend and cannot govern. Appropriations are therefore an important part of both the constitutional framework of New Zealand and the state sector management system.

## Votes

When Parliament considers legislation relating to appropriations, the appropriations are grouped within Votes. Generally, a Vote groups similar or related appropriations together. Responsibility for a Vote is assigned to a Minister of the Crown. When the Appropriation Act is passed, Parliament is said to vote resources to Ministers.

Typically, there is one Vote for each ministerial portfolio, but sometimes a ministerial portfolio may comprise an appropriation within a Vote that is part of another Minister’s portfolio. A ministerial portfolio may also span more than one department.

The appropriations in a Vote are administered by a department on behalf of the Minister. Some departments administer multiple Votes, providing outputs to more than one Minister.

## Estimates

The government’s request for appropriations and supporting information is presented to the House of Representatives at budget time in a formal document known as the main Estimates. The Estimates detail appropriations sought from Parliament by Vote Ministers for expenses and capital expenditure for a number of purposes including classes of outputs. Information on the price, quantity and standards of outputs is laid out in the Information Supporting the Estimates. The Information Supporting the Estimates also sets out how appropriations are linked to the government’s priorities and intended outcomes.

In addition to the main Estimates, there are also Supplementary Estimates. These seek parliamentary approval for Cabinet decisions for the current year that have been made since the last budget.

# Demystifying the lingo

State sector finance uses a raft of acronyms and technical jargon. These are the key terms you need to be aware of:

- **Appropriation** – the legal authority for the government to spend public money for a specified purpose. The authority is granted by Parliament each year by passing the Appropriation (Estimates) Act.
- **Baseline** – a general term that refers to the approved level of funding for a spending area. Although it is usually used to refer to the total approved funding for a department, in practice, it can also be used to refer to a Vote, service or business unit.
- **Estimates** – the formal document that is presented to Parliament by the government requesting approval of appropriations for the coming financial year. The full name is the Estimates of Annual Appropriations for the Government of New Zealand.
- **Estimates Review** – the processes by which Parliament scrutinises the appropriations that have been requested for the coming year. The review is undertaken by a Parliamentary select committee.
- **FNA** – Fiscally Neutral Adjustments (FNAs) are used to transfer funding between appropriations within a single financial year. FNAs must offset each other so that they are fiscally neutral and have no impact on the government's operating balance or debt.
- **Financial Review** – the process by which Parliament scrutinises the performance and expenditure in the annual report against appropriations. The review is undertaken by a Parliamentary select committee.
- **4YP** – the four-year plan (4YP) provides a snapshot of a department's strategic and medium-term planning. It describes what the department will look like in 4 years' time and how it will get there.
- **Imprest Supply** – the government is not authorised to spend money until the appropriations have been approved, which does not happen until after the start of the financial year. The Imprest Supply Act allows the government to spend money in advance of the yearly Appropriation Act being passed.
- **MBU and OBU** – March Baseline Update and October Baseline Update. Baseline updates are the formal mechanisms to update appropriations to reflect decisions made by Cabinet, to seek approval for fiscally neutral changes and to adjust forecasts.
- **Output Plan** – a formal agreement between a Minister and a department that sets out the outputs that will be delivered in the coming year, what they will cost, performance milestones and targets.
- **PFA** – the Public Finance Act 1989 (amended in 2013). This establishes the core principles of fiscal responsibility, governs the allocation and use of public money and establishes mandatory reporting and transparency requirements.
- **Responsible Minister** – the Minister accountable for the performance of a department from an ownership perspective. This includes capacity and capability, financial health, management of assets, investment in resources and governance.
- **Statement of strategic intentions** – a formal planning document that sets out the strategic objectives that a department "intends to achieve or contribute to" over the next 4 years.
- **Supplementary Estimates** – the formal document that is presented to Parliament by the government requesting approval for changes to the current year appropriations.
- **Vote** – a grouping of similar or related appropriations. Responsibility for a Vote is assigned to a Vote Minister.

Please contact us  
if you would like to talk  
about specific challenges  
your agency is facing.



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## Further Information

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