
REVIEW ARTICLES

The Schick Report: Evaluating State Sector Reform in New Zealand

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Allen Schick, The Spirit of Reform: Managing the New Zealand State Sector in a Time of Change, State Services Commission, Wellington, 1996

AN off-the-cuff comment by an overseas consultant currently working for the State Services Commission (SSC) in New Zealand conveys something of the impression the state sector¹ reforms have made upon the international policy community. She pointed out that in 1996 her agency hosted over 50 delegations from countries eager to learn from the New Zealand reforms. Not one failed to express anything but amazement and admiration, not just at the bold, comprehensive and innovatory nature of the reforms embodied in the State Sector Act 1988 (SSA) and the Public Finance Act 1989 (PFA), but at the reformers' success in ensuring that the principles which shaped their proposals were consistently reflected in public management practices. Not one, however, entertained any hope of completely replicating the New Zealand model, or of transferring it wholesale to their own countries.

Such a response to the New Zealand reforms permeates a report written by Allen Schick, a US professor of public policy, who was one of the more eminent visitors in 1996 to Wellington's control agencies. His report was commissioned by both the Treasury and the SSC as an 'independent review from a credible, external commentator, to assist with the on-going process of reflecting on and renewing the management framework' (p. 1). The biographical note to the report describes Schick as a prolific prizewinner who has 'been recognised five times by the American Society for Public Administration for the best article in *Public Administration Review*'. The report certainly lives up to the expectations generated by this description; the author displays not only academic virtuosity but clarity of thought and an elegant turn of phrase. The report provides a well-structured description of the dis-

¹ In this article the 'State Sector' refers to core government departments and Crown entities. It does not include state-owned enterprises or local government.

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inctive features, and of the strengths and weaknesses, of the New Zealand public management model.²

The Quest for Accountability

A recurrent theme in the policy literature is how reformers' intentions can become blurred, distorted or even subverted as they are implemented. Public choice theory and agency theory describe the public sector as a chain of principal-agent relationships in which control systems are rarely tight enough to prevent bureaucrats from pursuing their own interests or the interests of the groups that have 'captured' them. 'Garbage can' theories treat policy-making as a process which does not end with the passing of legislation but involves various stages of implementation in which 'intention is lost in context-dependent flows of problems, solutions and choice opportunities' (March & Olsen, 1989:34). From this 'new institutional' perspective, bureaucratic failure can arise not just from the pursuit of self interest but from bureaucrats' pragmatic tendency to follow traditional practices where ambiguity arises from the incomplete and inconsistent specification of directions. Most countries exhibit an almost fatalistic acceptance of this problem and a modest ambition to keep it within tolerable bounds.

Not so New Zealand, where Schick has been immensely impressed with the degree to which the reformers' intentions have been realised. In his view, the reforms were not just 'enormous, ambitious, and, in large part, unprecedented anywhere in the world', but, 'half a dozen years later', have wrought a 'transformation of the State sector from centralised control of money, personnel and other resources to devolved arrangements that give managers control of inputs, provide them with incentives to be productive, and hold them accountable for results' which Schick describes as 'extraordinary' (p. 2). What strikes Schick is that this revolution in public management has been achieved 'without going through the protracted pilot testing and cautious implementation that have slowed innovation in other countries' (p. 2).

Schick argues that the reform process has been able to unfold in a coherent manner in New Zealand because of its control agencies' unswerving commitment to the quest for greater accountability. He sums up this distinctive focus by observing that 'accountability has not been an afterthought; it was designed into the system at the outset, and as gaps in accountability have been identified, additional requirements have been imposed' (p. 73). This is reflected in *Government Management*, a Treasury brief submitted to the Labour government following its 1987 election victory, which provided the blueprint for the subsequent reform of the State sector. According to the Treasury, this reform process should be guided by the principles of

- *transparency*, so that the managers of government agencies should be given clear objectives which facilitate the monitoring of their performance and should, in

² The report can be accessed on the Internet from the SSC web site at www.nz.govt.ssc.

turn, be transparent in explicating these objectives and the means by which they are to be pursued;

- *decoupling*, according to which governments should be restructured into separate advisory, funding and service-provision functions so as to minimise the scope for policy capture by service providers;
- *congruency*, so that managers and others should have the incentives and information to achieve the government's goals rather than their own; and
- *contestability* of both policy advice and service delivery.

These principles were embedded in the SSA and PFA, which sought to establish the framework for a system of *ex ante* specification of the outputs of government agencies and *ex post* monitoring of their performance in delivering these outputs. The legislation made particularly sharp distinctions among 'outcomes', 'outputs' and 'inputs'. Ministries were expected to achieve specific outcomes by entering into contestable, contract-like arrangements with chief executives of government departments; these would specify *ex ante* the outputs they were required to deliver but leave them free to select the mix of inputs to be used in producing these outputs so that they would have 'flexibility in hiring and paying staff, obtaining office accommodation, purchasing supplies and services and spending on other inputs' (p. 2). Chief executives were required to be employed on a fixed-term basis and to enter with their ministers into performance agreements which set forth the standards and expectations according to which they would be judged and purchase agreements which specified the outputs their departments were to deliver in a particular year. This system has been extended to encompass the specification of, and accountability for, longer-term objectives: since 1994 the government has defined the medium-term outcomes it is trying to achieve in nine 'strategic result areas' (SRAs) and linked the outputs delivered by each department to these SRAs through 'key result areas' (KRAs), which now form the basis for their performance agreements.

This general shift toward an output-based accountability system could have been achieved only through a comprehensive overhaul of the public sector's budgetary and accounting systems. Budgetary appropriations for the operating expenses of departments are now made by output classes, and a capital charge is levied on the value of each department's net assets. To generate the information and incentives required to control and monitor departmental spending, there has been a shift from a cash flow to an accrual basis for financial statements, the budget and appropriations, while a comprehensive and detailed reporting system has been instituted within government departments. This requires them to prepare monthly financial reports, quarterly performance reports on their purchase agreements, half-yearly reports on the performance agreement and annual audited reports on financial results and outputs. Schick was struck with the speed with which these reforms were put into practice, observing that 'within about 18 months after enactment of the

Public Finance Act in 1989, all departments had shifted from cash accounting to budgeting on an accrual basis' (p. 3).

Managerialism vs Contractualism

The rationale for making managers of government departments accountable for outputs rather than outcomes is that this helps make them more accountable: the supply of outputs can be directly attributed to their performance, while outcomes may be influenced by factors beyond their control. This rationale was derived from 'contractual theory' (the term Schick uses to refer to the body of economic theories known variously as the 'new institutional economics', 'agency theory' and 'transaction cost economics'), which vied for influence with managerial theory when the reforms were on the drawing board. In a number of respects, the two sets of ideas converge. Both would argue for specifying objectives and measuring performance against them, for enhancing managerial discretion over input decisions, for fixed-term chief executives rather than permanent heads, for output-based appropriations and for shifting from cash flow accounting to accrual accounting. Many of the innovations introduced in New Zealand could be justified from a managerial as well as a contractual perspective. Schick goes so far as to suggest that the reforms that have brought most of the State sector improvement experienced over the past decade have been inspired by a managerial perspective. This is clearly the view of the senior and middle officials interviewed for the report. In conversations, they overwhelmingly endorsed the view that the most important change was freeing managers to manage. Some suggested that upwards of 75 per cent of the gain has ensued from this change alone (p. 23).

Managerial theory and contractual theory diverge, however, in the emphasis the latter gives to 'making managers manage' (rather than simply 'letting them manage') by making them contractually accountable for the delivery of specified outputs. Although this 'hard-edged contractualism' has made managers more accountable for those aspects of their performance which are under their control, it does have shortcomings and costs. Most obviously, the transactions costs incurred in negotiating agreements, monitoring compliance and preparing reports have been high, particularly for small departments, and have in some cases 'soaked up a substantial part of the efficiency gains' (p. 24) that they have been able to achieve after restructuring. Schick proposes that these transactions costs could be mitigated if some smaller departments were consolidated and if the reporting system were rationalised to remove areas of overlap and duplication.

More fundamentally, the contractual relationships established through the SSA were bilateral in character. This has made it difficult to take account of the 'ownership interest' of the third party (the government) in the long-run capacity of its departments to invest and innovate. This capacity might atrophy as purchasing parties, faced with funding cuts, try to squeeze as much output out of limited funds as they can in the short run. Moreover, although the PFA emphasised the distinction between 'outputs' and 'outcomes', Schick comments that 'despite expert and sincere effort', progress in the specification of outcomes has been slow. He again

relates this to the bilateralism inherent in the contractual model of reform since 'outcomes are externalities in two-party relationships; therefore it is exceedingly difficult to assign responsibility for them' (p. 26).

Schick is also concerned with the way the contractualist approach 'may diminish public-regarding values and behaviour in government' (p. 25). He worries that a public service ethic and a commitment to professional excellence may be replaced by a 'check-list mentality' through which managers focus almost exclusively on complying with the terms of their various contracts and arrangements. As a result of the tight monitoring of the provision of specified outputs, the 'invisible', unspecified, aspects of departmental service which would be supplied under 'responsible' management might be crowded out. Schick does not think that this problem will be 'remedied by even more detailed specification of performance' (p. 87) but advocates instead a 'responsibility' model of accountability. In doing this he distinguishes accountability — 'an impersonal quality, dependent ... on contractual duties and informational flows' — from responsibility — 'a personal quality that comes from one's professional ethic, a commitment to do one's best, a sense of public service' (p. 84). A starting place for renewing a culture of responsibility would be within the type of Senior Executives Service (SES) envisaged by the SSA. Schick attributes the failure of the SES to get off the ground to its incompatibility with the initially rigid bilateralism of the contractual relationships between ministers and chief executives. He recommends that every effort should be made to revive an institution which could potentially provide the pool of professional expertise in public management which is necessary to sustain a distinctive culture of managerial responsibility in the public sector.

The Likely Impact of the Schick Report

Despite their weaknesses, Schick emphatically rejects any suggestion that the reforms should be reversed. Rather he views these weaknesses as 'akin to the "bugs" found in state-of-the-art technologies after they have been introduced' and suggests that 'there is now a need to "debug" the reforms but that is a different matter from getting rid of them altogether' (p. 86). The Schick Report could be criticised for its paucity of hard recommendations in this respect; but this would seem to reflect the author's intention. Rather than tightening up an accountability system which is already very rigorous, Schick calls for a 'softer' approach which would not 'distinguish so sharply between producers and purchasers, between outputs and outcomes, and between the responsibilities of Ministers and chief executives' (p. 87).

His account of how the reforms have been driven by an unswerving quest for accountability does not, however, generate any confidence in the reader that this more mellow approach from New Zealand's control agencies will be forthcoming. It is a little too easy for Schick to argue that 'the most valuable asset that chief executives bring to their relationship with Ministers is not compliance but judgment and leadership' (p. 81). This implies that the current system provides scope to add these values to management practices. I would suggest that New Zealand's public sector could have been transformed only through the strong leadership supplied by

change agents committed to refocus its culture upon the advancement of a narrow set of principles. This new culture is radically different from the old one, which attempted to cultivate a 'public service ethos' in which action in the public interest involved a balanced assessment of the values, obligations and interests affected by the situation. Schick's concept of 'responsible management' contains echoes of this earlier culture and will be difficult to graft on to the new one forged by the reform process.

The impact of the Schick Report is difficult to assess at this stage. Schick himself is unlikely to be comfortable with the way his report has given ammunition to domestic critics of the reforms. Brian Easton, for example, enthusiastically hails the report 'as a watershed in the process of government sector reform' since it breaks from a 'foreign adulation based on a superficial understanding of what has occurred' to identify 'basic structural failures' which, if not addressed, 'will result in steadily deteriorating public service performance' (Easton, 1997:183-4). There is still, however, a considerable residue of appreciation among both the suppliers and consumers of public services for the historic achievement of the reformers in dismantling the outmoded Whitehall model of public administration. The commitment to a quest for accountability which made this achievement possible may, however, have left a legacy of inflexibility, of an incapacity to respond to rising public expectations of government agencies and to demands that they attend to a wider range of values. The significance of the Schick Report may be that its publication under the auspices of the Treasury and the SSC reflects a new willingness by these agencies to face up to this legacy.

References

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