Value for Money

Guideline

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Introduction

MFAT is committed to the pursuit of best value for money to achieve development outcomes from the ODA resources it manages.

This guideline outlines the public sector definition of Value for Money and PDG's derivative definition as it applies to the New Zealand Aid programme. It provides guidance on MFAT expectations in this area, how value for money is pursued during the activity cycle, and a number of possible approaches to assessment.

Definitions

The Good Practice Guide for Public Sector procurement guidance for public entities, 2008 defines value for money as:

> "Using resources effectively, economically, and without waste, with due regard for the total costs and benefits of an arrangement, and its contribution to the outcomes the entity is trying to achieve.

It adds that:

> "The principle of value for money when procuring goods or services does not necessarily mean selecting the lowest price, but rather the best possible outcome for the total cost of ownership (or whole-of-life cost)."

"Value for money is achieved by selecting the most appropriate procurement method for the risk and value of the procurement, and not necessarily by using a competitive tender."

Value for Money Assessment of Activities

MFAT PDG defines value for money of activities as:

> "Achieving the best possible development outcomes over the life of an activity relative to the total cost of managing and resourcing that activity and ensuring that resources are used effectively, economically, and without waste."

Assessing value for money requires that the overall benefit of an activity be weighed up and compared with the overall cost. This can often mean comparing and valuing outcomes (development impact and sustainability etc), with inputs (costs including time, effort, money expended and opportunity costs), a qualitative and quantitative exercise which ultimately requires judgemen**t** on the relative value of different criteria.

The three key aspects that need to be assessed are:

- Development outcomes
- Cost
- Effective and economic use of resources

Development Outcomes

Both the quantity and the quality of development outcomes as well as the assumptions or risks associated with their achievement need to be assessed. The New Zealand Aid Programme assesses activity quality against its Activity quality criteria of relevance, impact, effectiveness, efficiency, and sustainability.

Cost

The whole of life cost of managing and resourcing an activity sufficient to achieve the proposed outcomes and outputs, needs to be assessed. This requires assessment of the proposed total whole-of-life cost of all activity phases (planning, implementation and completion) . In addition to the activity budget funded from Non-Departmental (Crown) funding, the time and cost of the management and administration by MFAT staff members should also be considered when assessing value for money.

Effective and economic use of resources

Resources are used effectively and economically if:

- They are clearly justified and aligned to achieve the desired development outcomes
- They are sufficient in quantity and quality to provide for all the inputs/outputs required for the desired outcomes
- They avoid waste, unnecessary inputs, or duplication both within the project and relative to other work
- Rates or prices paid are market based or otherwise assessed to be fair and reasonable.

'Market-based' means prices that have by some means been subject to competition in the market such as through a price-sensitive competitive process that provides for fairness to potential providers.

'Fair and reasonable' means that the proposed prices or rates charged are comparable to those that would be charged by another provider for a service of comparable quality and circumstances. This requires some level of knowledge of the market and comparison to other providers or activities. The term is used, despite its greater subjectivity, because much PDG grant funding occurs outside of an openly contestable process.

Value for Money Assessment during the Activity Cycle

All activities are subject periodically to a level of value for money assessment appropriate to their size and risk.

This table shows the MFAT PDG expectations of value for money assessment that might be carried out at different stages of the activity cycle.

Activity Cycle	MFAT PDG Expectations
Concept Stage	High level assessment of the likely quality and cost of alternative modalities, designs, or contracting options.
Approval to Design	Formal sign off of an authority to design would require justification of why it is expected to deliver value for money, plus an assurance that the design process itself is also cost-effective.
Design Stage	Value for money considerations guide design work including activity content, procurement planning and budget development. For all activities except those where a competive procurement process is required, the proposed partner will provide as part of the Activity Design Document (ADD), a detailed costed workplan, outlining the proposed cost of each output to be delivered over the life of the Activity and the timing of delivery. A quality-based assessment process should be done with the partner to ensure the budget is complete and accurate, cost effective and reasonable in the circumstances. The level of output and, if required, input detail sought will relate to the result of the partner and/or activity risk assessment. While budget advice is optional, the level of financial advice sought should correspond to the complexity of the design.
Appraisal and Approval	The value for money assessment of the whole of life costed workplan or the procurement plan is reviewed and documented as part of the appraisal process and confirmed as part of the Activity Assessment. Where procurement will take place after Activity appraisal, the procurement plan articulates the procurement processes to ensure value for money is achieved. Unit Managers are accountable for

Activity Cycle	MFAT PDG Expectations
	final review and sign-off of the value for money assessment prior to assessment panel.
Sourcing and Selection	Competitive procurement processes and appropriate service specifications or terms of reference ensure best value for money assessment.
Negotiation and Finalisation of Budget	As directed by the tender panel, negotiation or confirmation may take place to ensure sound internal design logic which links outcomes, outputs, and inputs, and that works with the partner to ensure the budget is sufficient and to remove potential waste from it.
Contracting	Value for money has been confirmed and is reflected in the terms and conditions.
Monitoring	Monitoring considers and responds to progress in delivering outputs and their contribution to outcomes and changes in the external environment that might put value for money at risk. The assumptions underlying the initial appraisal should be checked periodically.
Evaluation	Value for money is assessed in activity evaluations and is a key part of evaluating efficiency. It compares the outputs, outcomes, impacts or changes brought about by the work (value) compared with the resources used (money). An evaluation can examine value for money in several ways: • Compare the cost of the intervention with experience or norms in other activities (in the same country/region or internationally), where similar outcomes or impacts have been aimed for and/or achieved. • Analyse the activity’s own cost structures to identify efficiency issues, including whether savings could have been made (without disproportionately compromising outcomes) through different methods or management, procurement, prioritisation, design, etc. • Make an assessment of whether better outcomes and impacts could have been achieved for the same cost.

Value for Money Assessment Tools

A range of assessment tools are available to provide analysis and information to support good judgement in decision making.

Assessment tools include:

- Comparisons with other activities
- Programme logic analysis
- Cost-effectiveness analysis
- Financial viability or cost-benefit analysis
- Economic cost-benefit analysis (CBA)
- Opportunity cost analysis
- Multi-criteria ranking
- New Zealand Aid Programme quality assurance controls

Assessment Tool	Description
Comparisons with other activities	Compare the costs of the activity, or the prices/rates charged for specific budget items with those in other activities with comparable outcomes and context. In some cases these may be available within MFAT or from other agencies. More specific guidance is also available or released from time to time, from New Zealand Government Agencies - specifically Treasury, State Services Commission and Office of Auditor General. This includes areas such as Capital Asset Management and Public Private Partnerships.
Programme logic analysis	A programme logic analysis assesses the internal logic of the programme and the fit between outcomes, outputs, inputs and budget.
Cost-effectiveness analysis	A cost-effectiveness analysis considers proposed outcomes and outputs, analyses the approach and budget and whether there are alternative ways of delivering the required outcome.
Financial viability or cost-benefit analysis	A financial analysis analyses the income and expenditure of the enterprise/service and the case for its viability.
Economic cost-benefit analysis (CBA)	Economic cost benefit analysis (CBA) assigns dollar values to all costs and benefits of an activity to produce a measure of the net monetary benefits (or cost) of the activity itself that can be compared or ranked against other activities. Commissioning a CBA depends on the scale and

Assessment Tool	Description
	risk profile of the activity. More information on CBA is available from Finance or Sustainable Economic Development team members. Treasury also provides guidance to public sector agencies at www.treasury.govt.nz/publications/guidance/costbenefitanalysis
Opportunity cost analysis	An opportunity cost analysis is the value of what you could do with those resources if they were spent elsewhere. All expenditure has an opportunity cost. It is often useful to compare the activity under consideration, with other areas of the programme that will not receive funding if it goes ahead, i.e. to ascertain which has the more compelling business case.
Procurement evaluation assessment	MFAT commonly uses a procurement evaluation that involves multi-criteria ranking. The weighted-attribute model seeks to balance the trade-off between price and quality by weighting the criteria to reflect their relative importance. Each criterion in the proposal is scored, and each is multiplied by the relevant weighting to give a weighted score. The highest scoring offer is the preferred supplier. Such an approach is also possible in the non-commercial area, particularly when there are competing proposals.
Quality assurance processes and tools	Appraisal and peer review processes provide quality assurance on development effectiveness prior to final design. Monitoring and review provide reflection and evidence of progress in achieving development outcomes and revalidate value for money.

Value for Money in MFAT Accountability Documents

Cost effectiveness and value for money for the New Zealand Aid Programme is reported annually in the MFAT Annual Report. A range of indicators are used, as set out in the *Statement of Intent 2009-12* (pages 48 to 49). These indicators include effective implementation of management priorities and of Government policies; proxies of cost effectiveness (such as compliance with international aid effectiveness or good humanitarian donor norms); and findings on Programme and activity cost-effectiveness from individual reviews and evaluations.

Value for Money Myth-Busting

Does value for money simply mean choosing the cheapest option?

No. Value for money does not mean the cheapest cost option. If you are buying a shirt, value for money does not lie in the cheapest option, but in the best combination of quality, warmth, durability, style etc, and price. Cost is an important parameter, but still only one of a number. Value for money includes considering whether it meets your needs, its quality and effectiveness, durability as well as considering the potential outlay.

Why do we need to negotiate during budget development?

The opportunity to undertake negotiations enables a discussion directly with the supplier or recipients in relation to reasonableness and cost-effectiveness, to ensure that the resources planned for an activity are sufficient to achieve the desired result (i.e. completeness) and will be at an agreed quality. This does not mean that budget negotiations are primarily oriented to trimming down costs – though achieving economy within budgets is important. In some cases, budget negotiations may identify under-resourcing of areas crucial to a successful outcome. What is critical is that MFAT can be confident that the costs included are fair and justified against outcomes, and sufficient to achieve them.

When should we consider undertaking a Financial Analysis or Cost Benefit Analysis on an activity?

Both financial and economic CBA are very useful tools, particularly if used with an awareness of their limitations. It is good practice to do a financial analysis of any activity or component that seeks to establish an ongoing business or service. This supports judgements about the sustainability of that service or viability of the business. An economic cost benefit analysis should also be considered for multi-year activities that commit significant resource (around $10 million or more) and/or for activities that have a very high risk profile.