

Beyond Privatisation: Government Strategies For Influencing Outcomes

By Peter Kenway, Guy Palmer and Keith Ruddle
With a preface by Professor John Kay

CONTENTS

	Page
Preface	1
1. Introduction	3
2. The Need For Radical Attention To The Delivery Of Services	5
A Mixed Inheritance	5
Non-plc Forms Of Service Delivery In Decline.....	5
The Inherent Limitations Of Regulation	6
3. A Unifying Theme For New Forms Of Government Action	7
‘Regulation By Values’	7
Regulation Of Society By Society	8
New Forms Of Enterprise	8
4. Strategies For Government Leadership	10
5. Tools For Pursuing The Various Strategies	12
Tools For Strategy 1 - Incentives And Deterrents.....	12
Tools For Strategy 2 - Stimulating New Institutions	12
Tools For Strategy 3 - Reviving A Service Ethos.....	13
Table 1 - Example Tools For Creating Incentives And Deterrents.....	14
Table 2 - Example Tools For Stimulating New Institutions	15
Table 3 - Example Tools For Reviving A Service Ethos.....	16
6. Conclusion	17

About The Authors

John Kay is Director of the Said Business School, University of Oxford.

Peter Kenway is Executive Director of the New Policy Institute.

Guy Palmer is Non-Executive Director of the New Policy Institute and a management consultant.

Keith Ruddle is Associate Fellow at Templeton College, Oxford University.

Published by the New Policy Institute

First published July 1998

New Policy Institute
103 Premier House
10 Greycoat Place
London
SW1P 1SB

Tel: 0171 222 8866 ext. 2116

Fax: 0171 222 3865

ISBN 1-9020-800-5X



PREFACE

John Kay

Towards the end of the 1980's, evidence started to become available which enabled comment on the British experience of privatisation to be based on evidence rather than rhetoric, ideology or assertion. Yet although the facts which emerged were relatively clear, their interpretation was complex. The firms which had been in public ownership in 1979 had, in general, shown marked improvements in performance. The timing of these improvements coincided with the government's commitment to privatisation - around 1983.

Yet these changes had occurred regardless of whether the business concerned had been privatised or when. The most spectacular changes had been achieved in British Steel and British Airways, under public ownership. The Post Office, for which there was until recently little question of any change in status, had done as well as any. And British Gas, although an early case of privatisation, was a laggard in terms of changes in its performance.

The lesson, which subsequent experience both in Britain and elsewhere has tended to confirm, is that it is not private ownership as such which is the key element. Better performance came from a set of changes in culture and control mechanisms which have been associated with privatisation, and which are perhaps most easily achieved under privatisation, but which are more subtle than can be registered in a simple chant of public bad, private good - or the reverse. Nor, despite some of the impressions given not only by Mrs Thatcher and reinforced by New Labour's love affair with business, is it that private business people have talents which are innately superior to those of public servants.

What has really mattered has been a revival of management autonomy, associated with a framework in which accountability is for results rather than for process, and which is after the event rather than before it. *How have you done?* replaces *Why are you doing that?* Now it is true that private ownership of firms in competitive markets is one of the best - perhaps the best - method of achieving that. Paradoxically, that is because the limitations of real accountability is the plc framework with separation of ownership and control and diffusion of ownership gives managers a great deal of short term freedom: while competitive markets impose tough sanctions on performance in the long run.

The key question today is how these benefits can be achieved in areas where this competitive market solution is technically or politically impossible. Technically impossible in those areas, such as the basic infrastructure of utilities, where monopoly is inevitable and some form of regulation has to be substituted for competitive market disciplines. Politically impossible where, as in education or health, the motivations of consumers and providers conflict with profit-maximising objectives - or where, as for law and order, the function is inescapably public. The challenge - one of the key political issues of the next decade - is to find institutional structures which are different both from centralised state direction or control and from competitive private ownership, but which incorporate the strengths, rather than the weaknesses, of each of these means of operation. That is the subject of this pamphlet.

1. INTRODUCTION

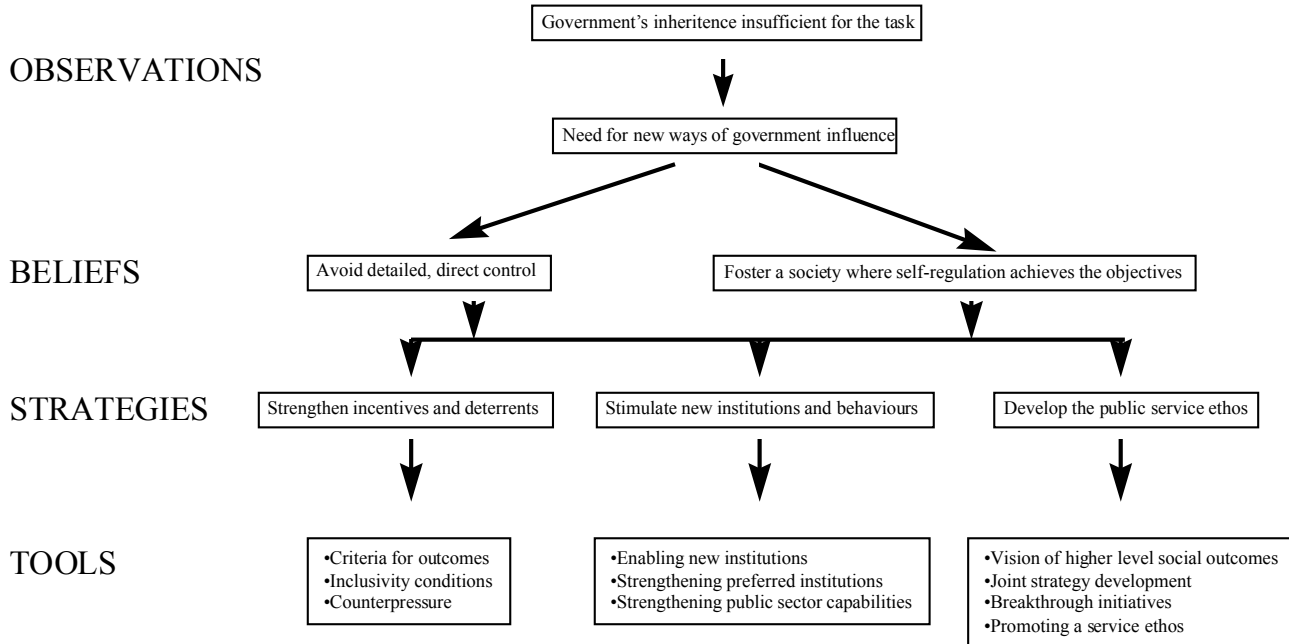
The performance of our major services, from health and education to the privatised utilities and personal finance, is of vital importance in modern society, both directly (because of the impact on citizens' well-being) and indirectly (because of the political significance and sensitivity). ***If the government is dissatisfied with the performance of a major service industry, what sorts of strategies does it have for doing something about it?*** Nearly a year into the period of office of a new government, with decisions to be made about a range of services and continuing public dissatisfaction with some key services, the time for such a debate is ripe.

The aim of this paper is to stimulate discussion about possible new forms of government intervention. It will be used to help the New Policy Institute plan a series of seminars and conferences around the general theme of government leadership.

Our involvement in two recent initiatives has suggested that the issue of new forms of government leadership is worthy of some debate and attention by government. First, Templeton College ran a substantial programme in 1996 with the (then) Shadow Cabinet and ministerial teams on the management of change in government and the role of the minister. These sessions stimulated lively debate on their emotional dislike of some of the Conservative managerial reforms, including privatisation (with its focus on financial objectives to the exclusion of social outcomes) and the loss of a 'public service ethos' in many privatised and public services.

Second, in a wide ranging seminar organised by New Policy Institute involving around 20 key thinkers in the area of the role of government, John Kay (Oxford University) and Andrew Adonis (the *Observer*) led a discussion critiquing the existing mechanisms for reforming service delivery and suggesting the need to investigate new models of intervention.

In this paper, we have tried to place the ideas and arguments discussed within a more general structure which is represented in the diagram below.



2. THE NEED FOR RADICAL ATTENTION TO THE DELIVERY OF SERVICES

A MIXED INHERITANCE

Especially in the latter half of their 18 year rule, the Conservatives paid substantial attention to the delivery of public and other services. Many public sector organisations were either privatised (e.g. the utilities), or brought into something of a pseudo-market (e.g. the health service). Regulated businesses operating in a (usually competitive) market became the order of the day, with a strong focus on managerial mechanisms and efficiency of operations.

But it is not clear how far the reforms have actually benefited the consumers, and whether the above model can successfully deliver higher level social objectives. A possible assessment of the Conservatives' record in the field of services is:

- **Successful:** BA, BT and (possibly) the health service internal market.
- **Jury out:** gas, electricity and water.
- **Unsuccessful:** railways, education.

The limitations of the last government's approach, coupled with the central importance of services and the persistence of problems within them, suggest that a government with social justice high on its agenda needs to follow a radical path: searching for new forms of intervention.

NON-PLC FORMS OF SERVICE DELIVERY IN DECLINE

Many autonomous, or semi-autonomous institutions in both the public and the private sectors have long been in decline. This is not just true of the public sector, where the nationalised industries of old have now almost entirely been replaced by plcs. So too in the private sector, many non-plc forms also seem to be in retreat, for example: the *de-mutualisation* of building societies and insurance organisations; the *demise of partnerships* (e.g. in accounting); the move away, by Lloyds of London, from being a group of *individual traders*; and the decline of *amateurism* within sport.

Within those parts of the public sector that were judged unsuitable for being fitted into a market-type model, the trend has been towards a loss of autonomy and greater central involvement. *Education* is a leading example, where the government has introduced a variety of initiatives (such as national curriculum, centralised inspectorates and league tables) which have increased central direction and reduced the historic freedoms of the individual professional. More generally, *quangos*, which by virtue of being appointed by a higher authority rather than elected, can also be seen as instruments of central direction.

None of the alternative forms (to plcs) is without its faults. But our view is that their decline should give cause for concern, given the deep seated difficulties with the ‘regulation of plcs’ model which is currently so predominant.

THE INHERENT LIMITATIONS OF REGULATION

Privatisation and commercialisation are motivated by a preference for devolved decision-making, the superiority of the private sector and market mechanisms. But, at least in the area of services, it is clear that private sector markets require regulation if their outcomes are not to be unacceptable.

The problem is that regulation (at least in the case of UK privatised industries) has been based on conflicting purposes, with the regulator as champion of the customers versus management whose overriding obligation is to the shareholders. But continuing dissatisfaction with the outcomes, from both government and public opinion, coupled with the inevitable tendency of regulators to act as political actors in their own right, pushes the regulator towards more detailed intervention. The distinction between regulator and management becomes less and less clear. There are echoes here of the struggle between the management of the nationalised industry and the civil servants or local government officers in the controlling department.

Our conclusion is that, while regulatory arrangements are always capable of improvement, any reforms are unlikely to do away with the tensions that are inherent to the combination of plc and central control. So, while regulation is a permanent feature, environments that are not built on these contradictory tendencies are well worth searching for.

3. A UNIFYING THEME FOR NEW FORMS OF GOVERNMENT ACTION

'REGULATION BY VALUES'

If new forms of government intervention are needed, how should the search for them be directed and indeed limited? One way of answering that is by reference to society and its relationship to government.

John Kay has used the notion of an economy 'regulated by values' to provide a sketch of a society in which government's role is occasional yet where the outcomes of myriad private decisions and actions are nevertheless usually socially acceptable. Its key features can be seen by way of contrast with three other alternatives, namely total deregulation, regulation by contract and regulation by rule:

- **Total deregulation** (the Russian model?). Anything goes. Redress is in private hands, relying on threats for effect. The strong (and those with money to buy them) rule.
- **Laws** (the American model?). Anything goes too. Redress is in private hands but enforcement is via civil law, rather than civil violence. Lawyers (and those with money to buy them) rule.
- **Rules** (the German model?). Nothing goes. Detailed rules and regulations prescribe what may and may not happen. Redress is in public hands, via administrative measures. Bureaucrats (and those with the means to influence them?) rule.
- **Values** (the John Kay model). Anything goes but imbued and guided by appropriate values, persons individual and collective regulate themselves. Nobody rules.

REGULATION OF SOCIETY BY SOCIETY

To our mind the key word in ‘regulation by values’ is ‘values’ rather than ‘regulation’. The defining characteristic is that individuals and organisations voluntarily restrict their choices to those which will result in outcomes that are satisfactory from a social point of view. It is a vision in which civil society - companies, associations and individuals, as well as public sector institutions such as schools and hospitals - ‘regulates itself in line with the public interest’.

Clearly, this will never be the sole answer and will never be fully attainable. Indeed, ‘regulation by values’ should be considered complementary to laws and rules rather than a mutually exclusive alternative. Nevertheless, if treated as an ideal to be worked towards, it suggests that ‘regulation’ of civil society by civil society can be much more powerful than direct regulation by government or its agents.

In abstract, the idea that civil society should regulate itself is quite familiar, since it is commonly invoked to lend support to the claims for superiority of the free market, which can, after all, be seen as a form of ‘social self-regulation’. By employing it here, in explicit opposition to the notion of the completely free market, it is being suggested that this liberal ideal can be detached from an automatic association with free markets and can instead take on a progressive connotation.

NEW FORMS OF ENTERPRISE

‘Regulation by values’ suggests a new model of enterprise where all the stakeholders (including employees, management and shareholders) are united around a clear purpose, which in our case relates to social outcome and purpose. Such unity is understood and believed throughout the enterprise, with a strong set of values guiding day-to-day decision-making and behaviour. It transcends defined boundaries and structures, and negates the need for micro-measures to manage the situation, as the relevant parties naturally work together to achieve the common goals.

Such notions are not new. Indeed, many from the public sector may point (perhaps with rose-tinted glasses) to a ‘public sector ethos’ which used to exist but which is now much weakened. Such ideas also have some academic support. For example, Canadian academic Henry Mintzberg has criticised the UK and other governments for introducing managerial change in the public sector without due thought to its different and complex ethos. He argues that privatisation and agency mechanisms (which are based on the assumption that activities can be separated and measured) can potentially yield efficiency gains but can also lead to a loss of higher level public objectives. He quotes the NHS as an example, where its division into a number of separately governed and managed businesses has not been adequately balanced with a continued unifying higher level purpose across the whole service.

Private enterprise itself provides many recent examples of ‘management by values’. In the Templeton debates, future Labour Ministers looked at examples of companies such as Rover, British Airways and Smith Kline Beecham that have undergone dramatic changes in behaviour and ways of working, where the leaders were not motivated simply by a drive for greater efficiency. Rather, their aim was to infuse the organisation with a new sense of vision, inspiring people towards a higher goal. These examples clearly illustrate the key role of leadership in such initiatives.

4. STRATEGIES FOR GOVERNMENT LEADERSHIP

The difficulties in an unregulated model arise when the values of key individuals and institutions are different from those that government believes are desirable of society at large but when no mechanisms exist for reconciling the two. We believe that there are three basic strategies for achieving such a reconciliation.

1. ***Strategy 1 - Strengthen incentives and deterrents.*** In this strategy, the government accepts the market as it is, and the current values of the key players in the market, but influences the environment within which these players make their decisions.

Putting a ‘regulation by values’ spin on this: by attaching private costs to certain forms of behaviour or attaching additional rewards for others, government can try and ensure that the decisions and behaviours of current institutions are influenced to produce outcomes which are closer to society’s values.

2. ***Strategy 2 - Stimulating institutions whose values are closer to those of the government.*** In this strategy, the government does not simply accept the current market and its players but seeks to change the environment to encourage new types of organisation to develop and thrive. Encouraging mutual organisations may be one example of such a strategy.

This strategy is perhaps be closer to the principle of ‘regulation by values’ - by fostering institutions whose values are closer to the social, government can try to promote a deeper change which would then lessen the need for incentives and deterrents.

3. ***Strategy 3 - Reviving a service ethos.*** In this strategy, the government accepts the market and its current players but aims to ‘win their hearts and minds’ to some of the government’s objectives.

This strategy emphasises the government’s role of working with organisations to achieve change. It requires a great sense of team working and collaboration, unrestricted by organisational boundaries.

The table below compares these three strategies in terms of their approach to the current market and its key players.

Targetted Organisations	Targetting Approach	
	<i>Acceptance of current values</i>	<i>Hearts and minds</i>
<i>Current players</i>	Strategy 1	Strategy 3
<i>Potential new players</i>	Strategy 2	Strategies 2 and 3

While the idea of creating incentives and deterrents is quite familiar, the other two strategies may be less so. One example of the second strategy is the last government's health reforms: the transfer of financial power into the hands of GP fundholders on the grounds that they are the best guardians of patients' interests. A more recent example of the third strategy might be the current government's campaign to articulate a series of welfare reform objectives.

5. TOOLS FOR PURSUING THE VARIOUS STRATEGIES

Using these three strategies to provide the basic framework for government leadership, we now turn to consider some specific tools that might serve these ends.

TOOLS FOR STRATEGY 1 - INCENTIVES AND DETERRENTS

Table 1 (at the end of the section) provides some example tools for progressing this strategy. These examples fall into three broad categories:

- ***Setting criteria for outcomes***, rather than focusing on the outcomes themselves. One appealing feature of this view is that criteria are quite close to values, which are what politicians know about. Another is that it leaves the initiative on how best to satisfy those criteria with the provider institutions (with regulators probably charged with deciding whether proposed solutions actually satisfy the criteria or not).
- ***Inclusivity conditions***. A different and probably more uncertain approach is to attach blocking conditions that deter too easy an abdication by providers, leaving those receiving the service high and dry. The idea is that by deterring providers from taking an easy option, they naturally search for new and different approaches that serve the interests of recipients better.
- ***Creating counter pressure***, by either requiring information to be provided about performance or perhaps by providing rights of redress. Some of the applications here will be familiar.

TOOLS FOR STRATEGY 2 - STIMULATING NEW INSTITUTIONS

Table 2 provides some specific examples and where again there are three types tool being suggested:

- ***Enabling new types of institution***. The idea here is to encourage a proliferation of different institutional forms, particularly those that are thought to have internal values that are closer to those the government believes should be promoted.
- ***Strengthening the position of preferred institutions***. The idea here is that government can strengthen the position of preferred institutions, either by granting them freedoms that they do not currently enjoy, or by encouraging mainstream service providers to seek them out as partners.

- ***Strengthening public sector institutions' capabilities.*** Perhaps the toughest one of all is to find ways of re-skilling and re-equipping public sector organisations for their role.

TOOLS FOR STRATEGY 3 - REVIVING A SERVICE ETHOS

Possible actions under this heading include:

- ***Creating and communicating the case for change and a vision of the higher level social outcome.*** Such communication would need to be persistent and in a variety of forms, finding as many ways as possible for the vision to be articulated.
- ***Enabling and facilitating joint strategy development.*** All the various stakeholders can be brought together, consulted or otherwise involved, with government actively leading/chairing the discussions.
- ***Creating and leading 'breakthrough' initiatives*** that clearly demonstrate a new and focused energy towards social outcomes. Such initiatives can involve private and public partners, might be stimulated by government money and resources, and require strong political leadership to transcend organisational/departmental boundaries.
- ***Promoting a service ethos,*** through education, positive recognition and practical examples. The citizen's charter represents one (albeit problematic) example of this approach, with research and publicity being two possible angles for the future.

TABLE 1 - EXAMPLE TOOLS FOR CREATING INCENTIVES AND DETERRENDS

Tool Type	Specific Tool	Example Application†
Outcome criteria	<i>Setting economic, environmental and social criteria for tariffs</i>	<i>Water charges after 2000.</i> † With the demise of rateable values as the basis for domestic water charging, government could leave water companies to devise replacements, but require that they meet certain specified economic, environmental and social justice criteria.
	<i>'Uniformity of service provision' criteria</i>	<i>For important, non-essential services, e.g banking, telecommunications.</i> Providers could be required to show that there are no concentrations of low service provision in their area (this being assumed to show something other than consumers freely choosing not to use the service).
Inclusivity conditions	<i>Statutory minimum period before customers are in breach of contract</i>	<i>Mortgage debt and re-possession.</i> † Lenders could be required to house a borrower for say 3 years from when arrears begins. By blocking off the easy route (eviction), the lender is forced to find new ways of coping with people who go into arrears.
	<i>Statutory shared responsibility for service provision</i>	<i>For essential services with many providers, e.g. education.</i> † While schools retain the right to expel (permanently exclude), they could be required to take in an equal number excluded from other schools. By raising the cost of exclusion, this encourages schools to co-operate in ensuring that excluded children remain within the system.
Counter pressure	<i>'Name and shame'</i>	<i>Mis-selling of private pensions.</i> A tool already employed by the government, this attempts to alter behaviour by exposing the 'shamed' institution to public criticism and hence a potential loss of public confidence and business.
	<i>League tables</i>	<i>School exam performance.</i> By publicising one or more measures of performance, schools may be provided with incentives to alter their priorities.
	<i>Public reporting requirements</i>	<i>Distribution of bank lending.</i> † Following the example of the US Community Reinvestment Act, banks could be required to report on the distribution of their lending, providing a source of leverage for disadvantaged communities seeking to attract funds into their area.

† indicates that the application has been developed (or is being considered) in the context of a particular New Policy Institute project.

TABLE 2 - EXAMPLE TOOLS FOR STIMULATING NEW INSTITUTIONS

Tool Type	Specific Tool	Example Application
Enabling new types of institution	<i>Legislating for new plc forms</i>	<i>John Kay's 'Customer Corporation'</i> . A form of company in which manager rewards are linked to customer interests rather than just the company's earnings. Seen as especially suitable for any form of monopoly utility, the conflicts usually faced by managers are lessened by aligning the interests of shareholders and customers.
	<i>Easing the creation of non-plc forms</i>	<i>Reforming the laws on charities, trusts, mutual associations etc.</i> Arguably, both law and practice make formation difficult but pay less attention to subsequent performance. This is the opposite to the position with limited companies. Reform could be based on easing formation plus tighter monitoring of adherence.
Strengthening preferred institutions' position	<i>Shifting economic and financial power towards preferred groups</i>	<i>Health service reforms.</i> Strengthening the position of GPs can be viewed as a means of ensuring that decisions are taken in the patient's interest. Presumes that GPs are better representatives of patients' interests than hospital managers and consultants.
	<i>Encouraging mainstream providers to seek partners</i>	<i>Membership organisations as customer intermediaries.</i> Housing associations, trade unions and credit unions can be intermediaries between financial institutions and their own members. Introducing conditions and/or incentives on mainstream providers could actively encourage them to seek membership organisations as partners.
	<i>Lifting restrictions on non-plc forms</i>	<i>Greater powers for building societies.</i> One of the arguments for a building society converting into a bank was that banks had greater freedom. Removing restrictions on building societies (as recent and indeed, not-so-recent, legislation has done) could be appropriate.
Strengthening the capability of public sector institutions	<i>Matching powers to responsibilities</i>	<i>Constituting Regional Development Agencies in a way that ensures their effectiveness.</i> Although the government sets great store by them, it is not clear that RDAs have the remit and powers to deliver what is required.
	<i>Removing conflicts in institutional objectives</i>	<i>Removing conflicting objectives within the Private Finance Initiative.</i> PFI decisions are arguably distorted by government capital spending limits, and year end spending decisions are arguably distorted by revenue cash limits. Moving towards a more standard accounting process for the public sector could potentially help remove such distortions.

TABLE 3 - EXAMPLE TOOLS FOR REVIVING A SERVICE ETHOS

The whole area of reviving a service ethos is an area that has not been much explored to date and thus examples are somewhat thin on the ground.

Tool Type	Example Application
Communicating case for change and vision	<p><i>'Welfare to work' and 'welfare reform' campaigns.</i> These are two examples where government has clearly recognised the need to argue the case for change prior to the development of specific policy proposals. Presenting a clear vision of the future is arguably an even more difficult task.</p>
	<p><i>Companies and helping to alleviate poverty.</i> Many people working for utility companies would agree that changes in tariff structures over the last decade or so have often worked against the interests of the poor but most would also argue that this is not a problem for them, as commercial organisations. When these companies were publicly owned, the situation was arguably easier. The government could set out its views on this subject and seek companies' cooperation in making progress in this challenging area.</p>
Joint strategy development	<p><i>Task Forces.</i> Task forces in health, education and other areas can be a powerful vehicle in bringing representatives of all the relevant stakeholder groups together in the context of a tangible set of problems to be resolved.</p>
	<p><i>Collaborative discussions with service providers.</i> The day-to-day dealings between companies and regulators often appear to have a somewhat adversarial nature. But there is arguably much more consensus between the companies and government on particular issues, and such consensus might be maximised from more in-depth discussions.</p>
'Breakthrough' initiatives	<p><i>One stop information centres.</i> Although experimented with by a number of local authorities in the past, one stop information centres have never really taken off. New and cheaper technologies are increasingly making such possibilities more attractive and government could decide to take a clear lead in this area. One area of recent discussion has been one stop centres to support single parents looking for childcare and work.</p>
Promotion of service ethos	<p><i>Citizen's Charter.</i> Although they might not have had the impact that was hoped for, the various charters were a clear attempt to promote a service ethos.</p>
	<p><i>Departmental 'get togethers'.</i> At least by rumour, the meetings held by ministers with their departmental staff immediately after the election had a major impact on morale and motivation.</p>
	<p><i>Research and publicity.</i> Work by the Audit Commission and others has clearly demonstrated that research and publicity combined can have a major impact on service ethos, with future initiatives perhaps focusing more on quality as well as value for money.</p>

6. CONCLUSION

Whilst not a definitive analysis, this paper demonstrates the need to search for new forms of government intervention and the rich range of possibilities potentially available to it. This is clearly a subject worthy of debate, and that debate must itself be wide ranging and discursive if it is to yield valuable results. The New Policy Institute will be arranging a series of seminars and conferences to take the discussion forward.