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Agencies in Search of Principles

by

Allen Schick*

Why agencies, and why now? The proliferation of agencies is not accidental; it entails much more than merely rearranging the organisational map of government. There is a logic to the popularity of agencies that sheds light on the current state of democratic governance. Every government that embraces agencies does so for its own reasons, but as diverse as they may appear to be, all the reasons are the same. Some governments set up agencies to empower managers, others to emphasise service delivery, still others to evade personnel controls or other administrative constraints. As different as these motives may be, all attest to the belief that the inherited department-centred model no longer satisfies the organisational needs of government.

Why not? One set of explanations is rooted in the theory and practice of management. A body of literature that first emerged in economics, then influenced business management and later migrated to public administration challenges the once-dominant view that tightly integrated and controlled organisations are more efficient than fragmented, self-operated units. The argument against integrated organisations can be summarised as follows: Hierarchical, centrally-controlled organisations lack initiative, are slow to adapt to changing conditions and are not adequately responsive to the interests of those they serve. Giving agencies operating autonomy spurs them to innovate and improve performance. Because they are freed from departmental fetters, agencies are inherently more adaptive and responsive.

From this “new” managerial perspective, the rise of agencies is simply the latest stage in the never-ending process of organisational change and experimentation. Every generation has its favourite managerial style, and as concepts of good practice evolve, so too does the organisational structure of government. The current fascination with agencies will not be the last instalment. In fact, one should not be surprised if integrated departments return to favour in the not too distant future.

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Managerial developments are not the whole explanation, however. They tell us why the few countries that have adopted the tenets of New Public Management (NPM) have created agencies; they do not explain why other countries that still have old fashioned public administrations have also established quasi-autonomous agencies. This paper hypothesises that the agency movement has profound implications that affect the role and capacity of the state. Creating agencies may be part of a process of breaking up the state into political enclaves, each with its own interests, power base, and financial resources. Departments were the building blocks of the 20th century state; the disestablishment of departments may be a hallmark of the post-modern 21st century state. The 20th century state was predicated on the concentration of power, the emerging 21st century state may be built on confederate lines, with agencies, sub-national governments, and NGOs vying with the nation state for legitimacy, resources, and authority. If this argument is valid, and it will require more than creation of some agencies to confirm it, then much more is at stake than the configuration of organisation units.

Defining agencies as instruments of management skews the discussion to questions of efficiency, such as: Is the civil service more or less productive when it is employed under an agency model than in centralised departments? Are agencies more willing to innovate than entities housed in departments? Broadening the issue to governance gives rise to questions concerning the changing role of the state, its control over devolved entities, and relationships with citizens. At this stage of analysis, one can only suggest a few of the many questions that may warrant consideration. These include: Does the government have the capacity and will to effectively oversee the actions of its agencies (and other devolved entities) and to intervene when appropriate? How should policy-making be linked to service provision, and what should be done when those who command the two sets of processes clash?

A number of writers have grappled with the difficulty of labelling agencies. Because they are diverse in structure and function, agencies do not fit under a single rubric. Some are within departments, but have operational freedom; some are free-standing units that have no formal links to departments. Some are new units established when the government took on new responsibilities; some are old units that have been restructured. The roster of agency functions includes regulation, policy advice, service delivery, tax collection, police work, technical assistance, research, and just about every activity found within government. The only common element is that agencies are not departments, that is, they are not conglomerations of multiple activities. The typical agency has a single or relatively narrow purpose, and each has substantial operating independence, even if it is still housed within a department.

Every agency has its own story, but all the stories are the same. To be an agency is to be an alternative to organisational integration. This facet of agency proliferation is captured in the Canadian concept of agencies as “alternative service delivery” units. Inasmuch as many agencies are not service providers, the

label is unduly constrictive. Nevertheless, the word “alternative” conveys a sense of where agencies fit on the organisation map. They are not just free-standing entities, they challenge long-accepted practice. (The word “alternative” is often used to connote anti-establishment behaviour. Thus “alternative medicine” refers to treatment that does not conform to conventional practice, and “alternative dispute resolution” refers to mediation and other non-adversarial means of resolving legal disputes.) The “service delivery” part of the label also is revealing, for it suggests that this has become the defining role of the state. If it is, what special status, if any, is conferred on the state as a service provider? Does it have a superior claim in performing this role compared to other providers? How is the character of the state transformed by depicting service as its principal responsibility? Does the “service delivery” label mean that the big questions on the scope and boundary of the state have been settled, at least for the time being, and politics revolves around lesser issues of how its job should be performed?

In suggesting that agencies are alternatives to centralised government, no claim is made that promoters of this model purposely seek to weaken the state. On the contrary, many proponents argue that the state will be strengthened by freeing up central organs, such as the Cabinet and the Finance Ministry, to shape policy and monitor performance. Rather than being captured by service providers, policy-makers would keep their distance from them, thereby preserving their capacity to set objectives, communicate expectations, and assure that their instructions are carried out. Cordoning off service provision in agencies would clarify the responsibilities of politicians and managers, and give ministers incentives and tools to hold providers accountable.

In assessing the agency model, one should pay less attention to motive and more to effect. The motive might well be to strengthen those at the top, but the reality might be a lot different. Once service providers gain operational independence, the state's monopoly in the authoritative exercise of governmental power is undermined. Nominally, agencies are (as the word denotes) agents of the state; in fact, however, they often act in their own interest and empowering them with administrative independence gives them license to pursue self-interest. It is for this reason that the rise of agencies has the potential to challenge the state.

In light of the foregoing discussion, it is appropriate to consider both the managerial and governmental roots and implications of agencification. Section 1 views agencies as instruments of management, and as means of enhancing efficiency in public administration. Section 2 reviews some of the conceptual roots of agencification. Section 3 deals with the implications for governance, especially as regards legitimacy in the exercise of power. The concluding section suggests that agencies may generate a counter-reaction to preserve the state's cohesion and special status. Such a counter-reaction is already underway in some countries that have most fully embraced the agency model.

1. Agencies as instruments of management

Agencies are an old idea that has been invigorated by contemporary management reform. The typical government had agencies before it had departments. When it added a new activity that could not be accommodated within an existing organisation, government created a new agency, not because it had a grand design but because it needed to have an organisation responsible for the work. The expansion of government inevitably led to the proliferation of agencies and to an over-extended span of control, weak co-ordination of related activities, and an unruly public administration. Most governments responded to this predicament by consolidating the separate agencies into functionally integrated departments. Thus, just as agencies are now valued in some countries as antidotes to over-confining departments, departments were once the favoured solution to the excessive fragmentation of agencies. Historically, departments and agencies have been rival forms of organisation: Departments have multiple subdivisions and responsibilities; agencies have a single responsibility and a simple organisational structure. Departments promote integration, uniformity, rule-driven behaviour; agencies promote diversity, adaptability, and self-governance.

The form of organisation makes a difference. One cannot argue that the contemporary flight to agencies is significant without also recognising the importance of the departmental form. Organisation structure makes a difference because it influences who has power and how services are provided. One should think of organisation structure as a boundary that influences behaviour just as the geographic boundaries of countries do. In particular, organisations matter because they determine whether related activities are integrated or separated, and whether policy and services are conjoined or de-coupled. The linkage of related activities and of policy and services have managerial and political implications.

Every national government has a portfolio of activities, some of which have no salient connection to one another, but some of which do. National defence and lower education are examples of the first situation; providing job training and unemployment benefits may be examples of the second case. There is no basis for placing defence and education within the same organisation; job training and unemployment services, however, may either be placed in separate agencies or integrated in a department that is responsible for other income support schemes. Having separate agencies encourages managers to give singular attention to their assigned responsibilities; integrating related activities in a department encourages managers to co-ordinate their work. Inasmuch as both a sharp focus on services and co-ordination are desirable, there is no permanent solution to this organisational issue.

A similar problem vexes the connection of policy work and service delivery. Every democratic government must both connect and separate its political and

administrative organs. It must connect them so that managers and other service providers comply with the policies and rules laid down by political leaders. But it must also disconnect administrative matters from direct political involvement so that managers are free to act in a fair and efficient manner, without regard to political considerations. No democracy can abide governing arrangements which free managers to disregard the policies made by duly selected leaders, and no democracy can allow politicians to intrude in administrative matters without regard to the rights of interested parties. The first criterion justifies the placement of operating units within departments headed by ministers or by senior managers appointed by them; the second dictates the operational independence of administrative units. Striking the right balance between co-ordination and subordination on the one hand and independence and flexibility on the other requires that politicians and managers be both empowered and restrained. Each must have authority and resources to carry out basic responsibilities, and each must be deterred from acting in ways that encroach on the other's domain. The result is an organisational map that is repeatedly restructured through legislation and practice to promote one vision or the other.

In drawing organisational boundaries, a key issue is whether the greater concern should be to promote policy coherence or to protect administrative due process. Where the former predominates, government agencies are likely to be consolidated into functionally integrated ministries or departments corresponding to the main sectors of public policy – transport, education, health, etc. But when administrative independence and responsive services are the paramount considerations, activities tend to be dispersed among free-standing agencies, many with their own boards. The former results in a small number of large organisations; the latter typically ends up with a large number of small organisations.

Through most of the 20th century, the functionally integrated model predominated in democratic countries. But this was not the prevailing arrangement during the 19th century. In the early years of the administrative state, the preferred practice was to separate politics and policy from administration by establishing independent entities to handle new governmental responsibilities. It was widely accepted at the time that government is more efficient when administration is walled off from political influence. Independent agencies were associated with other administrative reforms, such as standardised accounting systems and a meritocratic civil service. But as national governments expanded their activities and added free-standing agencies, many were troubled by an overextended span of control, inadequate co-ordination, and lack of uniformity in administrative procedures. These concerns spawned an administrative counter-movement to merge the previously separated entities into departments.

Sweden was one of the few countries to abjure functionally integrated departments. It elevated agencies to constitutional status by barring ministers from

intervening in particular administrative cases. This “ministerial rule” doctrine does not prevent the government from providing policy guidance to agencies, but it has been applied in ways that give agencies substantial operating freedom. The Swedish model is said to have influenced a number of countries to establish independent agencies.

In contrast to Sweden, during the 20th century, most countries departmentalised their public administrations. Functional integration in government paralleled, and was strongly influenced by, vertical integration in business organisations. The latter internalises within the firm production and assembly of the various components that go into final products; the former internalises within the department the various activities contributing to the same objective. Vertical integration enables the firm to more fluidly co-ordinate production. During the heyday, vertical multi-national firms (such as General Motors) dominated their markets and reaped huge profits. The evidence appeared compelling that this form of organisation was more efficient than firms beholden to outside suppliers.

Functional integration in government led to a relatively small number of departments, typically no more than 15, each of which contained related activities which may have previously been assigned to separate agencies. Once functional integration became the norm, governments habitually placed new activities within pre-existing departments. Exceptions were common, however, and it was a rare national government that had no agencies outside its departmental structure. Moreover, specialised bureaux within departments carried out particular tasks, so that the traces of agencies were not entirely erased by functional integration. But the bureaux operated within bureaucracies, that is, within large organisations that imposed uniform rules and procedures on their constituent units. Some bureaux had *de facto* independence; most, however, were truly subordinated by their departments.

Functional integration joins policy-making and service delivery in the same organisation. It assumes that a close linkage of the two is beneficial because operational results can feed back to policy. Although integration makes for an elongated, hierarchical chain of command, in its heyday it was thought to reduce administrative costs and friction, facilitate oversight by headquarters staff, reduce the number of officials reporting to political leaders, encourage co-ordination of related activities, and promote uniformity in the provision of public services. Of course, governments that have recently established independent agencies reject this classical view of public administration. They see functional integration as inefficient because it values compliance over performance and uniformity over initiative.

Functional integration does not itself resolve the question of how policy advice and service delivery should be linked. Although they coexist in the same department, there is still a need to distinguish one from the other. Several devices

have been introduced over the years to maintain separation within an integrated framework. One is to reserve top positions for political appointees, but to require that the remainder be set aside for career civil servants. Another is to impose procedural rules that assure administrative due process free of undue political influence. Such rules specify how civil service positions are to be filled, purchases made, the form of accounts, and other administrative procedures. The effectiveness of rules within integrated organisations often depends as much on behavioural norms as on legal constraints. Within a country's political administrative culture, there are informal understandings of where the boundaries are drawn and how they are enforced, when and how politicians may intervene in administrative matters, how contract between political and official levels is to be maintained, and so on.

To obtain the benefits of functional integration, it does not suffice that policy and operations be separated; it is also necessary that they be linked. In blueprint, the relationship is supposed to work fluidly by having policy guidance and procedural rules flow downward, and information on activities and services flow upward. Policy-makers would tell administrators what to do (and not to do) and would provide the financial and organisational resources to carry out assigned tasks, while managers would report on their work and on compliance with the policies and rules handed to them. Audits would verify the reliability of reported information and evaluations would assess the effectiveness of policies. Of course, the relationship between policy-makers and advisors rarely conforms to this blueprint. In practice, it is apt to be more interdependent and less hierarchical. Managers make policy and policy-makers often dictate how activities are to be managed.

Functional integration generates both co-operation and conflict. Sometimes, policy-makers and managers work side by side, without regard to status or formal roles. They fight on some matters and agree on others, and there are zones of indifference – matters on which some have a strong interest but others do not – which enable them to co-exist in the same organisation in relative harmony. Formally, policy-makers have the upper hand when interests collide; in fact, however, subordinates may have the advantage because they can withhold or manipulate information on what they are doing to subvert their departmental masters. Agents can opportunistically protect their self-interest because they know more about what is happening within their areas of responsibility than principals do.

2. Agencies as instruments of New Public Management

The principal-agent problem, which arises out of the differentiation of interests among those who work in hierarchical organisations (and in other settings) and asymmetric information on organisational activities and performance (principals are dependent on subordinates for much of what they know about services

and results) is one of the main conceptual drivers in discrediting vertically-integrated firms and functionally-integrated departments. While they once were seen as business superpowers that dominated their markets, many vertically-integrated firms such as General Motors now are regarded as organisational dinosaurs that are inefficient, captured by their internal suppliers, and slow to change. Nowadays, many successful firms outsource production, and rely on external suppliers for various administrative services such as payroll, product design, and marketing. The “virtual” firm, which is divested of all functions other than its strategic core and contracting activities, is rare, but so is the fully-integrated firm.

Disintegration has not advanced as far in public institutions, for most national governments still house major activities in big departments. Although all national governments have some agencies, only a few have reorganised their public administrations on this basis. Stray agencies tend to be creatures of expedience; they are often established because it seems the sensible thing to do in the particular case, not to fulfil some grand design. But when a country purposely de-couples agencies from departments, it is likely to be motivated by the argument that independent, single-focus entities are more efficient than departmentalised ones. For some governments, the logic of agencies is rooted in the innovative concepts and practices of New Public Management (NPM). Stripped to its essentials, NPM asserts that the performance of public organisations is enhanced when managers are given operating discretion and are held accountable for their actions and results. The operational independence of agencies is only one of NPM’s innovations, others such as performance targets and contracts may be dependent on the agency model.

Successful innovations have many parents, and NPM is no exception. It has roots in classical public administration where the argument has long been made that civil servants cannot be held accountable for performance if they lack freedom to manage, and in business management where the capacity to mobilise organisational resources defines effective leadership. One of the main conceptual roots is in “new institutional economics”, a field that focuses on principal-agent relationships, transaction costs, incomplete contracts, and other notions to explain why integrated organisations may be less efficient. It would take this paper too far afield to analyse these and other concepts, but it is worth stressing that the form of public organisations is strongly influenced by the form of business organisations. The influence may not be direct or immediate, but over time it is the most powerful explanation of change in the structure of public administration.

NPM has two core principles: One is to “let managers manage” by deregulating the use of operating resources; the other is to “make managers manage” by specifying what is expected of them and measuring their performance against these expectations. This *quid pro quo* – giving managers discretion in exchange for strict accountability – is promoted by carving out a specific area of responsibility

for each agency and empowering its managers to operate as they deem appropriate. But having been given discretion, managers must openly account for what they have done and accomplished. The two sides of the bargain are supposed to be interdependent: It is not reasonable to make managers accountable for performance if they are not free to manage; and it is not prudent to give them operating freedom if their performance does not matter. In practice, it often is much easier to fulfil the first part of the bargain than the second. It is much easier to divest administrative controls than to enforce strong accountability. This is certainly likely when expedience is the justification for agency independence. In these situations, it is easy to forget about the accountability part of the bargain.

Properly organised, agencies contribute to both operational efficiency and managerial accountability. Even though it has operational independence, each agency should be clearly responsible to its minister or parent department. Having been separated from its department, an agency remains tethered to it by means of performance targets that give advance notice of what is expected, contracts or framework documents that spell out its responsibilities, and reviews and reports which assess results. Performance is the shared concern of departments and agencies; it should foster an ongoing dialogue between the two sides to the relationship. It should link policy and operations; politicians and managers; money and programmes; plans and results. It depends on a steady flow of data on what is expected and has been accomplished, as well as on key persons who maintain watchful vigilance over actions and results. If those in authority don't pay attention to performance, measurements and other information will be of little value.

The NPM template for implementing the agency model is best exemplified by Britain's Next Steps initiative which was launched in 1988 and has been characterised by a parliamentary committee as the most ambitious management reform of the century. The core idea of Next Steps is summed up in a government report that recommended agencies "should be established to carry out the executive functions of government within a policy and resource framework set by a department". Although the first part of this recommendation has received most attention from countries that have sought to imitate Next Steps, the second part, which refers to the parent departments' role, warrants equal emphasis. Next Steps freed agencies to operate under the tutelage of their departments. Whitehall, the phalanx of British departments, was not dismantled; it plays a critical role at every stage of agency existence – from initial consideration of whether a particular activity should be entrusted to an agency, to thorough review of the candidate agency's resources and mission, launch of the agency, ongoing review of performance and periodic assessment of whether it should be continued.

Although few governments have fully adopted the British model, many have been influenced by it. Agencies would not be in the vanguard of organisational change if Next Steps or a similar innovation had not become an international suc-

cess story. In view of Next Steps' salience in the contemporary agency movement, it is important to comprehend its underlying rationale and mode of implementation. Derek Lewis, the former head of the Prison Service who was removed from his post by a minister dissatisfied with his performance provides a splendid explanation of Next Steps:

It was a myth that ministers ran major government services such as the Benefits Agency or the Passport Office; they had neither the knowledge or the skills to do so. But as long as the myth persisted, the civil servants, who were really in charge of the day-to-day operations, were not being given the authority to get on with the job, nor were they being held responsible for the performance of the agencies. The intention of Next Steps was to describe more precisely the respective jobs of ministers and civil servants, and to get away from the confusion that had persisted hitherto. Ministers would be responsible for setting policy, approving the agencies' plans, setting targets and monitoring performance; the civil servants in charge would be given the autonomy to get on and make it all happen. The performance of the agency and its chief executive would be closely monitored by key performance indicators ... Agency status also brought with it many tools that were commonplace in the private sector. The essential were: Clarity of roles, operational autonomy, the delegation of decision-making and holding agencies and their chief executives responsible for results.

Measured against these aspirations, many contemporary agencies in other countries fall short of the mark. Governments have granted independence without either clarifying roles and responsibilities, or putting the machinery of accountability into place. In many countries, agencies have been misbegotten at their creation, and it is highly unlikely that they will be set aright after that, for they have acquired independence without paying for it in the currency of performance. So little has been demanded of them at the outset that it is hard to ask more from them later on. One of the neglected lessons of Next Steps is that what happens before an agency is launched has a direct bearing on how it performs afterwards. Few countries have replicated the care with which Britain examined each candidate for Next Steps status before deciding whether and how to proceed.

In the Next Steps process, agencies go through a life cycle that typically consists of eight stages:

1. *Candidate status* in which an entity (or activity) is designated as a candidate to become an agency. This stage lasts three to nine months, during which an assessment is made of the appropriateness of this form of organisation.
2. *Prior options* is a formal review which considers the entity's mission and alternative ways of performing it.
3. *Ministry-agency relationships* are clarified, including matters on which the agency will be authorised to govern itself.

4. A *framework document* formally spells out the agency's objectives, operating conditions, responsibilities of the chief executive, relationships with the parent department, and various financial and personnel arrangements.
5. A *chief executive* is recruited in open competition and employed under a term contract that specifies working conditions and performance expectations.
6. *Performance targets* are published each year, giving the agency explicit notice of how its performance will be assessed.
7. *Annual reports* compare actual and targeted performance and include audited financial statements.
8. *Periodic reviews* are conducted at least once every five years to evaluate how the agency has performed and to consider changes in its operating charter.

Every country that sets up agencies does so in its own way. Some, like Britain, proceed via administrative processes, some do so via legislation. Some act in a piecemeal manner, establishing an agency when it deems it ripe to do so; some introduce a comprehensive process for conversion to agencies. Regardless of the approach, however, all governments have to grapple with the questions considered in the Next Steps process. Doing so before an agency is established enhances the government's capacity to balance independence and accountability.

3. Agencies as instruments of governance

Judging from the reasons provided by various governments, agencification has been driven by managerial considerations. But conditions of agency creation suggest that political factors are also at play. In most cases, decisions on agencies are made by political leaders who see something in this format that makes sense to them. Moreover, where it is implemented, the agency model has important, sometimes profound, implications for the role and authority of ministers, and the capacity of government to make and enforce policy. Countries that create agencies are not merely importing a new administrative structure; they are making big changes in the operations of government. Inevitably, therefore, political factors weigh heavily in decisions to establish agencies.

To probe the political logic of agencies, one might inquire: What has happened in the role or conduct of government that makes it receptive to this form of organisation? Agencies have arrived at a particular time in the evolution of democratic governance. What is distinctive about this time that renders integrated departments less politically appealing and single-focus agencies more so? One clue in addressing this issue is to focus not on what has changed, but on what hasn't. During approximately the past two decades, the size and scope of government in developed countries has been remarkably stable. National governments

have neither rolled back the boundaries of the modern state, nor have they expanded it. Few have seriously tried to do either. Of course, within the state there has been ongoing realignment of programmes and some substitution of new activities for older ones. Although one should be cautious in generalising across countries that are at different stages of political or policy development, it appears that many of the big governance questions have been settled or put aside, at least for the time being. This was the theme sounded by US President Bill Clinton in his second (1997) Inaugural Address: "... we have resolved for our time a great debate over the role of government. Today, we can declare government is not the problem, and government is not the solution." A similar sentiment has been expressed by Jonathan Rauch, an American political journalist, in his 1999 book, *Government's End*, "... it is possible that the government has reached its end... its overall scope and shape is no longer negotiable. They have evolved to a state from which they cannot, if you will, unevolve". If Rauch intends this conclusion to be an immutable statement on the future of government, he is certainly wrong for the current equilibrium might turn out to be only a pause. But as a statement of democratic politics in our times, his conclusion appears to be valid, not only for the United States, but also for the many other advanced democracies where, despite the political rhetoric, there is little programmatic difference between left-of-centre and right-of-centre governments.

The boundaries of the contemporary state are well demarked in the developed world. They include traditional watchman functions, such as the maintenance of law and order, protection against external threat, and basic health and safety measures. As vital as these are, in most national governments, these traditional roles account for a declining proportion of public employment and expenditure. The bulk of public human and financial resources is allocated to the direct provision of services or to financial support. Ours is an age when the definitive role of the state is as a service provider or financier. This is a leading factor in the emergence of agencies, which in Canada and other countries, are predominately service-providing organisations.

A service-providing role portends a fundamental transformation in the relationship between governors and governed. Where this relationship was once defined in terms of the rights and obligations of citizens, it is now often characterised in terms of the entitlement of customers to public services. This difference goes beyond labels, for it connotes not only that the language of business has penetrated the public sector, but that government performance is defined through terms and concepts more befitting a commercial than a political relationship. At first consideration, it may appear shocking that people may have greater leverage *vis-à-vis* government as customers than as citizens. But citizenship invests people with a limited voice and virtually no power of exit; customership arms them both with voice and exit. In today's world, it is the customer who is sovereign, because

contemporary governments have been socialised to give primacy to services; this is why the state has grown so large and why efforts to cut it down are so feeble. And this is what the demand for performance is about.

With its boundaries marked out and the big questions resolved, at least for the time being, the policy functions of government have become somewhat attenuated. Can anyone claim that today's governments in the OECD community make policy with a reach comparable to that made by predecessor governments a generation or more ago? True, there is much more formal policy analysis than was previously available, but much of it is tinkering at the margins of the relatively fixed boundaries of the state. Much of what parades as policy analysis these days deals with efficiency in the provision of services. Policy analysts compare the costs and benefits of alternative delivery systems; they do not have much role in setting the boundaries.

The agency model is a congenial form of government for the provision of services. In contrast to the departmental structure, it purports to separate policy from operations, and to give each agency a clearly defined focus on the service for which it exists. A department has a portfolio of responsibilities; an agency has a specialised responsibility. It is noteworthy that Australia has been one of the few governments to counter the agency trend, preferring to group programmes in broad portfolios rather than separate them in individual agencies. Australia has been an outlier in yet another way, making much larger policy and programme adjustments than have been tried in other OECD Member countries. Departments made sense for Australia; agencies were the preferred way for other countries.

Without stretching the analogy too far, one can think of agencies as the "boutiquing" of government. In the same way that modern department stores often are organised into specialised boutiques, each with its particular market niche, the modern government department is divided into boutique-like agencies, each with its particular line of work. And as each boutique is a profit centre in the department store, each agency is a service centre in government.

This perspective drives governments to have more rather than fewer agencies. The logic of departments is that they should be few in number, so that cognate activities are grouped together; the logic of agencies is that each service should have its own unit so that none is neglected. An agency that has multiple tasks can be expected to perform one or more of them poorly. An agency with a singular task has an incentive to perform its sole responsibility well.

The service providing state is a state whose performance is measured, targeted, reported, audited, analysed, budgeted, and so on in contemporary life. After all, performance is what service is all about, whether it is defined in terms of access, efficiency, volume, courtesy, or other qualitative or quantitative dimensions. The word performance tells us that the boundaries have been set, now

perform – that is, get on with the job. There would be little service to measure if government were not in the business of providing services. Performance, like services, de-politicises government. It is the common interest of liberals and conservatives, and parties of most political stripes. In the 2000 American presidential election campaign, Vice-President Al Gore noted that while he and his opponent George Bush disagreed on various educational issues, “we both are in favour of having new accountability on schools, new performance measurements”. Consensus on performance crosses party lines because all sides are assessed by citizen *qua* customers in terms of the quality of public services.

But where there are services, there are alternative means of delivery. As policy-maker, government has unrivalled authority organs of state power. As service provider, government is only one option, for it has no monopoly on who or how services are provided. Britain’s National Health Service, for example, was built to provide universal, uniform care for all citizens. Over the years, however, it has faced growing competition from private providers who charge for their services.

As service providers, national governments have at least three competitors: Sub-national governments, non-governmental groups (NGOs), and business firms. Each is reputed to have advantages, which have led some countries to take some direct service responsibilities from the national government, leaving it with a financing role. Sub-national governments are closer to the customer and can adjust their services to local needs and interests. The rationale for fiscal decentralisation is similar to that used in making the case for agencies: Government should be responsive and flexible, and should not insist on one-size-fits-all services. National governments and big departments are too remote from those they serve, too wedded to uniformity and procedural rules to give adequate attention to their customers. In some countries, decentralisation may be a prerequisite for reaping the benefits of agencification.

The same logic explains the contemporary fascination with NGOs. In poor countries, NGOs often are promoted or financed by international organisations in the expectation that they will be more honest, caring and efficient in bringing services to the truly needy; in developed countries, they may be financed by the government as a means of enhancing efficiency in public services. In some developing countries, NGOs have acquired informal recognition as substitutes for the government. They are seen as having a legitimacy that the government itself lacks. This broader concept of NGOs opens up troubling questions about democratic legitimacy which have been conveniently shoved aside by caring more about the rights of customers than of citizens. If government habitually fails to perform, why not bypass it altogether and rely on NGOs instead?

Business organisations are the third type of substitute. In almost every democratic country, public services are still overwhelmingly provided by public

organisations, but the definition of “core” has shrunk in some countries. Some consider air traffic control as an appropriate candidate for privatisation; some have contracted out policy advice; many rely on commercial firms to audit their financial statements. Some view agencies as a springboard for privatisation; others see them as a means of retaining service delivery in public hands. These distinctions aside, it is increasingly accepted that government and business are alternative service providers, and that choosing between the two should turn on which does a better job. Furthermore, it is now widely accepted that for government to be an efficient service provider, it must be organised along business lines, with managers given latitude to use resources as they deem appropriate.

Herein lies the fundamental challenge of agencification – not that it parcels out responsibility among quasi-autonomous enclaves, but that it is a key part of rethinking the role of the state. In an historical perspective, the state is special as the national repository of public authority. This specialness is being eroded for while the state may have a monopoly in exercising governmental authority, it does not have a monopoly in providing services. Services do not depend on legitimacy and authority, but on getting the job done, satisfying customers, and efficiently producing outputs. Once the state is cast as a supplier, it is prudent to select the form of organisation and mode of delivery that are best suited to the particular task, even if the upshot is a weakened state. In the service-oriented state, performance matters; in designing organisations, it may be the thing that matters most.

4. Restoring departmental capacity

Is it possible to reconcile a service-providing, agency-structured government with a strong, effective state? The answer is “yes”, but doing so requires a shift in focus from agencies to departments and ministries. The key question should be not whether agencies have freedom to operate efficiently, but whether departments have incentives and opportunity to effectively guide the agencies responsible to them and to oversee their performance.

In some countries, government weakness is regarded as a virtue. This may be the case in those transitional countries which have embraced various reforms that dismantle the command and control structures erected during their communist past. Agencies, privatisation, fiscal decentralisation and devolution of administrative responsibility are means of constraining state power. In these countries, the rationale for agencies has more to do with political ideology than with managerial performance. These countries will not move forcefully to reinvigorate the state until they stop being more concerned with over-centralisation than with performance.

In contrast to these countries, most countries that have converted to the agency structure have been swayed by the argument that this move will strengthen the state by clarifying missions and objectives, enabling central authorities to set per-

formance targets and monitor results, and giving agents (those who provide services) incentives to perform according to the dictates of their principals (those in parent departments and central organs). This theme is echoed in the popular management literature which urges governments to steer, not to row. After all, this is the way successful businesses are managed; it should also be the way effective business is run.

Improperly applied, the steering rather than rowing prescription may lead to government that does neither well. Two problems come into play: The freedom that agencies exploit when they gain operational independence; and the capacity of ministries and departments to provide policy guidance and oversee results. It is naive to assume that agents who opportunistically pursue their self-interest when they are formally controlled by principals will be more compliant when they are organisationally independent. It may be equally naive to assume that departments which give inadequate attention to service performance when operations are run by their own administrative subdivisions will be more attentive when services are hived off to independent entities. Principal-agent problems are more likely to arise out of asymmetries in salience and attention than in information. To put the matter bluntly, agencies care more about their services and performance than departments do. The British Government was able to implement Next Steps without encountering opposition from Whitehall because the big departments didn't care much about services and felt little loss when they were relocated to independent agencies. Why should they care more about services now that agencies have operational independence?

In the agency model, too much emphasis is placed on the operational independence of service providers and not enough on the behaviour of departmental overseers. For the relationship to work, that is, for agencies to comply with the policies and targets set out by those to whom they are formally responsible, it is not enough for managers to be free; their departments must actively guide and vigorously monitor what they do. To assess how well the agency model is working, one must examine whether the parent department is living up to its responsibilities.

Sweden is a case study of how difficult it may be for ministries to guide and oversee agencies. With as many as 300 agencies which employ upwards of 98% of state employees, the 12 ministries are not up to the task. Not only are agencies protected by the doctrine of ministerial rule against outside interference, the meagrely staffed ministries devote most of their resources to Cabinet and legislative work, and other policy or political matters. If they assign anyone to watch over agencies it is likely to be a junior person, not someone with real authority. Since the mid-1980s, the Swedish Government has taken a number of initiatives to enhance its ability to guide agencies and monitor their performance, but none have been particularly successful. These initiatives have expanded the operational discretion of agencies, established a multi-year framework for specifying

policies and performance targets, required agencies to report on results, and strengthened the audit process. The government has also overhauled the budget process to focus on results, and it has used the annual "Letters of Instruction" from ministries to inform agencies of the performance expected of them in the next year. Despite these moves, the government appears to be only marginally more effective in steering agencies than it was when the reforms were first launched more than a decade ago. The mismatch in agency-ministry staff is so great that the government has limited capacity to pay attention to agency performance. In Sweden, there is an ongoing dialogue between ministry and agency staff, formal and informal discussions throughout the year which partly compensate for imbalances in the relationship. Nevertheless, the fact that the government has felt impelled to introduce a series of reforms attests to the perception that it lacks means to steer its many agencies.

New Zealand's managerial system is centred around chief executives who have full responsibility for their departments. However, departments account for less than half of the money that is financed by the state budget. Most funds and many key services, such as health care and education, are provided by Crown Entities, non-departmental bodies that have broad operational autonomy. There are approximately 70 Crown Entities, plus 2 600 school boards. Most Crown Entities have a policy-making board which appoints the chief executive. Each Crown entity has its own accountability framework which typically includes a Statement of Intent negotiated with the responsible minister and an Annual Report. Despite these arrangements, studies by the Treasury and the State Services Commission have found serious deficiencies in the relationship between government and its Crown Entities. These include: Uneven and inadequate monitoring by departments and inattention by ministers to the Crown Entities for which they are responsible; unresponsiveness or disregard by Crown Entities of government policies; incomplete and inconsistent accountability requirements; and inadequate governance arrangements, along with confusion over the legal status of some Crown Entities. The government has drafted legislation to clarify the status of Crown Entities, but the heterogeneity of agencies has complicated the task of resolving this matter.

The British experience is most instructive, not only because the reputed success of Next Steps has spurred other countries to adopt the agency model, but because the Blair Government that came to office in 1997 has distanced itself from agency-centred public management. Without disowning Next Steps, it has shifted the focus from agencies to departments and the centre of government. A clue to this reorientation is contained in the 2000 *Next Steps Review* (relabelling the *Executive Agencies Review*). In contrast to the previous editions of this annual publication which listed agencies in alphabetical order, the Table of Contents of the 2000 Edition only lists the departments; it has no entries whatsoever for agencies. This may seem a small matter; it is not. The rationale for focusing on agencies is that citizens

should have easy access to those who serve them. Restructuring the report is one of a number of signals given by the Blair Government that agencies are to be subordinated to departments, and that the latter are to be the instruments by which government formulates policy and sees to its implementation.

While the Blair Government still says positive things about Next Steps, it has a modernisation agenda that depends on strong policy direction from the centre of government. Modernisation aims to make services more responsive and to improve their quality, but in contrast to Next Steps which pursues this objective through fragmentation, it does so through policy and organisational integration. Moreover, instead of separating policy from operations, modernisation wants them joined. The government issued a Modernising Government White Paper near the end of Blair's first year which did not even mention the Next Steps initiative. Instead of removing services from departmental custody, it made them central to departmental performance, and rather than relying on agencies for service performance, it placed responsibility on departments. In a sharp break with the logic of agencies, the White Paper relied on departments to take the initiative in promoting change. "Within Whitehall", the White Paper insisted, there should be "a new focus on delivery – asking every permanent secretary to ensure that their department has the capacity to drive through achievement of the key government targets and to take personal responsibility for ensuring that this happens".

Where does this department-centred strategy leave agencies? Agencies have survived, but with somewhat less autonomy than the initial design promised. Excessive independence, the modernisation logic dictates, gets in the way of policy cohesion and service integration. This theme is sounded in *Wiring It Up*, a manifesto on integrated service delivery published by the Cabinet Office in 2000. Revealingly subtitled, "Whitehall's Management of Cross-Cutting Policies and Services", this report demands stronger leadership from ministers and senior civil servants and it urges "using the centre (Number 10 [Prime Minister's Office], the Cabinet Office and the Treasury) to lead the drive to more effective cross-cutting approaches whenever they are needed". The report extols the Whitehall vertical management structure "because it is "highly effective in delivering many of the government's key policies". The model favoured by the Blair Government is hierarchical, with rules and guidance flowing down, and information flowing up. *Modernising Government* has a different view of public management than the one on which Next Steps is based. The agency model promotes the break-up of the civil service into administrative enclaves, each with its own salary and working arrangements. *Wiring Up Government* insists, as its title suggests, that civil servants should become accustomed to working across organisational boundaries. This report envisions the central government working to co-ordinate and improve the delivery of services. The critical relationship would be between government departments and local authorities; agencies would participate as departmental subdivisions, not as independent entities.

The Blair Government has expanded the annual expenditure review process into a means by which departments negotiate formal Public Service Agreements (PSAs) which specify the outcomes and results they will accomplish in the next three years. Recent PSAs, for the 2001-2004 fiscal years set out approximately 160 “commitments which the government can be held accountable for, and which departments will report on every year in departmental reports”. The role of agencies in the PSA process is to contribute to achieving departmental objectives. The approach is top-down: “high-level performance targets”, the 1999 Next Steps review stated, “will be cascaded to agencies to assist their attainment”.

The government requires that each Next Steps agency be reviewed at least once every five years. The latest instructions for these reviews stress that “agencies do not exist in isolation from the rest of government, and so greater emphasis will be placed on considering the performance of agencies in the context of their contribution to wider departmental and governmental objectives”. From a strictly legal perspective, the new emphasis does not change agency-department relations. Departments are formally accountable for policy guidance, programme co-ordination and service results, just as they always have been; and agencies still are accountable within their respective spheres of operations for costs and outputs. However, the new attention to departmental responsibility for services inevitably eats into agency autonomy. Agencies are to do their department’s bidding, even if it means doing things the department’s way rather than their own.

Much more is at stake in this realignment than operational relationships between departments and agencies. The Blair Government has taken charge of the instruments of management to promote its policy ambitions. Aided by a re-focused Treasury and a large, active Cabinet Office, Blair runs government from the centre, with the Public Service Agreements representing commitments by which the government itself will be measured. Blair’s interests lie in policy and results, but he knows that services connect the two. If the modern state is perceived to be a service provider, as was argued earlier in this paper, then it would be untoward for the government to stand aside and allow agencies a free hand in providing services. In bringing agencies within the ambit of Whitehall, the Blair Government does not want to intervene in operating detail, except when its strategic aims are at risk. It does, however, want to ensure that agencies operate in accord with government dictates to produce the intended results.

Next Steps was a harbinger of the agency movement; it exerted a strong pull on governments that were seeking to modernise the public sector. Does the new stress on departments presage a rethinking of the agency model? Part of the answer lies in distinctive features of Next Steps. It was implemented by administrative action, without any change in the legal relation between agencies and departments. Ministers and permanent secretaries are as accountable for the use of resources and service results after Next Steps as they were before. Next Steps

gave rise to some knotty questions concerning the responsibility of agency chief executives, and occasional confusion as to who should answer to Parliament on particular matters. Nevertheless, because of the manner in which Next Steps was implemented, there is nothing to undo restoring departmental leadership. The Blair Government has been able to reassert departmental authority without formally retreating from Next Steps. Countries which have legally separated agencies from departments may have a tougher job if they want to reunite the two.

But even countries that have granted agencies statutory independence may be impelled to pull back a bit. As in Britain, the issue is not whether to have agencies – this form of organisation will thrive for some time – but whether agencies should be de-coupled from departments or subordinated to them. To the extent that all governments have a need to co-ordinate policies and services and to join up their many fragments of organisation, the British experience is instructive. Governments will connect agencies and departments; they will have both and neither will be independent of the other.

On this basis, one can foresee a pattern of government management that is different from what has been tried heretofore. Initially there were agencies, then they were swallowed into departments, and recently agencies gained substantive autonomy. Until now agencies and departments have been rivals. The ascendancy of one has spelled subordination of the other. In the future, departments and agencies will coexist, in close alignment, but with each having its own zone of responsibility. When things are going well, the two will stay out of each other's way. When they aren't, each may blame the other, and the challenge for government will be to make sure that accountability does not fall between the cracks.

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We regret we are unable to take unsolicited contributions to the *Journal*. We are, however, anxious to receive feedback from our readers. Your views on how to improve the *Journal* are welcome and can be sent to: The Editors, The OECD Journal on Budgeting, OECD, 2, rue André-Pascal, 75775 Paris Cedex 16, France. Fax: (33 1) 45 24 17 06; email: pum.contact@oecd.org.

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