AGENCY THEORY AND AGENCY ENVIRONMENT: ELEMENTS AND RELATIONS WITHIN BRITISH CIVIL SERVICE

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Abstract

This article examines an important tool of politics, the dichotomy between politics and administration, to reform administrative systems. Due to its success and the pioneering role in the implementation of agency reform and resultant provision of lessons for many countries (i.e. Netherlands and Norway) the British case is selected for evaluation. The British Next Steps Agencies Reform is examined by deploying historical reconstruction model, and intended to find out its basic elements and interactions between different such actors of the initiative as politicians, bureaucrats, agencies and departments. This illustrates the scale and scope of the relations with the idea of having shed light on Agency theory. Having examined the essential elements the study wishes to focus on the mechanism which has been introduced by the initiative dispenses certain degree of power to agencies. In doing so, the paper targets a balance between two actors of political systems, bureaucrats, and politicians.

Keywords: Agency theory, administrative reform, the Next Steps initiative, policy-making.

1. Introduction

The Next Steps agencies reform is concerned primarily with delegation of power from the centre (of the ministries) to semi-autonomous agencies created out of an administrative reform in the UK. This essentially states that the agencies are evolved as separate entities by promoting certain common values and principles. Further, the position and responsibilities of the chief
executives are important as they practice the power emanating from the departments. The characteristics and the management of the organizations were developed in a unique fashion shaped by the leadership and the task. Autonomous executive units with a distinctive leadership, style and culture have the prospect of empowering the staff and encouraging their achievements. Agencies have been able to implement New Public Management type of elements to public bureaucracy since their establishment by Mrs. Margaret Thatcher in 1988.

The Next Steps ideology is based on the assumption that civil service work should be kept in the public sector, but directed by private sector values. As Mellon identifies in her empirical study, the initiative seeks to promote this end by using semiautonomous organizations with an empowered leadership.¹ In other words, the restructuring process requires separately identified organizations headed by chief executives who would be publicly or directly accountable for their agencies’ results. Therefore the Next Steps practice necessitates an assurance that agencies are handed to chief executives with ‘freedom to manage’. As Robin Butler, the then head of the civil service, states: “organizing those units as self-contained agencies makes it possible to define their mission more precisely and to delegate responsibilities to a Chief Executive accountable for achieving the mission”.² The aim of delegating responsibilities to Chief Executives was to promote efficiency and effectiveness of the agency business as well as creating a common ‘agency culture’.

The study aims to examine the relations between the actors of public administration, namely bureaucrats, politicians, ministries and agencies. Being based upon a micro-economy based theory, and driven by efficiency concerns, the Next Steps Agency reform provides a basis for evaluation of application possibilities to public administration. Therefore, this paper examines principal-agent theory and Next Steps history to foster a medium to discuss the

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relations within agencies. Having done so, there emerges a possibility to draw certain lessons for public administrations, as the reform introduces a power-share mechanism among different and often conflicting interests of actors.

As to methodology, the paper intends to highlight elements and relations with the idea of evaluating official and non-official documents. In other words, official publications, especially the discussions in the Treasury and Civil Service Committee of House Commons provide certain insights into the subject matter. The main reason for the examination of the period, namely during the first part of the 1990s has been an intentional one, as the disputes and discussions related to elements and relations were wide-spread in the era. So, the examination of the 1990s poses the potential of digging into very basic discussions, and therefore uncovering the relations in a simple environment, as during the following period the relations have been full of contradictions and complexities.

The article is divided into four sections. Following this introductory section, the second section deals with the theoretical and conceptual underpinnings of the case, including the scale and scope of the Next Steps reform and Agency theory. The third section evaluates the elements of the Reform and examines the relations within agencies. The components of the reform are reviewed to ‘test the waters’ for other countries which intend to learn from the British experience. The concluding section summarizes the findings.

2. Theoretical Examination: Agency Theory

As the following section highlights, the British administrative reform experience of 1988 has been set to sort the basic dilemma of administrative systems by restructuring the relations between two main groups of actors in public policy, namely the civil servants at the centre and periphery. The main actors of the reform were liberal-minded people from politics, public services and the civil society. Due to the strong personality of the Prime Minister, Margaret Thatcher, and the major issues of public
services in Britain throughout the 1980s the reform found a warm reception from different segments of the society at large.

The theoretical aspects of the Next Steps reform can be examined through the findings of the principal-agent theory. Like public choice, it is a branch of micro economic theory and therefore its essential assumptions indicate its economic orientation. In other words, the theory’s usage in politics or in sociology includes micro economic terms and concepts such as rationality and the notion of equilibrium.³

The principal-agent approach is indeed central to administrative theory. Principals (either politicians on behalf of the citizens or departments on behalf of the politicians) employ agents (either individuals or organizations) who have ‘professional’ knowledge to fulfill public services. Agency theory deals with the inter-relations between two actors, the agent and the principal, in situations where pure market organization does not apply.⁴ The relationship between the agent and the principal is between two tiers of a government. The theory implies that professional knowledge increases from top-to-bottom in public administration. Principal and agent represent administrative and professional functions respectively. In this vein, administrative function involves general ‘policy-making’ activity, while professional function is dealing with ‘implementation’ of public services.

The main aim of the application of such a distinct theory to practice is to create clearly-defined relations which are capable of pursuing efficiency and good use of resources. According to the theory, the agent is contracted to conduct specified activities. Therefore the principal retains a considerable amount of power to contract the ‘business’, to monitor and to control the outcome, and, if necessary, to punish or to get the service compensated,

whereas the agent is operating with a semiautonomous status and given a resources and responsibilities framework.\(^5\)

Initially, the theory was not intended to explain the political phenomena, but eventually it was applied in this way. Five basic assumptions identified by the theorists are worth examining to get a clear insight into the theory. Worsham et al. present these assumptions clearly, and briefly.\(^6\) Though the assumptions are general, their presentation is reasonably convenient to follow. Jensen and Meckling make the basic point of the theory that “if both parties to the relationship are utility maximizes there is a good reason to believe that the agent will not always act in the best interests of the principal”.\(^7\) Lane also asserts that “Public leadership in management functions may be exercised by administrative personnel or professionals and it may not be easy to draw the line where administrative authority is to reign and where professional authority is to be decisive. The tension between administrative routine and professional requirements is endemic in public administration”.\(^8\) So, we can mention two kinds of problems in the relations: first, the ‘agent problem’ is caused by the conflicting goals of the sides and by the difficulty involved in monitoring the agent’s behavior. Second, the issue of ‘risk-
sharing’ is caused by the differing views of risk from the perspective of the agent and the principal.⁹

To sort out the conflict the principal has to control the agent and to ensure that to a certain extent, the agent’s self interest matches the principal’s objectives.¹⁰ This nature of the relationship encourages us to accept that the principal ought to have more than one agent. Possessing more than one agent, however, limits the actions of the principal as to monitoring and making sure that they respect the objectives of the principal. The agent might pretend to be observing the objectives of the principal.¹¹ This is ‘asymmetric information’.¹² If the principal cannot observe the actions of the agent who possesses strategic information, the case of asymmetry occurs. Spremann highlights the difficulty that “the agent could make any promise with respect to his action and depart from it later on just because the principal is unable to control or to monitor the agent’s decision making”.¹³ Principals have some options to ensure that agents satisfy the expectations of principals, for example they might offer promotion, and performance -related pay if targets are met, or negative incentives such as losing bonuses and dismissal.

Laffin argues that using contracts to limit agent opportunism is the best way to overcome information asymmetries.¹⁴ The problem related to this aspect is to shape contracts in a way that serves for the objectives of the principal. Contracts were specified

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¹² Spremann, Agent and Principal, 6.
¹³ Ibid., 7.
by agency theorists on the basis of a formal model in which the outcome determined by the agent’s level of effort.\textsuperscript{15} 

The principal pays the fee and ‘enjoys’ the outcome. Nilakant’s equity model is reliable to explain and to illustrate the issue.\textsuperscript{16} 

The payoff is denoted by $x$, the level of effort of the agent as $a$, and the exogenous random element as $t$, then the relationship between the agent’s effort, the value of the output and the realization of the random variable is given by a production function $X$,

$$x = X(a, t)$$

The model makes two important assumptions: first is that “greater effort by the agent results in greater output for any value of $t$”. The second assumption is that “only one of the parties directly influences the probability distribution of the outcome”.\textsuperscript{17} 

The model’s main concern is on optimal fee schedules that create positive incentives for the agent’s activity. It is shown by this approach that agency theory is not only a contracting theory between agents and principals, but a theory of performance of the agent.

The theory assumes that the agent is risk-averse, while the principal is risk-neutral. Nilakant examines this issue and concludes that two scenarios are possible: the ‘optimal contract’ under incomplete information is the first one, and the ‘optimal contract’ under complete information is the second one.\textsuperscript{18} This indicates the existence of the first-best and second-best contracts. The first-best contract is similar to a wage contract, whereas the second-best contract places the outcome as a basis for the agent’s compensation. The more the agent works, the more the agent achieves. Since the agent is assumed to be risk-

\textsuperscript{15} Nilakant and Rao, Agency Theory, 653.
\textsuperscript{16} Ibid., 653.
\textsuperscript{18} Nilakant and Rao, Agency Theory, 654.
averse, the second-best contract causes a welfare loss to the principal. Nilakant suggests three kinds of actions to prevent any efficiency loss by the agent: to develop more efficiency monitoring strategies to observe the agent better; to base the agent’s compensation on his/her performance over a number of time periods, the role of chance events can be reduced and; to base the agent’s compensation relative to the performance of other agents, level of risk imposed on the agent is reduced.  

These theories have put a new emphasis on the design of new agencies designed to produce incentive structures which will create conformity to the principal’s preferences. The design aspect is dealt with in the following heading.

3. The Next Steps Case

The thrust of the Next Steps reform is something that has objectives and methods similar to New Public Management approach. Though the latter was a broadly defined package, publications which resulted from its introduction led to a ‘rediscovery’ of the former. The principles advocated by NPM were/are prescribed by the Next Steps initiative. For example a central principle of NPM, ‘output orientation’, is the centerpiece of the Next Steps initiative in Britain. In practice, this involves the separation of policy making and implementing functions, empowering chief executives and agencies, and the use of competition within the public sector.

The Next Steps agencies are designed as a vehicle in which to drive market techniques to the civil service. The Next Steps has tried to sort out the basic problems of government by introducing contractual relations in a manner that clearly distinguishes the appropriate responsibilities of various actors. Although the Ibbs Report, the founding study of the Next Steps, made it clear that

19 Ibid., 654.
20 Önder Kutlu, Comparative Public Administration, (Konya: Çizgi, 2006), 36.
21 Oliver James, Executive Agency Revolution in Whitehall (Basingstoke: Palgrave Macmillan, 2003), 5-9.
“they use the term ‘agency’ not in its technical sense but to describe any executive unit that delivers a service for government”, in retrospect, albeit unconsciously, it has been oriented from agency theory.\textsuperscript{22} Similarly, the contractual nature of the reform initiative has its roots in agency theory, too. Of course, one might argue that the theory may have been intentionally or unintentionally established. But, as is argued herein, market techniques have been intentionally introduced and contracting-out, internal markets, delegated financial control, and semi-autonomous agency structure are nothing but the tools of agency theory.

In November 1986, to drive managerial change in the government, PM Thatcher asked Sir Robin Ibbs of the Efficiency Unit to investigate ‘the next generation’ of organizational change in Whitehall, namely in British civil service.\textsuperscript{23} The report, Improving Management in Government: The Next Steps was conducted as a scrutiny in 90 days.\textsuperscript{24} In contrast, it did not focus on a particular service or a particular function, but intended to investigate the managerial reform since Mrs. Thatcher took over the power.\textsuperscript{25} By May 1987, the report was submitted to the Prime Minister.

Based on interviews with ministers and civil servants, the report concluded that most civil servants concerned with delivery of governmental services, and welcomed clearly defined management tasks and devolved budgetary responsibilities. As stated by Greer, the initiative also raised the conventional dilemmas of the public sector administration: “How do we divide policy and operational matters? How do we balance accountability

\textsuperscript{24} The Ibbs Report, Improving Management
\textsuperscript{25} Spencer Zifcak, New Managerialism: Administrative Reform in Whitehall and Canberra, (Buckingham: Open University Press, 1994), 70.
and autonomy? How do we minimize transaction costs?”. The Next Steps Report was published in February 1988, after the parliament election, identifying the following problems: “Top management is dominated by the policy and political support tasks; responsibilities for management at the top of the departments are unclear; the main pressure at the top is short term; outputs are neglected; there is little support or pressure value for money; the organization at the centre of government is fragmented; the civil service is too big and diverse to be run as a single rigid organization; central rules take away the flexibility manager need to manage; delegation is not always happening; the culture of the Civil Service is cautious and works against personal responsibilities; working and career patterns have changed relatively little”. This scathing attack led to three conclusions: “The lack of focus of top management on the service delivery and executive functions of government; the effects of treating the Civil Service as a single organization; the lack of effective pressure to get better results.” As such:

The report made three recommendations:
- We recommend that ‘agencies’ should be established to carry out the executive functions of government within a policy and resources framework set by a department;
- We recommend that departments ensure that their staff are properly trained and experienced in the delivery of services whether within or outside government; the staff will then be in a position to develop and interpret government policy and manage the agencies in a way that can maximize results.
- We recommended that a full Permanent Secretary should be designed as ‘Project Manager’ as soon as possible to ensure that the change takes place.

The first of these recommendations, the creation of executive ‘agencies’ was implemented. The second part of the

27 The Ibbs Report, Improving Management
28 The Ibbs Report, Improving Management
29 The Ibbs Report, Improving Management
recommendations was also implemented, as it is this framework that sets out the structural characteristics of agencies. As to the third recommendation, a Project Manager of Next Steps, Peter Kemp, was appointed with second permanent secretary status, with a small team working under him. The brief for Kemp and his team was to achieve the government’s stated objectives.\(^{30}\) The following tables illustrate different types of agencies in different departments.

**Table 1. List of Selected Next Steps Agencies**

<table>
<thead>
<tr>
<th>Name of Agency</th>
<th>Name of Ministry</th>
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<tbody>
<tr>
<td>Treasury Solicitor’s Department</td>
<td>Attorney General’s Office</td>
</tr>
<tr>
<td>Companies House</td>
<td></td>
</tr>
<tr>
<td>Central Office of Information</td>
<td>Business, Enterprise and Regulatory Reform</td>
</tr>
<tr>
<td>The Fire Service College</td>
<td>Cabinet Office</td>
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<tr>
<td>Royal Parks Agency</td>
<td>Communities and Local Government</td>
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<td>British Forces Post Office</td>
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<td>Government Decontamination Service</td>
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<tr>
<td>Meat Hygiene Service</td>
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<td>FCO Services</td>
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<tr>
<td>Forest Enterprise (England)</td>
<td></td>
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<tr>
<td>NHS Purchasing and Supply Agency</td>
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<tr>
<td>Criminal Records Bureau</td>
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<tr>
<td>Higher Education Funding Council for England</td>
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<tr>
<td>HM Prison Service</td>
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<tr>
<td>Forensic Science Agency</td>
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<td>Northern Ireland</td>
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<tr>
<td>Driver and Vehicle Licensing Agency</td>
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<tr>
<td>National Savings and Investments</td>
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<td>Child Support Agency</td>
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Although the Project Manager is responsible for making things happen, it is not his/her job to suggest agencies. Departments are responsible for identifying which activities may be suitable for agency status. Before an agency is set up, departments must consider three alternative options: abolition, privatization, and contracting-out. Moreover, the attempt has been designed to import certain private sector values to the public sector. Thus, ‘value for money’ thinking has gained momentum. So the notion of managing or controlling is seen in terms of four characteristics as a discrete organization, a defined task, a formal agreement setting out targets, and an identifiable Chief Executive accountable for the work of the agency.

Around 75% of total civil servants work in around 130 agencies now, counting over 300 thousand public employees. Table 1 illuminates the scale and scope of the change introduced since 1988.

4. Elements of Next Steps

Basically, there are six Next Steps features characterizing the components of the initiative: separation of the policy making and implementing functions; minimizing the political involvement of the politicians; empowering chief executive and agency; promoting openness; creating a common culture; and, focusing on the targets and performance-related pay. These elements are not available to the same extent in the Next Steps, some are explicit and some are implicit.

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33 Civil Service, 2010.
In line with many administrative theorists since Woodrow Wilson\textsuperscript{34}, the Next Steps reform has planned to establish executive units which are “to carry out the executive functions of government within a policy and resources framework set by a department”.\textsuperscript{35} According to the report, as mentioned, departments will be responsible for ‘policy’ matters which cover framework documents, budget, specific targets and the results to be achieved, whereas the executive agencies are dealing with operational and day-to-day issues.

Figure 1 illustrates the relations between agencies and government departments/ministries. Both actors have got certain responsibilities and privileges and they have to provide something to get other things.

**Figure 1. Agency-Department Relations**

![Agency-Department Relations Diagram]


It was thought that if resources and clearly identified responsibilities framework were given, agencies could achieve better results by focusing on the work to be done.\textsuperscript{36} Apparently, the most discussed part of the reform in the government, in the academia, in the parliament, and in the media has been the assumption of separation. The theory’s basic assumption was the


\textsuperscript{35} The Ibbs Report, 9.

\textsuperscript{36} HC 410, 1.
belief of separation in policy and operational matters. In reality, however, it has long been discussed and many eminent scholars and practitioners have not come to the conclusion that that kind of separation could be made.\textsuperscript{37} However, some others asserted that “the distinction...is more workable in practice than is supposed; and Next Steps does not depend on as sharp a divide as its critics imagine”.\textsuperscript{38} Surely, both policy making and implementation have very close ties which cannot be easily broken.

The Fraser report criticized the initiative as being so appropriate for weakening the amount of autonomies of the agencies, this meant lesser amount of flexibility and lack of autonomy for agencies.\textsuperscript{39} Nevertheless, lack of delegated power is not a virtue, especially in the ‘new public management’ era.\textsuperscript{40} The ‘type’ of agency plays very important role in identifying policy and operational matters, because there is a direct relation between the type and degree of difficulty.\textsuperscript{41} In Social Security Service for example, because of its sensitivity, operational issues become policy issues. Every decision made on applications contains policy functions as well as operational one. Therefore, service impact of policy decisions and policy impact of service decisions retains the conflict, and difficulty in itself.

Minimizing the involvement of politicians, the second element of the Next Steps, is a logical outcome of the separation in that responsibilities of every actor is identified and they play the role given by their Framework documents. Some academics argue,

\textsuperscript{39} A Report to the Prime Minister (The Fraser Report), Making the Most of Next Steps: The Management of Minister’s Departments and Their Executive Agencies, London: HMSO, 1991.
\textsuperscript{40} Kutlu, Comparative, 71-73.
however, that Next Steps consolidates politicians, namely ministers, with more powers as they are able to access to more information. The information, nonetheless, requires special skills and knowledge. So in practice, the availability of information may not mean much to politicians as they generally lack the knowledge required of the agency or area involved.\textsuperscript{42} Besides, the emphasis in this paper is on the identification of the civil servants as professional, appointed actors.

The creation of a common culture is the morale element of the Next Steps relevant to the transformation of the bureaucracy to its pattern. The Agency reform in Britain has achieved this goal by introducing a series of measures such as delegating personnel and financial powers to agencies, establishing separate administrative units, and setting quality standards and yearly targets.\textsuperscript{43} Relatively small and unified organizations (agencies) with distinctive features have a better chance to focus on meeting quality standards and targets. This orients members of any agency towards having a sense of solidarity and a separate identity.

Four implications can be derived from this examination, primarily for the Next Steps as ‘features’. Firstly, the ‘creation of a common culture’ for agencies in particular and civil service in general was an obvious element which was facilitated not only by the Next Steps reform but also by earlier attempts such as Rayner Scrutinies and FMI in Britain.\textsuperscript{44} Secondly, ‘separation of operational and policy functions’ was another element which was the basic feature of the agencies reform in order to improve efficiency of the civil service. Thirdly, the congeniality of the reform to the service required the ‘empowerment of Chief Executive and Agency’. In order to achieve this objective, as Bardwell highlights, Chief Executives are expected to have five


\textsuperscript{44} Kutlu, Administrative, 156-159.
types of leadership behavior: pioneers; visionaries; team leaders; role models; and, motivators. 45 This has been effective in motivating agency staff to work hard and achieve targets given for their operations. Fourthly, as a logical extension of these elements, ‘minimizing political involvement of politicians’ has also been a clear element of the Next Steps in the British civil service. In theory, Agency Framework documents and separation of the functions leave no room for confusion and ambiguity of responsibilities. In practice, however, needs to be examined in detail. Beside with their derivations from the Next Steps, the above elements provide a suitable ground for comparison as they are also relevant for other countries, say Turkey.

Independence and the development of ‘culture creation’ function in the agencies also deserve attention. Agencies having a certain degree of independence can decide their own way of dealing with problems and responding to situations. This gives personnel in a given agency a sense of belonging to a ‘special’ and ‘different’ organization than the ‘regular’ civil service. Moreover, morale among the staff of agencies increases and certain symbols mean different things from their immediately obvious meaning including the names or logos of the organization. The staff starts to behave in a particular way when similar problems occur. In this way, then, the agency reform has helped to create a common culture first in an agency and then in the agency system as whole. 46

Another feature of Next Steps is the ‘promotion of openness’ within administrative system. Charging the Chief Executive with the responsibility for replying to questions from MPs is a way of promoting openness. This makes the agency chief executives more visible in front of the public and implies that they have both the right and the responsibility to reply questions regarding their agencies. Publication of many annual reports, business plans, and framework documents are other obvious method of agency promotion. Agencies use the internet to publicize their success

46 Civil Service, 2010 (08.02.2010).
and express their versions of their performance. What is more, they issue press releases quite frequently to inform the public about their work or to introduce changes or amend rules and regulations.

An additional Next Steps feature is ‘focusing on the targets and performance-related pay’. The initiative donates special importance to this aspect by setting targets for agencies and asking them to achieve. In addition, the reform introduces performance-related payment to encourage and motivate agencies to increase their efficiency and effectiveness. The personnel know that the more of the targets they achieve the greater the rewards they will receive. As a result they work hard to achieve their targets and receive bonus financial benefits. Tangentially, staff might also recognize that increased performance helps the agency to remain as it is, as an agency, rather than being contracted-out or privatized.

An empowered chief executive and agency will create a positive attitude among the staff to concentrate on the work to be done. Open competition ensures that the chief executive strives to motivate agency staff to believe and act in such a way that they resemble a family in which the happiness of one member affects others. The Next Steps agencies reform has adopted a contractual form of organization in order to make sure that agents act in the interests of their principals. The main contract between the two parties are framework documents which, together with annual business plans and five yearly corporate plans, set out the framework and structure in which agencies must operate. Every agency should have a framework document with five basic elements: the aims and objectives of the agency; the nature of its relations with Parliament, ministers, the core department, other departments and other agencies; the agency’s financial responsibilities; how performance is to be measured; and the agency’s delegated personnel responsibilities and the agency’s role and flexibilities for pay, training and industrial relations arrangements.\footnote{HC 410, The Next Steps} Containing these features, the Next
Steps reform is a revolution in restructuring relations and redefining the central characteristics of the civil service.

Contracts, in the shape of framework documents, have a vital importance in this process in the sense that they, like constitutions, set up the structural dimension briefly, list the targets to be met, and clarify the relations between actors. Moreover, the periodic re-negotiation of framework documents provides machinery for monitoring agent’s performance and builds in the expectation that effective monitoring by principals will take place. Meanwhile, producing framework documents is not an easy task: it requires skilful persons, deep familiarity with law and regulations and the ability to predict possible. This implies Transactions cost theory And, in addition, requires searching out and to monitoring of the outcomes of the agency work, and eventually control and evaluation of the results in order to assess whether the agency has met its targets or not.

Contracts have been introduced to the civil service to replace the existing hierarchical relations with a market oriented one. Take the appointments of agency chief executives as an example. They are appointed on a short-term contract basis either from ‘inside’ or from ‘outside’ the civil service. They may be entitled to have performance-related pay and bonuses but may also be dismissed if they cannot provide a certain level of satisfaction. Furthermore agency staffs have also been given some incentives and sanctions in respect to the performance of agencies. For example, group performance pay can be earned by all agency staff if the yearly targets are met, and individual performance-related bonuses are available for rewarding senior agency staff.

Again, the ‘contract’ is the key word of the initiative and it is visible in various relations: framework documents, yearly business plans, five yearly corporate plans, service level agreements between agencies, and individual staff contracts. The Next Steps Initiative has asked that agencies and public organizations use contracts in every possible instance. As a

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48 Barry Hugill, "A Civil Service on its Last Legs", The Observer, (29.05.1994).
result, some agencies have moved to the position of being principals for other agencies, while, at the same time, they continue to be agencies of their parent departments. The basic principal-agent relation is between the ‘core’ departments and the agencies.

For principal-agent theorists, the key is to design the institution so that the agents are incentivized to pursue the aims of the principals and to set up monitoring arrangements that ensure that agent behavior can be monitored and, if necessary, controlled. The Next Steps agencies reform is consistent with this aspect of the theory. Targets and performance bonus systems and the autonomy given to the agencies provide a reasonable ground to motivate the executive agencies to increase their efficiency. Success benefits both sides: agencies continue to enjoy ‘the freedom to manage’ and financial benefits (and for the Chief Executives another term in office) and principals are provided more efficiency and outcome.

5. Relations within Agencies

In the relational frame of the reform the term accountability is used to cover two levels of politics: the first is the accountability of agencies to the departments and the second is the accountability of the ministers to the parliament in the form of ministerial responsibility. The term autonomy, however, will be used here mainly to discuss the relations between agencies and departmental HQs.49

The Next Steps reform is designed to take power from the centre and devolve it to the new executive agencies. The initiative has become successful by allowing civil servants to continue to concentrate on policy work and by giving agency staff the prospect of escaping from Treasury control and exploiting their independence. The idea and the method of the selection of the chief executives show that, when they are running their agencies,

they are relatively free from the traditional Whitehall constraints of upwards reporting.

Two important factors affect the amount of autonomy devolved to agencies: the extent of autonomy given to agencies at their launch and the role of the agencies in drafting framework documents. Regarding the first factor, agencies have variable degrees of autonomy and responsibilities. Depending on both the nature of the job to be done, and the economic and political environment, agencies are given a certain amount of responsibility and power to fulfill their duties. Given the fact that positions of agencies are reconsidered every three years to consider whether they should remain an agency or be privatized, the initially granted autonomy still has a steering role in the prospect of the executive agencies.

The second factor, on the other hand, may be more important than the first one, because it is the functional and active part of the issue. When a decision is being made about agencies, they should be given role in the decision-making process. In administrative policy making, it is easy to make a decision but often very difficult to implement it. To make more efficient and effective decisions, to set targets and to prevent resistance from the operational actors, departments need to consult with them. Agencies argue that only they are in the right position to set targets, whereas departments allege that unless targets are formulated centrally they cannot be realistic.

After examining the relations between departmental HQs and their agencies, the Fraser report of the PM’s Efficiency Unit criticized the Next Steps as being reluctant to delegate power to the agencies in 1991. Sir Angus Fraser, PM’s efficiency advisor, when answering the questions of Treasury and Civil Service Committee of the House of Common, said that:

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51 A Report to the Prime Minister
We think that the environment ought to be changed from being restrictive to becoming enabling. Operating constraints should be specified and justified afresh by those who want to retain them rather than freedoms always having to be fought for by the Chief Executives.

The main recommendation was that departments should devolve as much power as possible to the agencies. Therefore, the government’s basic argument for establishing such a reform should be consistent with the practice. The report’s recommendation of devolution is on the three aspects of the power. The report says that:

The objective should be to move to a position where Agency Framework Documents establish that, within the overall disciplines of the cash limits and targets, managers are free to make their own decisions on the management of staff and resources except for any specially reserved areas. The exclusion of any area from the Chief Executive’s authority should be positively justified.\textsuperscript{53}

Two aspects - control over finance and control over staff - are mentioned here but the other aspect, the power to adopt policy goals, is mentioned in TCSC by Sir Fraser: “It is implicit in the idea of delegation to Chief Executive that they may wish to vary some conditions of service”.\textsuperscript{54} Otherwise the report did not want to alter any legal autonomy given to the agencies. The basic idea behind these recommendations was to make agencies more efficient delegating more power.

It should be noted here that not all the agencies complain about the lack of autonomy. Mike Fogden, for example, the Chief Executive of the Employment Service, clarified his agency’s position as to influencing policy:

\begin{flushright}
\textsuperscript{53} A Report to the Prime Minister, para 2.7  \\
\textsuperscript{54} TCSC Seventh Report.
\end{flushright}
Indeed not only influence but, in fact, the Department look to us for information to enable policy formulation to proceed....In our Framework Document there are two key sentences: one is that the Chief executive is permitted to make proposals for policy changes to the Secretary of State, but equally as important, and perhaps some would argue more important, there is also a sentence which says no policy proposals regarding the work of the Employment Service can be made to the Secretary of State until we have actually been consulted.\textsuperscript{55}

The second aspect of the accountability issue which deals with the relations between departments and parliament contains similar problems as the first aspect. Basically, it faces the difficulty of how to accommodate the accountability of government to parliament. By launching the agency system, separating operational and policy functions and empowering the chief executive, the initiative has added a new tie to the existing system and eventually this has caused further confusion. In this vein, Hogwood argues that before 1988 ministerial responsibility was never clear for all executive activities.\textsuperscript{56} One thing to remember is that before the Next Steps the tradition of ministerial responsibility had been in effect and after the Next Steps it remained in effect. The important thing to note is the characteristics of the tradition, especially how empty it is as a means of control, something of a force in reality as the Westland Affair, the Clive Ponting Case, and the Churchill-Matrix Affair revealed how ministers cynically misled parliament.\textsuperscript{57}

As Elder and Page assert, early commentators on the Next Steps reform program suggested the development of the accountability and control over ‘an extended period’.\textsuperscript{58} However, the Next Steps

\textsuperscript{55} Ibibd.


reform intends not to change the fundamentals of ministerial responsibility but to alter the mechanics of how it is implemented. Accountability of the executive power to the legislation has been reorganized according to the functional separation. First of all, chief executives are appointed as Accounting Officers of their agencies to be directly responsible to the parliament for the deeds of their agencies. Ministers and departmental Accounting Officers are held responsible for policy issues. Chief executives may be called to Select Committee meetings (in House Commons) to give evidence about their agencies, because they are most capable of knowing operational matters.59

This change to the tradition of ministerial responsibility might seem to be reasonable. One can possibly say that there is nothing to be afraid of making the chief executives answerable to the select committees. However the issue is not so simple. First of all, as mentioned, we have practical difficulties to identify ‘operational’ and ‘policy’ matters. Operational and policy issues are intertwined and cannot be recognized easily. Moreover, who can assure that an operational failure has not been caused by a policy failure. Secondly, the confusion as to who is responsible for failure has paved the way for the negligence of accountability. In cases of controversy, ministers declined to answer select committee and MP’s questions arguing that those issues were operational and should be answered by chief executives.60

Ironically, when some chief executives have been asked questions they have declined to reply by claiming that those issues were operational. The dismissal of Derek Lewis in 1995, Chief Executive of Prison Service, by the Home Secretary Michael Howard, highlighted how sensitive the issue was.61 The dismissal of the head of the Child Support Agency was another example with similar reasons and consequences. Thus political actors are in a stronger position to defend them: they can easily prevent attacks from the public by redirecting the critique to non-political ones.

59 TCSC Fifth Report, xx
In reality, ministerial responsibility has nothing to do with separation of functions. The tradition requires politicians to be responsible to the parliament for the actions of the executive on behalf of the public. One may say that chief executives should respond to the day-to-day issues, while politicians are responding to the policy questions. However, at the end of the day, politicians who are the people in charge of the government and the executive, should take all the blame and the praise. Since the launch of the Next Steps, governments have not spoken out on any changes in the convention. Mrs. Thatcher stated that new agencies would continue to be in the civil service and staff would continue to be civil servants and, therefore, ministerial responsibility would apply to the Next Steps agencies. In other words, if the Next Steps agency personnel are civil servants and their functions are civil service functions, there should be no change in the convention of ministerial responsibility. As Riddell says “the Government has sought to be organizationally radical but constitutionally conservative”.62 With regards to the case of the Prison Service, it can be argued that Michael Howard should have resigned to show respect to the convention of ministerial responsibility. The way of taking disciplinary actions against chief executives and agency staff is always open for proceeding.

6. Conclusions

This study has found that public administration theory and administrative approaches in special and social theory in general have certain flexibilities to cope with changing conditions and priorities in organizations and in society. By the same token, the application of agency theory to civil service reform in Britain shows that an economy-based theory could do well in administration as long as some criteria are met. The requirements and functions of management, psychological and sociological facts and theories can be mentioned in this regard. Having established a power-sharing mechanism within public administration, the Next Steps agencies reform has produced a

reasonable amount of performance related to services provided. A basic dilemma of democracy has been brought to an end: politicians and bureaucrats set up a new framework by delegating implementation responsibilities to agencies and policy-making power to politicians. The process has worked out to introduce certain principles to public administration: creation of an agency culture, empowerment of civil servants, and a compromise between appointed and elected officials. It has been possible by the elements and findings of Agency theory. The reform has created a unique cultural atmosphere, where roles of the actors in public administration have been enriched and re-evaluated. Efficiency concerns, performance related issues and new responsibilities have driven the actors to reconsider their positions. This has solved the long-standing issue of accountability and ministerial responsibility. One of the important findings of the reform is related to the position of Chief Executive Officers of agencies. Being at the middle of relations between the principal and the agency, a new level has been created by the pressure of the reform. This implicitly indicates that administrative reforms might create certain levels in bureaucracy, which were not initially imagined by the reformers. In addition, ‘freedom to manage’ approach of private sector could also be applied to the public, because it is human nature to strive for freedom as social theory explains.

Consequently, the British experience of agency reform introduces new forms of management, with a strong degree of success. Elements of the reform are not unique to the UK, but the effects afterwards have been new as the traditions and conventions of Britain contouring human and non-human factors in a special package. As a micro economic theory, the agency model has achieved this end. The solution found by the Next Steps to deal with the dichotomy between policy making and implementation functions and the tension between politicians and public servants would be valuable for developed and developing democracies as they have been struggling to sort similar problems in their territories. The theoretical and practical aspects of the British experience have the potential to provide lessons for other administrative systems, especially in Europe. Many more
countries should pay attention to learn from this unique environment.

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