

# Shrinking the state 2.0: commentary on Ken Warren's 'A new model of collaboration' and related IGPS working paper

This commentary is a response to two papers by Ken Warren: his article in this issue of *Policy Quarterly* (Warren, 2022) and the longer, more detailed IGPS working paper on which it is based (Warren, 2021).

Stripped of the distracting clutter of business school jargon, both papers read to me as a rearguard action in defence of the rapidly unravelling public sector 'reforms' that were promoted and driven through in the late 1980s, starting with the New Zealand Treasury's 1987 briefing document *Government Management*, and embodied in the State Sector Act 1988.

The neo-liberal project has always had 'shrinking the state' as a central goal, and Warren's two papers represent another step down that path. He recommends adding two new elements to the post-1987 public sector restructuring (which I characterise as 'shrinking the state 1.0'). First, an entire realm of 'collective activity' is to be formally set up, in which greater agency and autonomy is granted to non-government providers of public services, overseen by a new cohort of 'collective investment managers' located within the central state apparatus but somehow freed of its constraints. Second, ministers are to be removed even further from control of and accountability for publicly funded provision of goods and services, on the basis of the unexamined claim that they 'cannot access the necessary information'

to understand 'complex, variegated and dynamic solutions' – an understanding which, by some mysterious alchemy, is to be achieved instead by the new 'collective investment managers', and by removing ministerial responsibility for 'outputs or outcomes' of policy, with ministerial accountability reduced to certification (on the basis of officials' advice) that the 'collective investments have the necessary respect or mana to achieve positive outcomes' (Warren, 2022, p.27).

No fully articulated basis for Warren's vision of doubling down on the existing 'funder-provider split' is to be found in either of the two papers reviewed here. His Table 1 just sets up a false dichotomy between the central state apparatus (characterised as involving 'hierarchical specialisation' and lacking 'commitment to

shared goals and the ability to achieve them', 'accountability to citizens', 'effectiveness', 'value-add through collaboration' or 'fast feedback loops from citizens') and a sphere of non-governmental 'outcome-based collaboration' that allegedly possesses all those virtues. Warren then seeks to upgrade and empower the 'collective' while leaving the central state stuck in Table 1 with bureaucracy, hierarchy, silos, and the unenviable task of balancing 'equity and efficiency'.

Any notion of a public sector free of silos is dismissed out of hand at the outset: 'bureaucracy necessarily has a hierarchical structure and therefore consists of many silos' (ibid., p.23). (Looking back to *Government Management*, it is noticeable that among the many criticisms offered in 1987 of the old New Zealand public sector, silos actually did not figure.) And there is no suggestion of reconsidering the radically disruptive make-or-buy thinking that drove the outsourcing extremism of the 1990s; on the contrary, 'the choice is no longer just between buy or make. It is between buy, make and enable' (ibid., p.25).

To put Warren's papers into perspective, it is worth recalling the key elements in the original public sector reforms post-1987. First, privatisation and corporatisation

removed whole swathes of the public estate from delivery of non-commercial services to the populace. Second, elimination of key agencies, such as the DSIR, the Forest Service and the Ministry of Works and Development, removed the option of the government ‘making’ rather than ‘buying’ key services. Linked to both of those, but most radical and fundamental, was the ‘funder–provider split’, which delegated the actual delivery of various policy outcomes to non-governmental providers operating under contract to the central agencies of government, while reducing ministries to mere policy shops. The state sector’s role was accordingly transformed from exercising actual ownership of particular policy areas and accountability for delivery of tangible results, to merely providing policy advice and signing contracts under which outside providers of services were funded. Warren speaks of the difficulty of ‘break[ing] down the walls ... between policy and operations entities’ (ibid., p.23), but at no point explains how those walls came to be constructed. He simply takes as given the post-1987 public sector architecture.

Policy design and delivery is inherently a complex and difficult process, which tends to benefit from being in the hands of dedicated teams with experience, professional skills, and direct connection with the ordinary citizens who are supposed to be the ultimate beneficiaries of policy. In *Government Management*, and in the implementation of the reforms, the reform architects put forward deceptively simple-looking solutions for those complex problems, based on a narrow misreading of the then-popular school of ‘public choice’ economics in the United States (see Bertram, 2021, pp.36–8). The importance of professional skills and institutional knowledge was downgraded, on the basis of the public choice claim that the holders of these attributes were driven by personal self-aggrandisement rather than vocational motivations and should therefore be excluded from access to the policy making process to prevent them from ‘capturing’ it. Once relegated to the outer circle of ‘providers’ and funded under arm’s-length contracts, the thinking went, they could be safely left to go about their business while the inner circle of officials could provide disinterested policy advice aligned with the goals of the

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government of the day. (In Warren’s rather confusing language the inner circle turn up as ‘specialists’ and the outer circle of actual professional specialists as ‘the collective.’)

#### **The consequence of separating funding and provision**

Three consequences of that structural separation of policymaking ‘funders’ from professionally qualified ‘providers’ now haunt the corridors of power in this country. The first was the loss of professional knowledge and ability in the now-insulated policy departments of state, which these days are run and dominated by managers rather than specialists (see, e.g., Gill, 2021; Gregory, 2003). Scientists are scarce in the Ministry for the Environment, engineers in the Ministry of Business, Innovation and Employment, qualified medical practitioners in the Ministry of Health, social work specialists in the top echelons of Oranga Tamariki – the list could go on. Stripped of deep professional knowledge and crippled by constant churning of senior management on short-term contracts, the policy departments have in turn lost the capability to provide

the fully informed advice and deep wisdom on which elected politicians ought to be able to rely in determining policy. Filling the knowledge gap by increasing resort to outside consultants merely doubles down on the original mistake of separating departments from delivery.

The second consequence was a collapse of genuine accountability and its replacement by bean-counting and managerialist slogans and jargon. To go back and read the annual reports of New Zealand government departments prior to 1984 is to enter a world of informative narrative, working through the events and decisions of the preceding year, evaluating outcomes in the qualitative terms that were meaningful to ordinary citizens while illuminating the financial and statistical records at the end of the reports. Since the late 1980s the reporting process has been reduced to an accountancy-focused recording of dollar amounts, accompanied by information-free corporate spin about key performance indicators. In turn that means that citizens and MPs seeking to hold ministers to account have far less to go on than the shareholders of most publicly listed companies, who have in their hands annual reports that typically begin with substantial and informative narrative sections.

The third consequence was the destruction of much of the team-building approach of the old public service. A century of experience and pragmatic experimentation had, by the 1980s, developed a set of public service departments with genuine roots in on-the-ground reality, and with clear ownership of particular areas of policy concern. Treasury’s characterisation of several of these long-established teams as self-aggrandising empires that would best be eliminated led to the loss of a huge mass of human and social capital built up over the preceding century. Without the Ministry of Works, major infrastructure projects have become case studies in contractual incompleteness, opportunism and waste. Without the DSIR, science has languished under the dead hand of private corporate influence and so-called ‘contestable’ funding. Without the integrated New Zealand Forest Service the conservation estate has been progressively starved of funding, while the unrestricted

log export trade has sucked life out of domestic wood-processing industries.<sup>1</sup> In education, health and social services the new ethos and corporate structures have hollowed out rather than strengthened the quality of decision making and service delivery. Inescapably the police and the military continue to operate on the team model; it was no surprise to see the latter called in last year to bring some order and efficiency into the operation (not the design) of the MIQ exercise.

#### Warren's proposals

What, then, does Ken Warren propose? His central concern appears to be that the creativity of non-governmental providers of various services that are ultimately funded by taxpayers is being negated by the bureaucratic practice of the central policy agencies with which they are obliged to contract, while those central agencies operate as self-centred 'silos' that fail to collaborate effectively with one another. Warren's proposed solution is to appoint 'collective investment managers' within the central government system who can cut through the red tape and direct funding to where it can be best utilised, providing 'assurance that a return-on-investment test is made of each proposal' (Warren, 2021, p.28). The qualities an 'investment manager' will have to possess look rather like Plato's ideal of the philosopher king – full knowledge of the policy area, ability to spot and reward talented provision, ability to accurately identify failing agencies and the power to cut them off summarily from their funding. In short, the ideal-type 'investment manager' in Warren's account looks suspiciously close to Treasury's self-portrayal back in 1987 as somehow better informed and wiser than any professional, vocationally driven provider actually engaged in service delivery.

Missing from Warren's analysis is any proper account of how cross-departmental coordination used to be achieved prior to 1987, apart from one brief reference to 'inter-departmental task forces' (ibid., 2021, p.11) in a paragraph that simply slumps into scepticism about overcoming silos. In the old system, officials' committees did convene to overcome the limited scope of individual departments' reach, and those committees often functioned quite

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effectively because the senior public servants attending the meetings were long-serving and experienced professionals – not today's generic managers – with genuine knowledge of their department's mission and with the authority to enter into multi-agency arrangements.

At the same time, Warren's portrayal of the resource allocation process is revealing in the language it uses. Professional providers of medical, mental health, social work, engineering, scientific and educational services to the public are not treated as pursuers of their chosen vocations in life; in Warren they are 'social entrepreneurs' clamouring for funding at the central policy agencies' pay-out windows (ibid., pp.26, 32, 34). Yet at the same time as they are placed in the position of competing for the favour and funding of the investment manager, they are supposed to cultivate simultaneously the process of 'collaboration ... at the front line' (2021, p.1; 2022, Table 1).<sup>2</sup> The relationships of a professional service provider with the individuals and groups they serve among the wider citizenry are a 'critical resource' – an asset on which the social entrepreneur seeks a return as a competitive supplier within a 'social entrepreneurs' supply curve' in a 'market' where the demand side is to be occupied by philanthropists and by the government (Warren, 2021, pp.14, 32–3), which dispenses public funding to those considered to possess 'mana' (a term from te reo Māori appropriated here to mean, apparently, some sort of peer-group recognition) (ibid., 2021 pp.iii, 2, 22–4; 2022 p.25).

The immovable core of Warren's position is the funder–provider split. His entire proposal boils down to tweaking the arm's-length relationship between those at the centre who have money from the Budget to dispense (the investment managers), and the vocational 'social entrepreneurs' to whom the task of service delivery is to be outsourced, along with the accountability for results from which the central agencies of the state will have abdicated.

It is important to be clear that what Warren means by the 'collective' is far removed from the self-sustaining locally based entities modelled by Ostrom (1990), on whose authority he relies. Ostrom's collectives are organised like the 'clubs' of Buchanan (1965) to restrict outsiders' access to shared resources while regulating insiders' access; this is completely different from non-governmental ventures formed to secure public funding for social outreach activities.

Notably, Warren treats accountability as a horizontal task to be conducted within his 'collective', leading to the attribution of 'mana', while the investment manager floats high above with job security while dispensing the fate of those below (Warren, 2021, pp.iii–iv, 23; 2022, Table 1). (Readers familiar with Swift's (1726, part III) account of the flying island of Laputa in *Gulliver's Travels* will know that this is not a new phenomenon.)

Here we find, I would argue, the essential contradiction in Warren's case. If the philosopher-king-manager ideal were attainable within the actually existing New Zealand public service, it ought already to have emerged, which it palpably has not. Warren argues (not uncontroversially) that 'a hierarchical public sector cannot realistically identify the best paths to improved outcomes' because 'there are different views about the nature of the problems, their cause and solutions. Pragmatic responses are required' (Warren, 2021, p.ii). How handing over the job to an individual manager within the state system would somehow break this impasse is unclear. Though there are no doubt many individuals both within and outside the existing public sector workforce who would fancy themselves in the new role, it is not obvious how to identify and appoint them.



Supposing the hypothesised all-knowing, all-seeing, wise investment managers exist and will be correctly selected in the recruitment process (conducted by whom exactly – who guards the guardians?), why should they have to operate through the complex and error-prone mechanism of arm’s-length contracting, rather than simply building collaborative in-house teams to deliver the goods and services? The problem Warren identifies – the proven inability of the existing central agency bureaucracy, trapped in its post-1987 funder–provider-split cage, to enter into complete, optimal contracts with outside providers – does not go away by appointing another bureaucrat subject to the same structural constraints.

Nor does his strongly drawn contrast between ‘specialist’ and ‘collective’ operating models (2021, pp.13–15) necessarily point to maintaining a funder–provider split for the collective. The set of alleged contrasts in Warren’s Table 1, besides containing several tendentious propositions, says nothing about this issue. Nor does the strange scatter plot (2021, Fig. 1 p.17; 2022, Fig. 2 p.25), showing an apparently positive relationship between ‘importance of goal congruence’ and ‘difficulty of measurement’, indicate that team tactics need be pursued through a separation of funder/‘principal’ from provider/‘agent’.<sup>3</sup> Nor does the extensive section (2021, pp.18–22) on how good professional and managerial practice should look in a ‘collective’ team-building setting resolve the issue; on the contrary, it throws a spanner in the works by concluding that ‘the responsibility of the public sector hierarchy is not to steer collective entities, but to create the environment in which the smart practices necessary for self-governing collaboration can flourish’ (2021, p.22; 2022, p.25) – a proposition that seems diametrically opposed to the role of the proposed ‘investment manager’ in dictating who survives and who exits (‘disinvesting well’ is one of the manager’s roles (Warren, 2021, p.28)). Basically, unless the investment manager is embedded within ‘the collective’, then that collective remains subject to the top-down dictation which supposedly was the initial problem definition. But if the manager is embedded, then ‘the collective’

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must be inside, not outside, the public sector itself, to maintain lines of accountability for securing and justifying fiscal outlays.

These contradictions become all too obvious in Warren’s discussion of ‘critical success factors’ in his working paper (2021, section 3.8, pp.22–5). Here we find ‘financial incentives to collaborators’ being ‘manipulated’ by the funder (p.22); ‘creative destruction’ of ‘poor collaborators’ (p.23); insistence that ‘principal–agent ... accountability between the public sector investor and the collective should encourage ... horizontal accountabilities’ (ibid., p.23); the requirement that at all times the ‘collective’ agent must adhere to a ‘vision’ that is ‘in alignment with Government objectives expressed in the collective investment strategy’ (p.24), even though ‘funding and accountability should not be a contract for services’ (p.23). While it may not be a ‘contract’ in Warren’s proposal, his ‘strategy’ certainly seems intended to be enforced like one – except that accountability of the ‘investment managers’ at the top is even more diffuse and intangible than under the current imperfect contracting regime.

The real problem, it seems to me, is not the failings of officials within the existing ‘principal’ funding agencies, nor their use of contracts rather than ‘strategies’, and it is not solved by replacing the existing ‘principals’ with a new set of individuals operating within the same, ultimately top-down, system of arm’s-length principal–agent interaction. The problem is inherent in the contracting-out model and the

funder–provider split, and the toxic tensions between ‘principals’ and ‘agents’ that flow from that model.

It is therefore extraordinary that Warren chooses Whānau Ora as his key example of the supposed difficulty of ‘trying ... to extend a specialist model to a collective model’ (Warren, 2022, p.25). Whānau Ora was crippled from the outset by being starved of funds by the central ‘provider’ agencies (basically Treasury) and constrained by the requirement that all of that limited funding has to pass through the contracting-out interface to external providers. Simply establishing Warren’s ‘separate legitimised centre of gravity in the system’ (op cit.) does not overcome the problem.

It is a pity that Warren has not delved more deeply into the economic literature around these issues. There are two sets of classic economic papers that could have provided him with a different starting point. One is Oliver Hart’s work on contractual incompleteness (Hart, 2017; Hart and Moore, 1999; Hart, Shliefer and Vishny, 1997). The other is Ronald Coase’s work on the theory of the firm and the make-or-buy decision (Coase, 1937).

Coase analysed the best balance for a firm between ‘buying’ its inputs from outside providers and ‘making’ those inputs itself. The New Zealand government before 1987 was built mostly around a ‘make’ model, with vertical integration from the policymaking minister down to the front-office/coalface staff. It benefited from the virtues of vertical integration and occasionally suffered from the disadvantage of failing to spot opportunities to ‘buy’ on terms that might have been advantageous to the public interest. The ‘reformed’ post-1987 regime for public services has been an extremist resort to the ‘buy’ decision, throwing overboard in the process all the advantages of vertical integration that Coase identified and eliminating much of government’s capacity to ‘make’.

One of the key potential problems associated with ‘buying’ rather than ‘making’ has always lain in the difficulty of writing purchase contracts that are complete and enforceable in a world where opportunism and uncertainty lie around every corner. Public officials are in an especially weak position when using

commercial contracts to purchase services in the open market, for reasons described in detail by Hart in his work. The problems of incompleteness and post-contractual opportunism (think Transmission Gully) led Hart to emphasise the potentially great value for the government of holding 'residual control rights' to do the job itself. Warren does indeed mention this phrase (Warren, 2021, p.35, though without citing Hart), but he nowhere reflects on its essential meaning, that government should always have at its disposal the genuine possibility of doing its own delivery – precisely the essential institutional asset which the late-1980s reforms stripped away.

Where, then, does this leave us? There is clear dissatisfaction at ministerial level with the failings of the existing model, and a process of re-centralisation of

governmental functions in housing, health, education, social services and other areas is getting underway. But this is happening ad hoc, without a well-developed overarching blueprint for the new structure that is to come. That Warren's proposals come from within the New Zealand Treasury seems to me a cause for concern rather than celebration. His basic thrust of moving ministers and the state further away from connection with the general public, rather than improving the quality of information and advice reaching ministers while opening a more responsive and creative interface between government and the general public, seems a retrograde rather than progressive step. Treasury has 'form' in this area, and a proper self-evaluation of, and accountability for, the mistakes of 1987–90 has yet to make it to

the public arena. Warren's claim that his self-described 'direct attempt to tackle the funding and accountability problem that has bedevilled efforts at collaboration to date' (Warren, 2022, p.27) – by devolving funding decisions into the hands of 'investment managers' – is 'respectful' of the constitutional position of ministers rings hollow. *Caveat emptor*.

- 1 In passing I should note that back in the 1970s and early 1980s I was an active critic of two of those teams – the Forest Service (over native forests) and the Ministry of Works (over Think Big and development planning). But that criticism was intended to nudge them to change their decisions and resource allocation, never get them abolished.
- 2 Exactly what the boundaries of Warren's 'collective' are supposed to be is unclear. At times he seems to mean the individual 'social entrepreneur' and his/her particular organisation, operating parallel to and in competition with others. At other times 'the collective' seems to be shorthand for the entire body of non-governmental providers.
- 3 In passing it should be noted that characterisation of the central public service bureaucracy as a 'principal' rather than an 'agent' seems to turn the usual constitutional conventions on their head.

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