EVALUATING PUBLIC SECTOR REFORM IN NEW ZEALAND: HAVE THE BENEFITS BEEN OVERSOLD?

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In the mid-1980s and 1990s, New Zealand radically reformed its public sector. Changes included corporatising and privatising state owned enterprises; introducing performance related individual contracts for senior staff; increasing departmental management autonomy; changing financial management and reporting requirements, including moving from input-based to output-based reporting; a move to strategic planning for the government; and departmental decoupling, including promoting policy-operations and funder-provider splits. The reforms drew heavily on public choice theory, new institutional economics and new public management. The New Zealand reforms have been promoted by some, such as the OECD and the Auditor General of Canada, as exemplars of public sector reform. This article argues that while there have been efficiency gains from these changes, these have sometimes been oversold. The benefits have often been off-set by significant costs.

Introduction

New Zealand has a Westminster-type political system with ministerial responsibility and a single house of parliament. It has a relatively politically neutral public service with appointment on merit (rather than patronage) and is largely free from corruption. Before 1984 the public service's statutory base was provided by the Public Finance Act of 1977, the State Services Act of 1962, the State Services Conditions of Employment Act of 1977 and the Health Service Personnel Act of 1983. Departmental chief executives were appointed on permanent tenure and a central body, the State Service Commission, was
responsible for employing public servants across the public sector. Departments were multi-functional and often relatively large, providing a range of policy advice, regulation, implementation and administration of legislation and the provision of services.\textsuperscript{1} The New Zealand state had traditionally played a considerable role in the economy including the ownership of infrastructure and trading enterprises. These government owned businesses accounted for 12 percent of GDP and 20 percent of investment in 1984.\textsuperscript{2}

After their election in July 1984 the Labour Government introduced a series of wide sweeping reforms to the public sector. Changes made since 1984 include the corporatizing and privatizing of state owned enterprises; the introduction of performance related individual contracts for senior staff; increasing departmental management autonomy; changing financial management and reporting requirements, including moving from input-based to output based reporting; moving to strategic planning for the government; and departmental decoupling, including promoting policy-operations and funder-provider splits. The reforms were heavily derivative of public choice theory, new institutional economics and new public management.\textsuperscript{3} While fiscal pressure and the general desire to make the New Zealand economy more competitive were driving forces in the quest to make the public sector more efficient, there was some suspicion of the public service by the incoming government and some desire to make them more accountable to the wishes of ministers. The Treasury, by far the most powerful department in the public service, was important in designing and advising on the changes that should be carried out.\textsuperscript{4}

This article describes the details of the changes themselves before examining evidence of increased efficiency in the public sector. It argues that benefits that have arisen from the New Zealand model have been oversold and have mostly arisen from increasing managerial autonomy and introducing new management processes, rather than the introduction of contractual arrangements to the public sector. Costs of the changes include an increase in reporting of performance measures of sometimes doubtful usefulness, high transition costs of the changes, and erosion of some accountability mechanisms in the wake of disaggregation of departmental structures.
The Main Changes

Departmental and Financial Management

After 1984, the Labour government introduced a wide range of management and financial reporting changes into the public sector, the two most important acts in this case being the State Sector Act 1988 and the Public Finance Act 1989. While largely Treasury driven, this legislation received strong support from the cabinet.\(^5\)

The State Sector Act 1988 redefined the role of the departmental chief executives. Rather than being appointed as permanent heads, they became chief executives appointed on three to five year contracts, with the possibility of renewal.\(^6\) Appointments are made by the State Service Commission, but recommendations must be approved by the Governor General in Council. A performance agreement is negotiated with the chief executive by the State Services Commission on behalf of the responsible minister and the remuneration of chief executives is to some extent contingent on performance as monitored by the State Services Commission acting for the minister. The performance agreement includes key result areas (see below), general requirements for free and frank advice, good management and employer requirements, sometimes specific personal requirements made of the chief executive by the responsible minister, as well as other ownership requirements. The performance agreement is also cross-referenced with the department purchase agreement (see below).\(^7\) Chief executives can be removed for "just cause or excuse" by the State Service Commission with the agreement of the Governor General in Council.

The State Sector Act gave chief executives the responsibility for appointing and paying their staff, a responsibility that was previously held by the State Services Commission. The Act also created a senior executive service in the public sector who were to be employed on individual contracts, with the (largely unsuccessful) aim of developing a collegial management class.\(^8\)

The passing of the Employment Contracts Act in 1991 introduced individual contracts of employment between employer and employee, moving away from the active state involvement and sponsorship of
collective negotiation that had persisted since the late nineteenth century. This has allowed the negotiation of individual contracts with staff below senior executive service level. As at 31 December 1996, 28.2 per cent of staff were on individual contracts up from 16.5 per cent two years previously. The majority of staff are employed on open ended contracts (either individual or collective) with 7.7 per cent employed on fixed terms. The public service is still highly unionized, compared to the private sector, and the Public Service Association acts as the bargaining agent for a large proportion of public servants.

The Public Finance Act 1989 put in place arrangements to monitor the performance of departments and introduced important changes to financial management, including clarifying the responsibility of chief executives for the financial management of their departments. A key feature of the Public Finance Act was performance measurement being moved from input controls to output controls, outputs being the goods and services (including policy advice) produced by the department. The minister becomes the purchaser of agreed outputs from the department, and chief executives are held accountable for their production in (since 1993) purchase agreements signed by the chief executive and the minister. These outputs are defined and specified in the annual estimates and purchase agreements, which also monitor their production. Purchase agreements can be renegotiated without having to return to parliament if appropriations do not change. Outcomes were not seen as easily attributable to chief executives and therefore not conducive to measurement. The focus on production of outputs also meant that ministers became better able (in theory) to purchase them from other (including non-departmental and non-government) sources, such as in the case of policy advice or health services provided by voluntary groups. This concentration on output purchasing has encouraged some ministers to employ staff to advise on and negotiate purchase agreements. Departments may also advise ministers on output purchasing from Crown entities or other non-departmental suppliers.

The Public Finance Act also introduced accrual accounting into the public sector. Cash accounting, whereby payments received and made are recorded for the year, was supplemented by a system
whereby the resources used in the production of goods or services were matched with the revenue or services produced in the same period. This allows the cost of the production of outputs to be better calculated allowing for better information for purchasing and ownership decisions.\(^\text{13}\) The Act also stipulated that financial statements be prepared in accordance with generally accepted accounting practise\(^\text{14}\) and introduced a capital charge for departments, reflecting the opportunity costs of capital.

The National government, elected in 1990, passed the Fiscal Responsibility Act in 1994. This reflected the advice of the Treasury and the wish of former finance minister Ruth Richardson to improve the transparency of budget decision making. The Act, as its name suggests, requires the government to be ‘fiscally responsible’. This involves formulating and reporting its fiscal policy objectives to parliament. Responsible fiscal management is defined as the following:

- Debt should be reduced to prudent levels;
- Operating expenses should not exceed operating revenues over a reasonable period (i.e. budget deficits should not be maintained);
- Crown net worth should be maintained at sufficient levels to counter adverse events;
- The fiscal risks facing the government should be managed prudently; and
- Fiscal policies should be consistent with predictable stable tax rates.

The government must report to parliament how it is to comply with these fiscal principles and any departure from them must be justified and an explanation given of when they will be complied with in the future. The Act also requires disclosure of the fiscal consequences of economic policy decisions. This includes publishing three year forecasts every half year and four to six weeks prior to a general election. These forecasts include the usual financial state-
ments, as well as a statement of fiscal risks and contingent liabilities which describes and (if possible) quantifies the fiscal risks associated with the forecasts. The Minister of Finance and the Secretary to the Treasury sign statements of responsibility declaring that all policy decisions have been included in accordance with the Act, and that the Treasury has used its best professional judgement in preparing the fiscal impacts of the policy decisions.

After the 1993 election, the National government moved to introduce a new system of strategic management. This involved developing key result areas (KRAs) which outlined yearly objectives for departments and held chief executives accountable for their achievement. KRAs are developed to assist each department to deliver policies and services that will aid the government in meeting its strategic result areas (SRAs). SRAs outline the long term policy visions of the government. The development of KRAs and SRAs reflected the concerns of some in the government and the bureaucracy regarding the lack of policy coordination between government departments and the insufficient attention being given to the collective interest of government. Policy goals of government were seen as not clearly articulated and some departments were dissatisfied with having their roles reduced to producing outputs with the relative lack of attention to outcomes that this entailed. There was also a wish to operationalize the broad long-term policy goals set by the National government in its document *Path to 2010*, while the State Services Commission wished to improve the performance monitoring of chief executives.

SRAs were developed in consultation with departmental chief executives and senior ministers. They are of varying specificity and fall into one of nine broad categories: maintaining and accelerating economic growth; enterprise and innovation; external linkages; education and training; community security; social assistance; health and disability services; treaty claims settlement; and protecting and enhancing the environment. KRAs focus on critical aspects of the department's business and, while they are part of an annual contract, KRAs that support SRAs are expected to have a three year focus. KRAs are confirmed (or revised) each year by officials meeting with ministers to see whether they are internally consistent and are assisting in the achievement of the SRAs. KRAs form part of the performance agreement of the chief executive.
In June 1997, a "standards letter" for chief executives was announced by the State Services Commission. This was developed in response to concerns that responsibility and accountability issues in regard to chief executives needed further clarification, and to recommendations from the Schick Report that accountability should encompass responsibility based not only on more precise specification of results, but also taking into account values, judgement and leadership. These letters were sent out to existing chief executives and are given to new ones. They set out standards of personal behaviour which the government expects from chief executives, the demands that the new position entails, as well as outlining the broad goals of the government. Standards include: the service chief executives must give to the minister; representational duties; leadership of the department; professional and personal ethics; responsibility and accountability; statutory independence; collective interest; and collegial relationships with other chief executives.¹⁹ According to the State Services Commissioner, these sometimes intangible behaviours are not among the details which are usually set down in employment contracts and statutes. But they are critical to the proper functioning of the Public service and the Government. Finally, these documents are intended to reassure the public of the values which the Public Service chief executives hold.²⁰

**Institutional Change**

Alongside reform of the management of the core public sector, a host of institutional changes have been introduced into the public service. These have included the corporatisation and privatisation of state assets and the disaggregation of departmental structures, including the introduction of policy-operations and funder-provider splits. The Labour government introduced full cost pricing for government goods and services by 1985.

Treasury had argued in its 1984 post election briefing papers *Economic Management* and in subsequent writings that government departments should attempt to replicate the alleged superior efficiency of private firms and the market by reorganising the way they deliv-
ered their goods and services. This process came to be known as corporatisation. Corporatisation was first announced in the *Economic Statement* of December 1985 and formalized in the State Owned Enterprises Act 1986. Government owned enterprises that traded in goods and services were moved from traditional departmental management structures to ones that attempted to make them behave more like commercial enterprises. These are known as state owned enterprises (SOEs).

Corporatisation quickly evolved into privatisation, with the initial drive again coming from the Treasury. The perceived fiscal benefit of the sales was an important factor in encouraging the sales; however, for some ministers and a number of officials efficiency arguments were more important. The first privatisation was the petrochemical company, Petrocorp, in 1987. This was followed by a wave of asset sales that were continued by the National government after 1990 (see Table 1).

Further changes have included the reorganisation of departments, including the separation of funder and provider services and of policy and operations. Examples of this include:

- The division of the multi-function Department of Health into the Ministry of Health which provides policy advice and regulatory functions; a health authority funded by the department; and hospitals which (along with private providers) sell health services to the health authority.

- The dissaggregation of the Department of Scientific and Industrial Research specialist into crown research institutes which compete for funding from the government owned Foundation for Research, Science and Technology, for contract research from departments and for private funding.

- The division of departments into separate policy divisions and operational divisions under one chief executive, such as in the Department of Social Welfare and the Department of Labour.

- The splitting of multi-function departments into policy ministries
### Table 1

**Corporatisation and Sale of State Assets in New Zealand**

<table>
<thead>
<tr>
<th>Year</th>
<th>Events</th>
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<tbody>
<tr>
<td>1987</td>
<td>• Government announces it will sell shares in the Bank of New Zealand and Petrocorp. &lt;br&gt;• Budget (18 June) announces the Government will sell all its shares in New Zealand Steel, and shares in the Development Finance Corporation, Petrocorp and Air New Zealand. The budget also announces the Government Property Services Corporation and Forestry Corporation will issue State enterprise equity bonds (a form of non-voting public shareholding) equal to 25% of total paid-up capital, while other SOEs will be authorised to do the same. &lt;br&gt;• Government Economic Statement of 17 December announces a programme of ongoing asset sales with the intention of reducing public debt by one third by 1992, with the benefits of sales assessed on a case-by-case basis.</td>
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<td>1988</td>
<td>• Sale of Petrocorp with 15% to the public, 70% to Fletcher Challenge, and 15% to Brierly Investments &lt;br&gt;• Health Computing Service sold to Paxus Information Services &lt;br&gt;• DFC sold to National Provident and Salomme Brothers. &lt;br&gt;• Bank of New Zealand 26% sold to Fay Ritchwhite, 16% floated (58% government share sold to National Australia Bank in 1992.)</td>
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<td>1989</td>
<td>• Postbank sold to ANZ Banking Group &lt;br&gt;• Shipping Corporation sold to ACT (NZ) Ltd &lt;br&gt;• Air New Zealand sold to consortium of New Zealand and foreign companies. &lt;br&gt;• Landcorp Financial Instruments sold to Mortgageors &lt;br&gt;• Rural Bank sold to Magnetons Holdings. &lt;br&gt;• Communicate NZ sold to DAC Group Ltd</td>
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<tr>
<td>1990</td>
<td>• Government Printing Office sold to Rank Group and others (1989-91). &lt;br&gt;• National Film Unit sold to TVNZ</td>
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<td>1991</td>
<td>• State Insurance Office sold to Norwich Union &lt;br&gt;• NZ Telecom sold to American and New Zealand consortium, with 30.8% now floated &lt;br&gt;• Tourist Hotel Corp sold to Southern Pacific Hotel Corp (NZ) Ltd. &lt;br&gt;• NZ Liquid Fuel Corporation, Synfuels Stocks and Current Assets, and Maui Gas sold to Fletcher Challenge and others. &lt;br&gt;• Forestry Cutting Rights sold to a variety of companies (1990-1992). &lt;br&gt;• Export Guarantee Ltd sold to State Insurance Office (an ex-SOE).</td>
</tr>
<tr>
<td>1992</td>
<td>• NZ Railways Corp (Bus Services) sold to co-operative of NZ operators. &lt;br&gt;• Housing Corp Mortgage sold to TSB Bank Ltd, Postbank, Mortgage Corp of NZ and others (until 1996). &lt;br&gt;• Studies on four SOEs commissioned by Government to reach decision on privatisation. &lt;br&gt;• Government supply brokerage sold. &lt;br&gt;• Taranaki Petroleum Mining Licenses sold to Petrocorp/southern Petroleum. &lt;br&gt;• New Zealand Timberlands sold to ITT Rayonier.</td>
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<tr>
<td>1993</td>
<td>• New Zealand Rail Limited sold to Consortium. &lt;br&gt;• Wrightsons Rights sold to Domestic and International Institutions</td>
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<tr>
<td>1994</td>
<td>• Government Computer Services sold.</td>
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<tr>
<td>1996</td>
<td>• Various airports sold to local authorities. &lt;br&gt;• Maori Development Corporation sold to the Maori Development Corporation. &lt;br&gt;• The Radio Company Ltd sold to NZ Radio Network Ltd. &lt;br&gt;• Forestry Corporation of NZ Ltd sold to consortium of Fletcher Challenge, Brierley’s and Citifor Inc. &lt;br&gt;• Works and Development Services Corporation NZ Ltd sold to Downer and Co and Kintas Kellas.</td>
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<tr>
<td>1997</td>
<td>• Timaru Airport sold for nominal sum to Timaru District Council.</td>
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and operational departments or non-departmental crown entities. For example, the Department of Justice was divided into a policy ministry and operational departments such as Corrections and Courts. For state housing, this has involved splitting off the provision of state housing into a crown owned limited liability company operating on a commercial basis, with policy advice provided by a Ministry of Housing. The Department of Transport, employing 5000 people in 1984, was split into a 60 person policy ministry and a number of independent entities, while traffic officers were absorbed by the police force.26

- Contracting out such things as financial record keeping and auditing, support services, consultancy services and policy advice.

Evaluating the Changes

Reports on the public service reforms have often been laudatory.27 However, there are few detailed empirical studies. Drawing on these reports and other writings, this section critically examines the success or otherwise of the reforms and attempts to highlight failures and reservations that might be held regarding the changes. There do seem to have been significant efficiency gains associated with the reforms. At the same time, there have been significant increases in reporting costs, transitional costs associated with the changes, and concerns raised regarding ownership and accountability issues.

Efficiency Gains

Efficiency is used here in its commonly used sense – that of producing the maximum possible of an acceptable quality and cost of goods and services from the smallest possible resources or inputs.28 Given this definition of efficiency, there seems to be evidence of significant efficiency gains arising since the reforms. Despite the fall in the numbers of public servants, and in some cases decreasing funds, a number of writers claim there have sometimes been either an improvement in the cost, quality and quantity of goods and services from the public sector, or at least no drop in quality and quantity.
The reforms have been successful in contracting the public sector. \textsuperscript{29} Staff numbers decreased from 85,738 in 1984 to 31,810 as at 31 December 1996 (including 14,244 staff employed in Crown entities). \textsuperscript{10} A part of these changes in personnel is attributable to the corporatisation program and subsequent asset sales. The public sector’s share of total employment fell from 27 percent in 1987 to 20 percent in 1994. Government expenditure as a percentage of GDP fell from close to 38 percent in 1987 to 35 percent in 1996/97. \textsuperscript{31} As at June 1996, the public sector consisted of 44 departments, 2,910 Crown entities including 2,677 schools, 16 state owned enterprises, and the Reserve Bank of New Zealand. \textsuperscript{32}

At the same time, there are a number of reports that suggest departmental efficiency has improved. According to the Office of the Auditor General of Canada in 1994, despite the lack of adjustments to departmental budgets to reflect price increases, there is little evidence of falls in either quantity or quality of goods and services. A Treasury survey of four departments found that the first had reduced average unit costs by 10-20 percent over four years, two had significantly increased workloads with only small budget increases, while there was little change in unit costs in the fourth. \textsuperscript{33} Studies by the New Zealand Treasury have found expenditure targets had generally “been achieved with some precision” and that there “is evidence of productivity gains, where unit costs of a sample of standard outputs have been measured over the duration of the reforms.” \textsuperscript{35} According to Scott et al a report commissioned by the Treasury suggested significant savings from improved cash management systems due to better accounting and information systems, and enhanced incentives due to the capital charge. Appropriations had been reduced for five years, without there being observable changes in output volume or quality. \textsuperscript{35} It is claimed that there are observable improvements in the use of assets, especially working capital and cash. \textsuperscript{36}

One major evaluation of the reforms has been the 1996 Schick Report. After interviewing more than 100 chief executives, senior manager, observers and politicians, Schick claims that:

One does not have to search far for efficiency gains in the reformed State Sector. New Zealand managers are convinced
they are doing more with less - in some cases with a lot less - and they have been able to reduce costs because of the new flexibility in managing resources. In interviews, many proudly pointed to cost-saving initiatives: leasing less expensive but high quality accommodation when they were no longer compelled to take premises assigned to them by the government; acquiring state-of-the-art information technology (IT) systems and modern office furnishings when they were liberated from constraining procurement regulations; hiring temporary and part-time workers in response to seasonal or cyclical fluctuations in workloads; eliminating whole layers of management and the controls they wielded; negotiating wage levels that reflect market conditions rather than government-wide civil service contracts. These and other cost savings have been made possible by the reforms. They could not have been achieved if managers were still bound by ex ante controls enforced by central agencies.

Managers have a much clearer understanding of their role and responsibilities; more timely and complete data on the cost of doing business and on what they are accomplishing with public funds; greater awareness of the needs and interests of clients and customers; and expanded opportunity to change operating procedures, the use of resources, and working conditions. They welcome the flexibility to select the best mix of inputs and the option to negotiate individual employment contracts. Many like the explicit output measures that let them know what is expected and how well they are doing.37

Contributing to these efficiency gains were improvements in management practises. A 1995 review of costing systems and user charges found that departments had introduced “sound systems for accounting for expenditure in terms of outputs, but there remained considerable variability and room for improvement in the quality of management accounting systems.”38 According to senior officials interviewed during the Canadian Auditor General’s study, improved
cash management generated savings had covered the costs of adjustment. The 32 public sector managers interviewed by Norman were supportive of the financial management changes and the introduction of accrual accounting. While some had reservations regarding the degree of reporting involved, respondents believed there was:

- Better financial reporting in [their] organisation and at the government level.
- A clear separation of capital from operational expenditure, allowing more rational decision making in the financial field.
- Greater financial discipline and checks on unnecessary activity (as a result of user pays.).

The movement of departmental trading activities into SOE structures may have also delivered significant efficiency gains. The New Zealand Institute of Economic Research found that in the seven larger SOEs revenue increased by 15 percent from 1988 to 1992, while after tax profits rose from NZ$262 million to NZ$1.023 billion. Staff numbers declined by 53 percent during the same period. A study by Spicer, Emmanuel and Powell in 1995 found that among five SOEs “it is reasonable to conclude that Electricorp, CoalCorp, and Television New Zealand are more profitable than their predecessor organisations [and] the Government Computing Service is less profitable on average, but operates with much smaller margins and with a much enhanced operating efficiency.” There is also evidence that customer service had improved in some SOEs. For example, New Zealand Post’s prices for standard letters have decreased in real terms to possibly the lowest in the OECD, while service delivery performance has improved, although some rural towns faced post office closures. There are few detailed studies of privatisations in New Zealand and none have separated out effects of deregulation and technology change. However, the privatized Telecom has been ranked by the World Competitiveness Report as one of the best telecommunication firms in the world and service has, in general, improved.

The lack of detailed empirical work means that claims of unequivo-
cal efficiency gains should be treated with caution. A number of caveats should also be drawn regarding apparent efficiency gains so far measured. Some productivity improvements may be largely due to considerable increases in hours worked, especially in the smaller ministries. This implies that efficiency gains may be in part due to tighter employment conditions and shrinking public sector resourcing, rather than necessarily being a reflection of efficiencies gained through new management practices or institutional change. It is also unclear to what extent apparent efficiency gains are being delivered by such things as the improved competitive environment due to deregulation, improvements in technology, or the political will of ministers. For example, alongside the corporatisation and privatisation process, a number of changes were introduced to the New Zealand economy that increased competition and modified the regulatory environment. This, in part, forced SOEs, privatized firms, departments and their out-sourced providers to become more competitive. Advances in telecommunications and information technology have increased the productivity of individuals and organisations, allowing them to achieve more with less. Finally, the part of ministers themselves should not be ignored. They too may have a considerable role in encouraging increased efficiency in their departments through moral suasion and stressing the need for cost reductions and efficiency, and in the quality of the decisions and suggestions they themselves make regarding policy and appointments.

The great scope of public sector innovations also means that it may be difficult to establish without further study whether all or only part of the changes are delivering efficiency gains. Despite much being made of the integrated nature of the reforms, it is possible some changes have delivered benefits, while the gains of others have been equivocal or negative. As Schick implies, where gains have been achieved these are more likely to be associated with freeing managers to manage, while “problems and disappointments” have been associated with “the contractual mode of reform” (as examined below).

**Economy Wide Effects**

As well as the reforms increasing the efficiency of the public sector,
they may have contributed to a better performing national economy. It seems possible there is relationship between the performance and the efficiency of government and the performance of the economy, although this link is difficult to establish.\textsuperscript{46} There have been fiscal surpluses since 1993/4 with surpluses reaching $1.9 billion or 2 percent of GDP in 1996/7 and $2.534 Billion or 2.8 percent of GDP in 1997/8.\textsuperscript{47} There has been an increase in government net worth so that since 1995/6 it has been positive with assets exceeding liabilities by $3.3 billion.\textsuperscript{48} It has been claimed by Campos and Pradhan that these improvements in fiscal performance are associated with New Zealand’s reforms.\textsuperscript{49} However, as Scott et al point out, such studies do not adequately distinguish between political will and the effects in improvements in management and information systems, although changes in processes may facilitate achievement of political goals.\textsuperscript{50} It is also the case that there may be other factors that contributed to an improving fiscal situation that might not be related to changes in public sector management. These include the efficient broad based GST (VAT) operated in New Zealand and the economic recovery in New Zealand after 1993/4.

It should also be noted that the New Zealand economy has not performed well since 1984 on such measures as economic growth and employment creation. New Zealand has been one of the worst performing nations in the OECD measured in terms of economic growth with GDP per capita declining by 10 percent relative to the OECD average from 1984 to 1994, reaching its lowest of 81 percent in 1992, before recovering to 87 percent by 1995.\textsuperscript{51} While the economy recovered post 1993, growth slowed again after 1996 and by 1998 New Zealand had again entered a recession.\textsuperscript{52} It is possible that the public sector reforms have contributed to New Zealand’s poor economic performance. The shedding of staff by the public sector during the reforms contributed to unemployment, at least in the short term, and may have contributed to the extended recession of the late 1980s and early 1990s. Withdrawal of government services and reductions in employment may have had particularly severe results in regional New Zealand.
Increased Reporting Costs

The public sector reforms have resulted in a substantial increase in reporting costs. The detailed reporting requirements for departments and chief executives include such things as the twice yearly forecasts required in the Fiscal Responsibility Act and the reports and statements required by the Public Finance Act, the extensive review of chief executive performance, as well as the cost of negotiating contracts and monitoring their compliance. Reporting costs will be especially onerous and take up a relatively greater proportion of resources if a department is small. According to some managers interviewed by Schick, "these costs have soaked up a substantial portion of the efficiency gains achieved by their organisation." Similarly, there are extensive transaction costs inherent in the development and monitoring of health contracts required since the health reforms. There is also some irony in public sector reformers borrowing heavily from supposed models of private sector management, at the same time some writers have recognised their limitations in describing actual behaviour in the private sector. For example, considerable work has been carried out on the existence and efficiency of "trust" and reciprocity relationships in business, referred to in the literature as networks or relational contracting. It may be that the new contractual relationships have weakened or replaced pre-existing efficient trust relationships in the public sector.

Nor is it entirely clear that the vast amount of information generated in the various rounds of reporting and monitoring is as useful as proponents claim, or that quantitative measures (such as outputs) provide the best information to monitor the performance of the public sector. According to Mascarenhas, this information may facilitate in the management of the public sector but there is no guarantee or improvement in performance. Information based on performance measures has distinctive uses depending on its purpose . . . Unfortunately the current mood favouring the adoption of private sector measures indicates a clear preference for quantitative indicators over qualitative, overlooking completely the variation in end users.
There are also problems with adequately specifying and pricing outputs. There have also been considerable resources devoted to adequately specifying outputs with mixed success, especially in the case of policy advice. While there have been attempts to develop pricing for outputs, these have yet to meet a large degree of success due to the smallness of New Zealand and the lack of contestability this entails.

Concentrating on an ever increasing series of performance measures may also encourage a "check-list" mentality in management where chief executives perform their specified tasks and concentrate on bilateral agreements with the minister rather than look at broader issues of collective interest, the relationships between different departments, or their individual department's development.

As well as the difficulty in defining quantitative measures (such as outputs) in such a way that they measure useful goods and services of the public sector, performance contracts may not be sufficiently flexible in the face of changing political environments and the uncertainty associated with political demands. This may especially be the case if there are shifting government coalitions, under the recently introduced proportional electoral system, MMP. To insist too strongly on the idea that the minister can independently set outcomes and outputs which they then purchase at arms length from the department is also naive, given the power the department will exert in advising on and developing outputs, outcomes, KRAs and policy priorities.

Ownership Interests

The ownership interests of ministers may not be well served by performance monitoring based on short-term financial reports. Even in business "ownership is not measured exclusively in terms of net financial worth ... Value [is] added by goodwill, management capacity, expected future performance and other intangibles." The minister, as owner, should have some interest in the long term development of the department, and therefore possibly in inputs that facilitate this development, such as training and information systems. However, this interest in inputs is something, as Schick points out, that
runs counter to the logic of the focus on departmental outputs. There is also a danger that ministers could sacrifice the longer term interest of the department for short term political opportunism. According to one former chief executive interviewed by the author:

My main concern is that a combination of political changes and the power imbalance in the contractual arrangements between politicians and the public service may result in significant “principal opportunism” to the long-term detriment of the capabilities of the latter.

There can also be a tension between the ownership and purchaser functions of government, especially in the case of crown entities. According to Gilling:

... it is difficult [for the Crown] to withhold payment until agreement can be reached, as this may jeopardise the viability of the Crown entity. If the entity continues to be paid regardless of whether a contract had been signed, then there is little incentive for the entity to reach agreement with the purchaser.

It remains to be seen whether the introduction of KRAs and SRAs will encourage a greater focus on the collective interest of government and contribute to the achievement of the strategies of government. At the same time, despite considerable efforts devoted to the task, there are still problems linking outputs to government outcomes. Whether the introduction of “standards letters” will improve the provision of qualitative factors and the better preservation of such things as ownership remains to be seen. It is possible, however, that given the difficulties of measuring such intangibles as “leadership”, “collegiality” and “collective interests and tensions” that exists between these concepts and the logic of other reforms, those measuring performance might continue to rely on the existence of supposedly easily measurable outputs and target result areas. Alternatively, adding further measures of performance, without removing others, will just add to the already large burden of performance monitoring.
Transition Costs

It is probable that the transition costs of restructuring have been high. According to Boston et al, it is even possible that ‘in some instances the fiscal and social costs outweighed any subsequent longer term gains in productive efficiency.’ Along with the actual fiscal costs of paying redundancies and other costs such as welfare or other benefit for some of those made redundant, transition costs have included the disruption of government business, loss of morale and the loss of institutional knowledge.

In contrast to public sector reform in Australia which was based on consultation outside and to some extent inside the public sector, the early stages of the New Zealand reforms were very much imposed by a Treasury-ministerial nexus on a public service that was largely unconsulted and unprepared. Lack of communication of the purpose and reasons for some of the changes to lower level staff may have undermined staff efficiency, at least in the short and medium term. The high level and speed of departmental restructuring and redundancies may have contributed to uncertainty, as well as loyalty and morale loss amongst staff, and so affected the efficiency of their work. This may have particularly been the case for operational departments and in departmental services working outside the capital (Wellington) at “the coal face.” There may also have been an erosion of institutional knowledge and memories through loss of staff and the breakdown of personal relationships and networks. Change may have also diluted positive departmental values and induced distrust of future changes. While it is difficult to measure whether there has been a decline in the quality of services given, it is possible, despite claims by the Treasury and others, that quality has deteriorated, in some aspects at least. One former chief executive interviewed by the author implied that the loss of institutional memories meant the quality of legislation in New Zealand had suffered and that ministries and departments needed to consult widely to compensate.

There have also been significant fiscal costs associated with the reforms. These have included the disruption of government business and the resources diverted to developing and carrying out restructuring and paying redundancies, as well as possible subsequent flow on
effects such as welfare and other payments. For example, the cost of paying 1402 redundancies in 1996 was approximately $47.2 million, at an average of approximately $33 666 per employee.  

Theoretical Purity

The reforms in New Zealand are heavily derivative of public choice theory, new institutional economics and new public management. While it is not in the scope of this article to go into any detail regarding the problems with some of these theories, it is worth bearing in mind that they are all contested on both a theoretical and empirical level, particularly in the case of public choice. Critics have questioned whether agency theory is indeed applicable to the public sector. Even some of those mostly sympathetic to the reforms, such as Schick, have reservations regarding the characterisation of public servants as being fundamentally driven by the instrumental rationality of neoclassical economics contained in public choice and the new institutional theories. It is also the case that some of the changes could be criticised using the same theories that are used to justify them. This is particularly the case for transaction cost analysis; as noted, many of the changes, including the decoupling of departments, have involved significant increases in transaction costs. Despite this, there seems to be an unhealthy degree of theoretical purity in some public service publications and amongst some influential consultancy reports. Theoretical positions, often highly contested internationally, are frequently given as accepted truths. This is particularly the case with regard to the policy-operations split.

At the same time, the belief that a better public service can be developed as a thought experiment working from first principles and drawing largely on theoretical models, should be treated with great caution. As Boston et al point out, there is not one best way of designing the public sector and different types of structures will have different advantages and different benefits so that there is often little to decide between models. This means the “quest for a unified or general theory of institutional choice is misconceived.” There is also a danger that a policy revolution working from a theoretical blueprint can be very wrong. A more gradual process where change is made
incrementally may not always provide the “best” solution, but it may at least avoid large errors. A more gradual process may have avoided some of the problems of transition identified above by lessening loss of morale, allowing institutional memory to evolve, avoiding disruption of government business, and reducing fiscal costs.\textsuperscript{77}

**Accountability and Responsibility Concerns**

Concerns have been raised regarding the erosion of accountability involved with the decoupling of some departments and crown entities from central control. In the case of crown entities, concern has been expressed regarding how accountable to the legislature and the executive funds spent on and by the entities actually are, while governance structures have been scrutinised for possible inadequacy of their accountability and monitoring mechanisms. Concerns have also been expressed on whether ministerial responsibility and departmental accountability have been undermined by the public sector reforms in the wake of the Cave Creek disaster in which a faulty viewing platform at Cave Creek in Paparoa National Park collapsed in April 1995, killing 14.\textsuperscript{78}

Crown entities are legally distinct from the crown, but ostensibly accountable to a designated minister. They come in a variety of forms including companies (such as the crown research institutes), trusts (eg Road Safety Trust) and a number of other structures given distinct status by legislation. Crown entities are usually managed by a board appointed by a responsible minister or, in the case of schools, an elected board of trustees. In 1995/6 the Crown had an equity interest of $11 billion in Crown entities and provided revenue of $9.4 billion.\textsuperscript{79} A considerable proportion of these funds do not seem, however, to be either adequately monitored or accountable to the executive or parliament in any effective way. For example, in 1995 the Auditor General (who reports to parliament) claimed that NZ$2.5 billion had been taken out of the jurisdiction of the office.\textsuperscript{80} The Audit Office found it could only look at money defined as “public money” which excluded such things as the funds paid by regional health authorities (RHAs) to crown health enterprises, as RHAs did not fit the definition of government contractors.\textsuperscript{81}
There also seems to be a lack of adequate monitoring of contractual relationships with crown entities and of crown entity governance structures. The Treasury admits this, saying the "extent to which responsible ministers and their advisers do monitor contracts with Crown entity boards, and can or do enforce them ... is uneven." The 1994 closure of one crown research institute, the New Zealand Institute for Social Research and Development (SR&D), provides an example of this. The Institute was a small social research organisation that had devolved from the Department of Scientific and Industrial Research (DSIR). Its closure involved staff redundancies and consequent redundancy payments, the cancelling of a number of research contracts, and the loss of tax-payer funds, as well the loss of a potential source of alternative policy advice for the government. A number of payments in excess of those required by staff employment contracts were made to fired staff. The Institute had received little direct funding from the taxpayer (in this case the Foundation for Research, Science and Technology) compared with the funding once provided to the New Zealand Planning Council or the DSIR Social Science Unit (from which it evolved). It also seemed to have success in attracting private and public sector research contracts.

The reasons the Institute was disestablished are not entirely clear. However, problems with the board-appointed senior management and a lack of willingness to address the issue may have been contributing factors. It was possible the board wished to avoid the embarrassment of removing the manager in question as it is likely this would have resulted in court action and could have endangered the viability of the organisation. There was marginal media interest in the decision, and a question asked in parliament, but the board of directors seemed to have avoided any examination of, or sanctions for, their actions and possible omissions. The Treasury has also drawn attention to the limited accountability and monitoring processes with regard to the Accident Rehabilitation and Insurance Corporation.

Concern has been expressed whether some aspects of ministerial responsibility and departmental accountability have been undermined by the public sector reforms, partly in response to the disaster at Cave Creek. The disaster gave rise to a Commission of Inquiry which, while not holding any individual or collection of individuals jointly
or collectively responsible for the disaster, was critical of the department and claimed that victims “were all let down by faults in the process of governmental departmental reforms.” The reluctance of the chief executive of the Department of Conservation and the responsible minister to resign following the report raised questions regarding real responsibility and accountability under the reforms.

Gregory claims the disaster has highlighted that the public sector reforms have not led to clarification over the lines of accountability, as partly intended. Instead, with reintroduction of the largely untenable policy-administration division inherent in the split between the “outputs” purchased by ministers to achieve their policy “outcomes,” ministers and chief executives “now have statutory grounds for playing the game of passing the buck.” The disaster, where the viewing platform collapsed partly due to the lack of suitable bolts, provides a dramatic, if tragic, illustration of this. As Gregory notes:

What was to be regarded as an output, and what was an outcome, given that the chief executive was responsible for the former and the minister responsible for the latter? Was a bag of bolts an output that should have been “purchased” by the minister in order to ensure a desirable outcome in the form of a safe viewing platform? Was a safe platform . . . itself an output that should have been “produced” by the chief executive.

. . . the matter of buying bolts or of designing and building a secure platform might have been seen as a “mere” matter of administration; but it was one that had huge political and policy implications, and personal consequences.

The new culture of “doing more with less” might have contributed to the disaster and the disaster itself has highlighted the possible obfuscation of ministerial responsibility and departmental accountability that might still occur under the reforms. However, while the sometimes confusing new language of public sector management may have given officials and politicians yet another avenue to attempt to evade blame, it is doubtful that the ministerial response after the tragedy would have been greatly different before the public sector changes.
No minister has resigned for reasons of responsibility since Apirana Ngata in 1934, and that was because of a conflict between duty and interest. There was never a question of anything beyond vicarious responsibility for the responsible minister in the Cave Creek case. In any event, the responsible minister Denis Marshall did resign unexpectedly a year after the disaster, although he remained a minister in cabinet with responsibility for other portfolios. Similarly, while the chief executive did not immediately resign as might have been expected, a number of more junior staff did leave their jobs, with the chief executive resigning two years after the tragedy. Finally, the force that ministerial responsibility still holds as a convention in New Zealand is primarily political as “ministers of the Crown are still politicians who must maintain some credibility both with a parliament and their own cabinet and caucus, as well as with a voting public.” It is possible that this political sanction (especially with regard to loss of electoral support for the government) was important in the Cave Creek disaster.

**Summary and Conclusion**

The radical reforms of the public sector in New Zealand have been much lauded and touted as exemplars for other countries to follow when reforming their own state sectors. These reforms have included introducing contractual arrangements into public sector appointments and performance monitoring; allowing greater management autonomy; changing financial reporting; restructuring and disaggregating departments; and corporatizing and privatising state owned enterprises. There is some evidence of significant efficiency gains in the public sector.

Yet, it is possible that the benefits of these reforms have been oversold. While there have been some efficiency improvements, these have been hard to measure and may be partly to do with improvements in competitiveness through deregulation, technology improvements and political will. It is also possible that where efficiency improvements associated with the changes have been made, these have been more related to the growth in managerial autonomy, some changes in financial reporting, the clarifying of objectives of the public sector.
sector, and the stress on delivering better performance, rather than with the new contractual structures associated with other changes.

There have been considerable costs associated with the reforms. These have included: an increase in costs through the growth in reporting and monitoring requirements; the focus on short-term financial and quantitative measurement with the neglect of qualitative and other "intangible" measures; the comparative neglect of ownership issues; and the considerable transition costs of the changes, including loss of institutional memory, redundancy payments, and disruption of government business. There have also been accountability concerns raised following the reforms and the decoupling and decentralisation of departmental structures. Finally, there is some evidence that even in New Zealand there has been some recognition of the problems with the contractual aspects of the reforms. Since June 1997, the focus has shifted back towards requiring the delivery of more intangible benefits from departmental chief executives including leadership, collegiality and regard for the collective interest of government. It is possible that the benefits that have been delivered by the reforms could have been delivered without the costs and trauma of a policy revolution such as that suffered, and without the complications that have arisen from a sometimes doctrinaire adherence to contractualism and the ever increasing array of reporting requirements.

NOTES


6. A number of Chief Executives, such as the Solicitor General, the Commissioner of Police, and the Chief of the Defence Force are appointed under different conditions.


9. The figures for crown entities were 29.9 per cent on individual contracts as at 31 December 1996, up from 16.5 per cent two years previously, with 12 per cent on fixed term contracts.

10. Input controls were previously provided by the highly detailed Treasury instructions. Departments were also required to use centralised monopoly suppliers.


12. A 1994 amendment to the Public Finance Act placed all appropriations on an accrual basis, with exception of departmental capital contributions and repayments of debt, which are cash based. There are seven types of appropriations. These are: expenses incurred on each class of outputs; benefits or other unrequited expenses; borrowing expenses, capital injections; the purchase or development of capital assets; and repayment of debt. The allocation of expenses to outputs is made by the individual departments according to their individual cost accounting policies, which must be disclosed, in the department’s financial statements (see Ball, I. “Reinventing Government: Lessons Learned From the New Zealand Treasury.” The Government’s Accountants Journal Fall (1994), pp.19-28). They should, however, be able to identify the full cost of outputs. There are also attempts to develop ‘prices’ for outputs through such methods as competitive tendering, price and performance benchmarking and creation of shadow pricing (see Dangerfield, Geoff. “Key Issues for the Future of Public Management.” Paper delivered to Future Issues in Public Management, State Services Commission, Wellington, New Zealand (1997).


14. The Financial Reporting Act 1993 established the Accounting Standards and Research Board. This was to set accounting standards binding on both the private and public sector. The Government and Departments produce the following financial statements: statement of financial performance (operating statement); statement of financial position (balance sheet); statement of cash flows, and statement of contingent liabilities. Departments also produce statements of objectives and statements of service performance. A balance sheet with an attached audit opinion is produced within three months of the end of the financial year.


17. Examples of KRAs for the Ministry of Commerce include:
   - Further reduce barriers to the free flow of goods and services by facilitating an effective interface between New Zealand's regulatory and border regimes and those of other countries
   - Establish and monitor programs to reduce compliance costs and develop proposals to improve the quality of regulation. Quoted in Boston and Pallot (1997).


24. In New Zealand the term "department" is usually applied to government organisations that provide operational services, as well as policy and regulatory functions while "ministry" is usually applied to organisations that provide policy and regulatory functions only. These names are not consistently applied however.

25. Formerly Crown Health Enterprises.


Internet site http://muldoon.govt.nz/pubs/canada/report1/toc-can.htm, 1995. It is worth noting that there is some overlap in those contributing to the reports and those instrumental in initiating the changes. Dr Graham Scott, a former Treasury Secretary was important in the Canadian Auditor General’s report, while the Treasury are always important in assisting in the preparation of the NZ OECD reports.  
28. This is similar to what is called production efficiency in economics.  
29. For those who believe that a smaller government is necessarily a better one, something inherent in some of the New Right thought influencing the public sector reforms, this would be seen as a positive outcome in itself.  
30. This comparison may overstate the change as the 1984 figure is by head count while the 1996 figure is by full time equivalents.  
35. Scott, Ball and Dale (1997). Unfortunately an absence of clear references to the source of these ‘Treasury reports’ cited by the various government reports and writers makes it difficult to establish if they are indeed different ones, or the same ones differently reported.  
46 There also seems to be a number of examples of national, regional and metropolitan economies that seem to perform well despite relatively inefficient and/or corrupt public sectors  
Evaluating Public Sector Reform in New Zealand

50 Scott, Ball and Dale (1997)
54. There has been an increase of 10.9% in the twelve months to June 1996 and 10.6 per cent to 31 December 1985 in those employed by the Ministry of Health.
57. It is especially difficult to establish useful quantitative measures for policy advice.
60. As well, there may be further costs in negotiating new contracts between governments and chief executives. It may be however that the KRAs are vague enough as to allow sufficient flexibility for chief executives.
61. This belief that there can be an administration-policy split is one that is rejected in most public administration literature. See, for example, Campbell, C., and D. Naulls, "Policy Makers and Facilitators: The Boundaries Between Two Bureaucratic Roles," in H. Clarke and M. Czudnowski, eds., Political Elites in Anglo-American Democracies. (DeKalb. Northern Illinois University Press, 1990)
63. Ibid, p.45.
68. Some Departments, such as Social Welfare, were reorganised several times during this period.
69. Some respondents in Norman’s (1995, 2) study felt there had been a ‘horrendous loss of institutional memory’.
70. Some of those taking redundancy were able to set themselves up as consultants and sell their knowledge and skills at higher prices back to the public service, often to their previous employers.
73. The number of persons affected by restructuring in 1996 was 1447. The worst
year I have (very approximate) figures for is 1992 in which around $85 million was paid out in redundancies and over 2000 employee affected by restructuring.

77 For example, allowing a greater level of natural attrition rather than large redundancies.
80 Mascarenhas, p.236
81. In 1998 regional health authorities were amalgamated into the Health Funding Authority
83. Some research contracts were continued by staff after they left the organisation.
86. Gregory (1998), p.239.
89. The standard letters given to chief executives now suggests they resign after serious failures in management for reasons of public interest. This is the case even though they might not consider themselves at fault and that there may be no legal obligation for such a resignation.

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