ACCOUNTING FOR CHANGE

Reconciling the Demands for Accountability and Innovation in the Public Sector

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PART II

REPORT

CHAPTER I

The Issue: Accountability and Innovation

Managers in the private and public sectors have at least one thing in common: they both work with other peoples' money. The word "manager" is badly defined. Sometimes the word is used generically to describe people in a wide variety of positions whose function is to coordinate the activities of others to achieve results. But this general usage masks some important differences among different kinds of managerial positions. One key distinction is between "top level" managers and "middle managers." "Top level" managers are assumed to have ultimate accountability, wide discretionary authority, multi-functional responsibilities, and independent relations with an organization's external environment. "Middle managers," in contrast, are assumed to have responsibility to the organization, narrower authority, single-function responsibilities, and mediated relations with the organization's external environment.

In this essay, I will use the word in its most general sense, though I think it would be fair to say that, when pressed, I am thinking principally of "top level" managers in the public and private sectors. In the context of the public sector, I mean the idea of "top level" manager to include both political appointees and senior civil servants, though I recognize the important differences between the two. I am encouraged in this by the observation that, in life, everyone is a middle manager. Everyone has a boss and some subordinates. Everyone has a past and a future. Everyone has great hopes and limited capabilities. Since the concepts I develop are relevant to "middle managers" in this general sense, I feel comfortable in speaking to top and middle managers in the private sector, and to political appointees and senior civil servants in the public sector.

In the private sector, the "other people" are owners and shareholders. In the public sector, they are citizens, taxpayers, and their elected representatives.

The Demand for Accountability

Because managers act for others, they must be accountable to them. Otherwise, the "others" cannot be sure that the managers will adequately serve their interests. Without accountability, the managers might pursue inappropriate purposes, or choose unwise means. They might even steal some of the assets entrusted to them for their own benefit. The only way the "others" can be sure that managers keep to the straight and narrow path is to demand an accounting of their activities and accomplishments.

While both private and public sector managers share the burden of accountability, the concrete form differs from one sector to the other. By all accounts, accountability is far easier to establish, negotiate and operate within in the private than in the public sector.

In the private sector, managers are commonly accountable to only a small number of "principals" -- the chief executive officer and the board of directors. Moreover, these overseers are commonly united in their ultimate objectives -- to earn financial returns for the shareholders. In contrast, managers in the public sector are accountable to a tangle of overseers including political superiors, elected representatives, the media, and varied interest groups. There is no guarantee that they will agree about the organization's proper goals or objectives. Indeed, the expectation is the opposite: most often, they will contest the proper ends and means of the organizations they oversee.

Private sector accountability is also reportedly facilitated by the existence of financial measurement systems that produce reliable information about organizational performance in terms that matter to the overseers. The account given here ignores the problem of managing high-tech firms whose investments will take a long time to produce market returns. It also ignores the problem of valuing the services of important parts of private firms that do not contribute directly to bottom-line performance. Nonetheless, the account captures an important part of people's perceptions, and some of the reality, of the difference between managing and accounting for performance in the public and private sector.

Typically, private sector enterprises produce products or services sold in markets. The revenues earned provide a reasonably accurate measure of the value of the organization's products to those who purchase them. The revenues, in turn, can be added up, compared to costs, and profits calculated. Profits, viewed over time, reveal the on-going capacity of the organization to achieve the objectives of the overseers -- to earn financial returns. This information about the organization's performance and its value comes in early, regularly, and at low cost to the firm.

Measuring the performance and value created by public sector enterprises is far more difficult. Public sector overseers can measure the processes, activities and outputs of the organizations they superintend. But to go further than this -- to try to determine whether the public sector organization achieved its ultimate goals, or produced something more valuable than the costs used to support its activities -- overseers must invest in specialized evaluation efforts. These are expensive, and take a long time to produce their results. Even so, the final results are often equivocal. In these respects, then, oversight is far easier in the private sector than in the public. Yet, this does not diminish the demand for accountability in the public sector. Indeed, because suspicion of governmental power is deeply ingrained in our political culture, the demand for accountability is far sharper and more insistent in the public sector than in the private.

The media's voice is a particularly shrill one that, by all accounts, exacts a particularly oppressive and unjust toll on public sector managers.

The Tension Between Accountability and Innovation

Within the structure of accountability, managerial innovation has always posed special problems. On the one hand, to the extent that managerial innovation is important to the performance of organizations in both private and public sectors, systems of accountability should be designed to encourage and stimulate innovation.

On the other hand, strict systems of accountability that hold managers in thrall for performance on agreed-upon objectives using well tested means may serve to inhibit innovations. The reason for this tension, of course, is that innovations are inherently risky; they can fail as well as succeed. Often, the probabilities of success or failure are not well known, and the concrete paths to success are often hard to chart in advance.

The uncertainty of innovative efforts frustrates many of the common forms of accountability -- particularly in the public sector. Without prior knowledge about what results managerial efforts should achieve, or how particular new efforts can be expected to succeed, overseers cannot reliably monitor managerial work. The net result is that the overseers cannot be sure that managers are performing well or badly. If they are to encourage innovation, they must share the risk and give up some certainty and control over the managers who work for them.

Again, the private sector seems to have developed better methods for dealing with this basic dilemma. No doubt, one of the main reasons is that the institutional arrangements through which investors become entangled in sharing the risks of experimentation differ. In the private sector, investors can choose to invest in risky ventures, or to resist their allure. Moreover, once they decide to invest in a risky venture, they can limit their exposure by changing the form of their investment from equity to lending.

In the public sector, on the other hand, citizen/lenders are all forced to share the risk, and to share it in the same way. Citizens are free to express themselves in political processes as to how much and what kind of investments and risks the public sector should undertake. But the ultimate decisions are collective decisions. We cannot earmark our taxes to more or less risky ventures, nor pull out when, to our eyes at least, the evidence on performance is negative.

A second reason that the private sector is more open to innovation is that the value of experimentation is more widely recognized in the private than the public sector. Indeed, it is now commonly recognized that innovation is the key to the successful long-run performance not only of individual firms, but of the private economy as a whole. Moreover, the private sector expects innovation to come from its operating managers and executives as well as from entrepreneurs. They are expected to take the initiative and given the freedom to do so.

In contrast, to many it seems fundamentally illicit to experiment in the public sector. If executives or managers in the public sector can't be sure that an innovation will succeed, they shouldn't undertake the experiment. It is simply wrong to gamble with other peoples' money. Moreover, to the extent that innovation is important in the public sector, the common view is that it should be initiated by elected representatives rather than managers. Anything else is inconsistent with democratic political theory.

Finally, the existence of the financial performance measures described above also give the private sector an advantage in overseeing innovation as well as routine, overall performance. Because the principals can often learn relatively quickly whether a risky enterprise has succeeded or not, they can give innovators and innovations a little more rope; there is less risk that they will end up making a big mistake. This is not always true, of course. Because the public sector finds it harder to learn quickly whether a risky investment has paid off, it tends to demand more up-front assurances that an idea is a good idea. Since that, too, is hard to provide, the public sector turns out to be more risk averse than the private sector.

For all these reasons, the public sector's systems of accountability are less open to managerial innovation than the private sector's. They are, at the outset, less accepting of the need for and value of innovations. They tend to demand much more information up-front, and to rely on these up-front analyses more than on after-the-fact evaluations. They are far less tolerant of bad outcomes, and seek scapegoats more publicly and more enthusiastically than the private sector. Partly for these reasons, the public sector may also attract fewer innovators. The net result is that there is less innovation in the public sector than would be true if the systems of accountability were more similar to those in the private sector.

That, at least, is the conventional wisdom.

The CEG/KSG Conference as a Method of Investigation

The Council for Excellence in Government and the Kennedy School of Government decided to test this conventional wisdom, and to learn what successful manager/innovators did in the public and private sectors. To do so, the two institutions undertook an innovative project of their own. The CEG includes among its Principals many individuals who have held managerial positions and innovated in both the public and private sectors. Those experiences left their scars. Those scars, in turn, traced out a durable record of the differential demands for accountability between the two sectors. Similarly, the recollections of these managers could be expected to indicate what particular features of the accountability systems claimed their attention. And finally, their own resourcefulness and inventiveness in dealing with the demands for accountability could teach us how skilled managers coped with the two different systems. Thus, the cumulative professional experience of the CEG Principals represented a resource that could be tapped to learn more about the objective systems of accountability that operated in the two ostensibly different worlds, and the subjective experience that they produced.

To tap that well of professional experience, the CEG and the KSG relied on two devices. First, we produced four case studies. The focus of each case was a CEG Principal who had introduced important innovations in both the public and private sector. The cases described what the CEG Principals had done in each sector, what they thought about what they had done, and their reflections on the experiences of the two different systems. By learning from them what part of their oversight systems had captured their attention, and how they responded to the demands, we could learn what was similar and different between the two sectors. Moreover, because it was the same person innovating in both sectors, we could control for the effects of individual style and temperament in gauging the differential demands of the two sectors.

Second, using KSG faculty, we facilitated analyses and conversations of these cases with a larger group of CEG Principals who attended a conference on innovation and accountability in the public and private sectors at the Kennedy School of Government. The conference was held from May 7 to May 8. Approximately 75 CEG Principals attended, along with a small number of media representatives.

The aim was to use the cases to provoke discussions that would draw out the individual experiences and generalizations of a far larger group of CEG Principals than those we could write cases about. Thus, the observations, experiences, and practices that were described in the cases could be tested against a far broader set of experiences.

Throughout the conference, we were particularly interested in the role of the press in facilitating or frustrating innovation. This was reflected in the following facts: 1) the opening discussion which set the tone for much subsequent discussion involved a manager who found himself the focus of intense press scrutiny; 2) a press panel was an important feature of the conference design; and 3) several representatives of the press were invited to participate, and made special presentations at the end.

The reason for this focus on the press was that many managers in the public sector complained bitterly about the press, and its impact on their ability to manage and innovate. They thought the press scrutiny they faced was not only too exacting, but badly focused. The press seemed far more interested in their personal conduct or spectacular instances of organizational failure than in their intentions and plans for the organizations they led, or the organization's overall performance. Moreover, the press scrutiny in the public sector seemed far more intrusive than in the private sector; thus, a clear and important difference between systems of accountability in the public and private sectors. Because the press is such an important institution in a democratic society, and because it was widely viewed by managers as having a dysfunctional effect on their ability to manage and innovate in the public interest, it was worth giving this issue particularly close attention.

The methods we developed to investigate the nature of accountability and the hazards they create for innovation were not strong enough to establish firm conclusions about the forms of accountability in the private and public sector, the impact of the differences on levels of innovation, the salience of the different aspects of accountability to managers, or the techniques that are useful in innovating in the context of the different systems. The four cases and the discussions simply do not generate enough evidence to accomplish these objectives. Furthermore, we did not collect evidence quite systematically enough to be sure that the generalizations suggested are firm and solid. Nonetheless, the project does create an opportunity to frame the issues for more detailed analysis, and to set out some hypotheses in the form of tentative conclusions. That is the purpose of this report.

CHAPTER II
An Analytic Framework

At the outset, it is useful to establish some definitions to fix conceptions and set up the framework for analysis. Such an exercise helps to capture the varied insights that emerged from analysis of the cases we developed and the subsequent discussions with the CEG Principals. It also helps to keep the discussion focused on the particular questions related to accountability and innovation, rather than drifting into a far more general discussion of the differences between public and private sector management.

The Blurry Line Between Public and Private Sectors

One unexpected problem came up in defining what was meant by "public" and "private" sectors. As one participant explained, "I'm not sure any more what the distinction is between the public and private sector. It seems to me that there is now a continuum."

Of course, at one level, the distinction is perfectly clear. A "public" organization is one that is launched to achieve agreed-upon public goals by elected representatives, and whose operations are financed by tax revenues. Its value registers in the extent to which it achieves the goals assigned to it by the public and its representatives.

A "private" organization is one that is initiated and owned by private individuals and is financed by revenues earned by producing and selling products and services. The value of a private firm's efforts registers in the minds of those who consume its products and services, and in the returns to shareholders.

While at the theoretical extremes the distinction is clear, in the real world, the distinction is becoming blurred. There are essentially two reasons.

Public Purposes and Private Organizations. First, increasingly society seems to rely on private organizations to accomplish public purposes. For example, government now contracts with private companies not only for the development of advanced weapons systems, but also for policy advice, picking up the garbage and even for the imprisonment of offenders. Similarly, government increasingly regulates private firms to ensure that they contribute their fair share to public purposes such as protecting the environment, guarding against industrial accidents, or ensuring equality of employment opportunity.

More subtle, but potentially as significant, is the fact that profit-seeking private enterprises are now sometimes held informally accountable for meeting public obligations. Increasingly, they are supposed to be "good employers" and "good neighbors," as well as to make profits for their shareholders. A CEG Principal, reflecting on the accountability he felt as a private-sector executive, clearly revealed the force of these claims, saying:

> We're continuously making judgments that reflect the claims of competing interest groups on our bottom line. We're making judgments about how much to invest in the quality we deliver to our clients. Of course, we can squeeze the quality tighter and show a better short-term bottom line. But we often judge that that would not be good for us over the long run.... Of course, you can't lose money. But there are degrees of pricing aggressiveness, and decisions about investments, and the claims of different groups that also go into your strategic calculations.

Indeed, the emergence of public accountability for private organizations drew lots of comments and discussion in the CEG/KSG Conference. It was stimulated chiefly by an anomaly that appeared in the Len Schaeffer case.

In the public sector, Schaeffer, as the Commissioner of the Health Care and Finance Agency (HCFA), had been charged by Secretary of Health, Education and Welfare Joseph Califano with the responsibility for combining the Medicare and Medicaid programs in a single, coherent organization, that could save money through streamlined administration, and eventually emerge as a purchaser of medical services powerful enough to use its combined purchasing power to shape the delivery of health care services throughout the country. In the private sector, as the President of California Blue Cross/Blue Shield, Schaeffer faced a similar challenge -- to restore the agency to financial viability by consolidating Blue Cross of Southern California with Blue Cross of Northern California, eliminating many jobs, and shifting the organization from one that simply "paid bills" to one that supplied "managed care."

The surprising anomaly to the CEG Principals was that, as he made the necessary organizational changes, Schaeffer seemed to face sharper and more demanding public accountability in the private sector than in the public. Specifically, the press savaged his efforts to cut jobs at Blue Cross of California. The resulting unemployment, concentrated disproportionately on minority employees, made him a target of press attention. This, in turn, forced him to manage the firings with a carefully designed press strategy. In the public sector, he faced much less scrutiny for equally dramatic organizational changes affecting a great many economic interests. As one CEG Principal observed:

> The interesting difference is that (in the public sector) he made this dramatic organizational change and didn't get pilloried in the press. He moved jobs out of Washington, D.C. to suburban Baltimore. He did the same thing in the private sector eight years later where you might expect less focus, and he got pilloried and called a racist. Yet, the Washington case was as open to criticism as the California case.

This comment was seconded immediately by another Principal who summarized: "He seems to have operated more in the public view in the private sector than in the public sector."

These trends, increasing the formal and informal accountability of private profit-making firms to the public for the achievement of public purposes, produce convergence in both the objective form and subjective experience of accountability in the public and private sectors. As private sector companies are drawn into public purposes, their accountability widens to include government agencies, public interest advocates, and local communities. The experience of managing in this world becomes more like managing in the public sector.

Public Agencies as Private Companies. Second, in pursuit of greater efficiency and responsiveness from public sector bureaucracies, society has increasingly constructed public bureaucracies on principles drawn from private sector management. By setting up authorities and independent regulatory agencies, legislatures have sought to insulate public agencies from the pernicious influence of politics.

By "deregulating" public sector management practices, and reorienting agencies to a "customer focus," overseers and managers in the public sector have sought to increase the accountability of public sector managers to the organization's clients rather than to its pre-existing procedures.

One participant in the conference thought he saw a trend in trying to get more of the public's business conducted through public bureaucracies that were set up to operate like businesses:

> An interesting question is whether we are moving increasingly toward a mode of government in which we agree that we have to create these entities which are immune over substantial periods of time from political control as long as they work within certain bounds of discretion. This often allows the agencies to pay competitive salaries, build up continuity of personnel, and develop business-like ways of thinking.

A second participant enthusiastically and immediately agreed:

> That's absolutely the case. Most of you probably don't remember the Synthetic Fuels Corporation. (Laughter) Not a great success story admittedly, but that was a very interesting venture. The

argument at the time was that you could not trust the political process to make these kinds of decisions, and therefore would have to create something independent. Many agency budgets are really just a grab bag of special interests. The Department of Energy is a very big case in point.

Whether there is a trend toward doing more of the public's business through special kinds of government agencies that operate with some degree of independence from political policy-making and oversight processes or "nonprofit" private enterprises that voluntarily assume public responsibilities is hard to tell from the data we collected. It might be significant, however, that of the four cases we wrote, involving eight different organizations, five of the organizations could be considered one of these hybrid types: HCFA, Blue-Cross/Blue-Shield, Fannie Mae, DARPA, and MCC, either because they are public organizations that rely heavily on private organizations to achieve their objectives, or because they are private organizations that have important public objectives, or the government as an important client.)

As a CEG discussant observed, "Most of the 'private' organizations that we're looking at -- whether it's the technology consortium or Blue Cross of California, or Fannie Mae -- are really quasi-public corporations." This observation could be nothing more than an accidental result of the cases we selected. Or, it could be the systematic result of the kinds of people who become CEG Principals. Nonetheless, it seems clear that such organizations exist in the public sector, and that they show up in the careers of those who want to manage in both private and public sectors.

Managers and Managers

Our discussions (and subsequent reflections) also indicated that care was also required in defining the concept of "manager." At an abstract level, the idea of a manager is pretty clear: someone who occupies an institutional position that gives him or her direct responsibility for delivering operational results by deploying assets entrusted to him or her for that purpose.

To a degree, a useful conversation about management and accountability can be held at this level of abstraction. But to carry on a serious discussion of accountability and innovation in the public and private sectors, it soon becomes necessary to move to a more concrete characterization of the managerial positions one wants to discuss. Once at a more concrete level, one must recognize and accommodate the wide heterogeneity of managerial jobs that exists not only between public and private, but also within each of these sectors.

In the public sector, for example, it is important to distinguish "chief elected executives" (such as Presidents, Governors and Mayors), from "political appointees" at the cabinet and subcabinet levels, and from "senior civil servants." Such distinctions reflect not only different levels in a bureaucratic hierarchy, but also the proximity of a manager's connection to the legitimizing power of popular elections. Both features, in turn, are related to the amount of initiative and discretion a manager in the public sector is allowed to have, and to whom he or she is accountable.

In the private sector, it is important to distinguish "chief executive officers," from "middle managers with discrete profit/loss responsibilities," and from "middle managers without strategic responsibilities." As above, these distinctions reflect one's position in a bureaucratic hierarchy. But they also reflect the degree of exposure the managers have to the external market environment, and the kind of initiative and responsibility they are expected to take with respect to that environment.

For the most part, our discussions implicitly assumed that we were talking about managers who sat at, or very close to, the top of bureaucratic hierarchies in both the public and private sector. That focus was natural, for it was these positions that seemed to afford the greatest opportunities for innovations. In the public sector, the focus was on cabinet or subcabinet appointed officials -- perhaps those senior civil servants or staff members who were entrusted with important initiatives taken by officials at those levels. In the private sector, the focus was on CEO's, or managers with significant profit/loss responsibility.

Managerial positions implicitly excluded from the discussions were mid-level managerial positions whose discretion was tightly bound within bureaucratic mechanisms of accountability. These positions were excluded because they seemed to offer less scope for leading and innovating. By implicitly excluding such managers, however, we may have exaggerated the differences between the public and private sector. After all, most managers are middle managers, and the middle management positions may be the most similar across the sectors. In such positions, most of the manager's accountability is to the organization's internal control systems rather than to the external environment. And, to the extent that those systems of accountability are very tight, everyone is forced to operate and feel like a bureaucrat.

By excluding such positions, we may also have excluded some positions in which innovation can or should occur. After all, one of the most important challenges facing managers in both public and private agencies today is to find ways to authorize and stimulate innovations at all levels of an organization -- not just at the top, or off to the side in staff positions. That is the important idea that lies behind the concept of total quality management, and the development of quality circles. To the extent that managers succeed in building organizations that are innovative throughout, the distinctions between top-level strategic managers, and mid-level operating managers may disappear.

So managers occupy many different kinds of positions. The positions are determined by the particular institutional structures developed in the public and private sectors that distribute slightly different rights and responsibilities across the different positions. In some positions, relatively broad scope is created for innovation. In others, the scope is much narrower. These differences influence not only how much and what kinds of innovation will be forthcoming from different managerial positions, but also how hard, and in what particular ways, managers in the different positions will have to work to create room for undertaking the innovations.

Accountability Relationships

Accountability, too, is both a simple abstract idea and a complex, concrete experience. At the abstract level, accountability can be represented as a moral and legal relationship between a "principal" (who owns or has some other legal and moral right to control the use of a particular asset), and an "agent" (to whom the "principal" delegates the detailed decisions about how best to use the "principal's" assets). The moral and legal structure of the relationship obliges the "agent" to use his delegated authority as efficiently and effectively as possible on behalf of achieving the "principal's" goals and objectives.

Two Kinds of Relationships: Principals and Stakeholders. Note that an important feature of an accountability relationship is that the aims of some (the "principals") are established as preeminent while the aims of others are treated as subordinate. Thus, "agents" are accountable to "principals," but not ordinarily the other way around.

An accountability relationship differs, then, from what is commonly called a "stakeholder" relationship. A "stakeholder" is anyone who has an interest in what a manager does with his borrowed resources. It includes, for example, not only the owners, overseers and custodians of an enterprise, but also its lenders, suppliers, customers, clients and employees. Of course, a manager may in some loose sense be "accountable" to all the "stakeholders." For example, it may be prudent for the manager to understand and accommodate the interests of the stakeholders in defining purposes and organizing activities. More controversially, the manager may have some moral and legal responsibilities towards other stakeholders such as employees, clients, or surrounding communities.

Strictly speaking, however, managers are commonly accountable only to a subset of the stakeholders: those whose moral and legal right to determine the future direction of the enterprise is preëminent. To whom

such pre- eminence should be accorded is often an important managerial question.

Indeed, this question about to whom a manager was accountable drew a great deal of attention in the CEG/KSG meeting. Some particularly thorny issues arose in the public sector context including:

- Whether one was accountable only to one's immediate political superiors, or in addition to others in the executive or legislative branch who also took an interest in an organization's performance;
- Whether and in what ways one was accountable to the press and the media; and
- Whether and in what ways one was accountable to the people who worked for the organization, and their views of what it was proper for the organization to do.

The cases developed for the conference afforded significant opportunities for differences on these matters to arise and be aired. In the DARPA case, for example, Craig Fields described the development of an "adequate consensus" about one's purposes as an important task of public sector management. Clearly he meant to include congressional committees opposed to administration policies in this definition, as well as other expert opinion about potentially valuable new directions for public sector enterprises. Yet, he paid a price for his openness to the concerns of these others; he was fired from his position for seeming to give too much support to the idea of using DARPA to support the development of an "industrial policy" -- an idea that the administration for which he worked adamantly opposed and sought to weaken.

Similarly, the Len Schaeffer case drew a great deal of discussion about what managers owed to employees of organizations they led. In both the public and private sectors, Schaeffer relied on a radical reorganization to achieve his strategic purposes. In the private sector, the radical change was accompanied by sizable layoffs. The questions raised focused on the extent to which a less wholesale and brutal approach would have been more appropriate. At issue was the tension between the manager's accountability to his principals for performance on the one hand, and his responsibility for treating employees fairly on the other. Schaeffer's case was contrasted with Paul O'Neill's approach at ALCOA in which an apparently far greater effort was made to engage the employees in designing and managing the process of change.

Finally, the Greg Coler case, prepared for other purposes and discussed in plenary session at the beginning of the conference, made it clear that press coverage of public sector managers was an important de facto part of the public sector's system of accountability, in the sense that it seemed to mobilize the formal systems of accountability, and inevitably grabbed the attention of public sector managers. But it also raised the question about whether press coverage properly focused accountability, and therefore made a moral as well as prudential claim on public sector managers; or whether the coverage was so misdirected that a manager's duty lay in resisting rather than facilitating its claims.

Terms of Accountability. Within the basic structure of accountability, many different concrete forms of accountability can be established. One can capture the important differences by looking at how the terms of accountability differ. One key feature of the terms of accountability are the substantive values, goals or objectives that are to guide the manager's actions. (These can be defined in more or less concrete and specific terms.) A second key feature is how performance with respect to the defined objectives will be measured. (The measurements can be made on processes, outputs, or outcomes.) A third concerns the frequency and detail of reports that are filed. (A manager can be monitored very closely, or only occasionally.) A fourth concerns the extent to which the reports will be questioned and audited. (The manager's reports can be trusted or treated skeptically.) A fifth concerns the methods available for renegotiating the existing terms of accountability. (There can be continuous, ongoing discussion between the overseers and the managers, or the communication can be rare and ritualized.) And so on.

The variety of terms is important because the concrete form of accountability can have important implications for the ways that "principals" and "agents" behave, and for the overall performance of the system. In some trusting relationships, managers will be left largely alone to give their full attention to the achievement of the principals' purposes with little controversy or distraction. In other suspicious relationships, a great deal of the energy of both principals and agents will be eaten up by debates over the accuracy of reports, or the propriety and wisdom of alternative courses of action.

Evaluating Systems of Accountability. The value of a particular system of accountability, then, can best be judged by the extent to which it: 1) embodies a proper ordering of stakeholder interests in guiding the goals and methods of an enterprise; 2) provides both appropriate reassurance to principals and affords them appropriate opportunities to intervene to protect their interests; 3) motivates appropriate behavior from the agents, including providing opportunities for the agent to take the initiative in recommending changes in the terms of accountability; and 4) does all this at the lowest possible cost in terms of resources claimed, initiative blunted, and controversies ignited.

The task of those who set up systems of accountability, then, is to construct them in such a way that the interests of the principals can best be served. The task of those who operate within systems of accountability is not only to live up to their demands, but also to shape them in ways that are best designed to serve the principals' interests.

Defining Innovation

Innovation also turned out to be a somewhat slippery concept. The cases were focused on particular innovations in the public and private sector, but it was no easy matter to describe what the innovation in the cases were. Moreover, it was not really clear that the idea of innovation should be limited to one particular innovation that was introduced. To many CEG Principals, what was important about the idea of innovation was not that a particular innovation was developed, adopted, and implemented in a particular organization, but instead that some capacity for continuous innovation was established in an organization.

In the Len Schaeffer case, the public sector innovation was the administrative consolidation of the Medicare and Medicaid programs into a single coherent organization -- the Health Care Financing Administration. The goal of the consolidation was not only to produce some administrative economies of scale in operating the huge benefit systems, but also to create an organization that could become a very powerful buyer in the health care sector of the United States, and use that leverage to force cost reductions and technology improvements. The private sector innovation was to consolidate two different Blue Cross/Blue Shield organizations into a single organization, reduce overhead costs, and then reemerge as an organization providing "managed-care products" to different market segments rather than simply pay fees for service to Blue Cross/Blue Shield subscribers.

In the Larry Dale case, there is one small public sector innovation involving the development of "partially assisted housing" in Maryland early in Dale's career, and a far larger and more significant innovation that draws Fannie Mae into the co-insurance market for multi-family housing, and allows Fannie Mae to outcompete HUD for this market. Key to that second innovation was seeing that the real risk taken by the co-insurers was not the underwriting risk of properly estimating what projects would be economically viable and which not, but instead the lender risk of relying too heavily on a small number of co-lending firms, and then adapting the program to reduce the chance of co-lender failure.

In the Paul O'Neill case, the innovation in both public and private sectors turned out to be the development of analytic frameworks that challenge managers at the top and middle of organizations to keep thinking about what they are trying to produce, and what might be more effective means of achieving the results they are trying to achieve. The challenge in both cases is not only the technical challenge of inventing these frameworks, but the managerial challenge of giving them force and vitality in the policy-making and operational life of the organizations whose activities they are supposed to influence.

In the Craig Fields case, there are many particular innovations mentioned. For example, a key DARPA project, closely related to the organization's interest in pursuing "dual use technologies" that can be used in defense and civilian applications, is one focused on the development of high density television. A key project in MCC, Fields' private sector enterprise, is the concept of "enterprise integration," which uses information systems to speed up customized manufacturing and delivery and reduces the need for inventories. These projects are seen not only as important in themselves, but also as key products designed to reposition the organizations Fields leads in their environments -- as the leading edge of strategic changes. But what is in many ways most innovative about the organizations that Fields leads in both the public and private sectors is that they are organizations whose entire mission is to be innovative. This requires important innovations in the structure of the organization, and in the ways in which the organizations may best be held accountable.

The variety of innovations in the cases challenges any simple prior notion of what defined an organization. It also threatens to overwhelm any simple classification scheme. Nonetheless, it seems useful to offer both a general definition of innovation, as well as to recognize some particular types of innovation that might occur. For our purposes, an innovation was nothing more than an important change in the way that a public or private sector defined its purposes, or carried out its business. It did not have to be an entirely new idea. Nor did it have to involve every aspect of an organization's effort. It just had to be some kind of change introduced by a manager.

Obviously, this is a very broad definition. It doubtless includes many initiatives that serious students of innovation would reject as unworthy of the name. Moreover, there is a price to be paid for being so undiscriminating. By accepting any change as an important innovation, attention is diverted from important questions about what sorts of innovative ideas are particularly valuable, and what sorts of conditions encourage people to become particularly creative. Nonetheless, the broad definition has two advantages. First, it focuses attention on something that is a necessary if not sufficient condition for truly innovating; namely, the process of leading change. Second, it includes experiences that a great many managers have had in trying to improve the performance of their organizations.

Within this broad definition of innovation, it may be particularly important to distinguish several different types. One type could be called a "program" innovation in the public sector, and a "product" innovation in the private sector. These are changes in a portion of an organization's activities -- something new that is added to the organization's ongoing set of activities, products, or services.

A second type we could call an "administrative" innovation in both the public and private sector. These are changes in the ways in which organizations are structured, measured, staffed, or otherwise equipped to do their work.

A third type we could call a "strategic" innovation in both public and private sectors. These refer to changes in the overall position of an organization in its environment. They often involve a redefinition of purpose, product, or market, as well as important changes in operational programs or technologies or administrative arrangements. They are meant to make claims on all aspects of an organization's performance.

There are relationships among these different types of innovations, of course. By definition, strategic innovations often imply a significant number of program or product innovations and administrative organizations. It is also behaviorally true that many things that start out as programmatic or administrative innovations may become, either intentionally or unintentionally, strategic innovations. Nonetheless, one can still distinguish among these types.

It might also be useful to distinguish between any particular innovation (whether program, administrative, or strategic) on the one hand, and the creation of innovative organizations on the other. Sometimes an important strategic innovation for an organization is for it to adapt its administrative systems to allow it to become a more innovative organization in general. Other times, it is simply important for an organization to make a one-time change to a new market position, and then refine its methods for operating in that particular environment.

Using this classification scheme, one can revisit the innovations that turned up in our cases and make some useful distinctions. Schaeffer's public sector innovation (the consolidation of Medicare and Medicaid in HCFA) could be classified as an administrative reorganization designed to achieve a strategic objective. His private sector innovation could be classified as an administrative reorganization designed to achieve a strategic repositioning of the organization, and to spawn new product innovations. Dale's work on partially assisted housing in the public sector and multi-family housing in Fannie Mae could be viewed as program and product innovations respectively. O'Neill's innovations (the analytic frameworks) could be viewed as administrative innovations designed to stimulate improved productivity in the businesses he was in. Fields' innovations are strategic innovations in the principal foci of organizations that have been explicitly designed to be continually innovative.

Management, Innovation, and Leadership

A theme that ran through the discussions at the conference was the relationship between management, innovation, and leadership. Often, the line between management and innovation seemed to blur, since it seemed that part of what good managers did was to introduce innovations into their organizations, or facilitate their development. The line became particularly blurry once one accepted a broad definition of innovation. As one participant observed, "Any good management is about innovation. Managers have only two essential tasks. One is to keep things going that their organizations are already doing well. The other is to change the things the organizations are doing so that they're doing them better."

Similarly, the line between innovation and leadership also seemed to blur, since it seemed clear to everyone that introducing innovations or facilitating their development required a kind of leadership. One had to put oneself forward -- either in claiming the virtue of a particular untested idea, or in creating a space within which others in one's own organization could be innovative. In these acts -- suggesting an idea to be implemented or a problem to be solved -- lay the challenges and hazards of leadership.

If innovation is an important task of management, and if innovation seems to require leadership, then it follows that management requires some kinds of leadership. That is a natural enough conclusion, but it seemed that there were many in the group who still wanted to distinguish management from leadership. In their view, at least some part of management was concerned with maintaining the status quo, as well as introducing change; and another part of management was simply executing changes that had been suggested by superiors. These parts of management did not necessarily require the manager to be an innovator or leader. One participant explained, "I would couple innovation with leadership and risk-taking. These are, I think, quite different from routine management."

Another saw the difference in terms of the techniques they used to make something happen in the world:

> Good managers are people who change the physical reality of how things happen in order to achieve a desired result. That's what a manager does. He's not an analyst. He's not a thinker... Managers either tell people what to do or they write procedures. They're very close to what happens...Leaders are people who inspire others to act, usually without giving direct orders. And they usually inspire people by their ideas, by what they say and how they say it, and what they write and how they write.

Key to the special techniques important to organizational leaders was their ability to foster and encourage leadership from below as well as

to give inspirational direction from above. One CEG Principal described a key technique as "guided autonomy." The notion was that top-level managers sketched purposes and aims, and left it to subordinates to fill in the detail with concrete proposals and actions about which they got feedback from the top level managers. The same Principal argued that it was this kind of leadership that was particularly important in creating innovative organizations rather than simply introducing important new innovations into their organizations. Whether this was part of management or leadership remained a little obscure.

Of course, one need not decide what portion of a manager's job requires innovation and leadership to observe that whenever it does require these things, the three become blurred. And, since our conference was focused on managers who innovated, and the problems they faced in introducing or facilitating or implementing their innovations, it was not surprising that these things became confused in our minds.

What seems substantively important, however, is the idea that innovation is often an important part of successful management, and that introducing or stimulating innovations does seem to require some of the temperaments and skills we associate with leaders. This is particularly true if the kind of innovation that someone is introducing is a basic change in mission of an organization, or an effort to create an innovative organization.

The reason, no doubt, is that in making any change, and particularly in making large and risky changes, someone typically has to stick their neck out, and in doing so, cast themselves as a leader as well as manager. They can't hide, because everyone both inside and outside the organization wants to know who is the author or initiator of the change. They may also want to know by what authority he or she makes the change. But the interesting fact is that no matter what the answer to that question, no matter how much the manager can shift the responsibility for the change to some higher authority, the overwhelming tendency among those who are asked to make the change will be to attribute the change to the one who is making it happen.

A Managerial Point of View

These ideas help define the framework for our inquiry into accountability and innovation in the public and private sectors, but they do not quite describe the point of view we will adopt in carrying out the analysis. Throughout, our approach will be to look at the issues of accountability and innovation from a particular vantage point: the perspective of a value-creating manager -- one who wants both to be accountable and to perform well; who is motivated to innovate when necessary or appropriate; and who defines success in terms of building adaptive organizations. The questions will be what forms of accountability such managers would be likely to encounter in the public and private sectors, and what they could do to introduce or facilitate necessary innovations in the face of those systems of accountability.

This perspective differs from another common perspective, the one adopted by a systems analyst or institutional designer who wants to understand the properties of broad institutional arrangements that have been established. The interesting questions from that vantage point include such issues as whether there is too much or too little innovation in the public sector, and what particular features of accountability in the public sector seem to determine these results. Only in the last section of the report will we shift our perspective to an evaluation of the different systems of accountability in the public and private sectors.

The reasons for adopting the managerial rather than institutional perspective are essentially two. First, our methods of interviewing managers about what they see and do is better suited to answering questions about managerial perspective and technique than questions about system performance. Second, the audience we are interested in addressing are the managers rather than the systems designers. Indeed, although we recognize the Founding Fathers as important systems designers, we cannot quite figure out who their contemporary peers are. Therefore, much of what can now be done to improve performance in the public sector lies with improving the practices of managers rather than altering the shape of public sector institutions. In any case, that is what now animates our interest.

Chapter III

Accountability in Private and Public Sectors

Initially, the managers who participated in the CEG/KSG conference judged the structures of accountability to be quite different in the public and private sectors, and to differ along the conventional lines. They thought that public sector managers were accountable to many more people than private sector managers. They felt much more publicly exposed in the public sector than in the private. They thought the substantive terms of accountability encoded in mandates for managerial action were less coherent and less stable in the public sector than in the private. They thought it was much harder for public sector managers to measure performance, and therefore more difficult to recognize when change was necessary, and more difficult to persuade others of the need for change.

The more they discussed the issue, however, the more it seemed that the differences were of degree rather than kind. Consider the following exchange that occurred within one of the discussion groups:

> *Participant*: The question that keeps coming up is how different is accountability in the private and public sector.
>
> *Participant*: In the public sector, you're accountable to the public and the constituency that oversees your program.
>
> *Participant*: You know, most organizations have the same type of constituency. You don't have a Congress. But you do have stockholders. You do have a board of directors (usually composed of external as well as internal people).....
>
> *Participant*: Remember that when we stopped yesterday, we had a list of the chain of accountability for Schaeffer at HEW. It included Califano, the President, OMB... And we were talking about whether we were accountable to the press. I think the consensus was that you really weren't accountable to the press, but the press acted as auditors. They're there to investigate on behalf of the public (also on behalf of selling more newspapers!). If you do another list of what that chain of accountability looks like in the private sector, I think you've got stockholders, Board of Directors, employees, organized interest groups, and customers. I think the difference between the two lists is that there are a lot more levels and players involved in the government accountability. And I think that makes it more difficult. But it's not dramatically different. I mean, it's the same set of issues you gotta deal with. Increasingly on the private sector side, you've got to deal with the press. They were just all over

us at Blue Cross, and I think they're all over other companies when they smell something.

Participant: Thinking about my own company, we're also involved with regulators at the federal and state levels. We're also involved with legislators at both levels because there are continually bills in Congress or in the states that directly affect our business.

Participant: You know, you could add to that list, too. I think the claim that there are fewer people in the private sector, and fewer entities to answer to, is simply wrong. In my company, I'm a president. But because I'm one of 13 wholly owned subsidiaries, I also answer to a group president, and the chairman. We could also throw in the investment community whose views are extremely relevant.

Participant: Let me try to restate my point. If you simply add up the number of people you have to satisfy, what you find is in the private sector there are more people you have to satisfy. I mean you're right: it's about the same in the two sectors.

Participant: The suggestion, then, is that there's been a convergence over time in the way that the different sectors feel from the perspective of accountability.

This is an intriguing exchange, but let's look at the evidence on these points a little more closely.

To Whom Accountable?

With respect to the number of people to whom managers are accountable, the cases revealed that sometimes public sector managers were accountable to relatively few people, and that private sector managers were sometimes accountable to a great many. Len Schaeffer, for example, said that in the public sector he only really had to please two people: Joe Califano and Hale Champion, his immediate superiors in HEW. In contrast, in the private sector, he had to carry an entire Board of Directors, and found himself vulnerable to public attacks on his policies from those who were concerned that he would reduce employment in the State of California, further disadvantage minorities, and reduce health benefits to needy populations.

Similarly, Craig Fields said he noticed no important change when he moved from DARPA to MCC. In both positions he was held accountable by many different principals for many different things. At DARPA, some had wanted a rigorous focus on the development of military technology, while others thought that dual use technologies represented particularly valuable DARPA products. At MCC, different investors wanted him to concentrate the organization on different products that were particularly valuable to them. In both cases, he found it necessary to search for an "adequate consensus" rather than complete agreement about what he was supposed to do.

The experience of the case protagonists, particularly their experience with multiple principals in the private sector, was echoed by discussants in the small groups. One participant declared:

> I run a trade group. I am accountable to the press, the trade press, a board of directors, and a membership of 200 banks. To change and innovate in my job is as difficult as it is in government. In some ways, it is more difficult.

To some degree, the discovery that structures of accountability were quite complex in the private sector as well as the public could be an artifact of the changing positions of the CEG Principals. Most of them started their careers in the public sector, and their experience of public sector accountability was therefore as mid-level to upper-level managers who were relatively insulated from the full ravages of political accountability. In contrast, in the private sector, they had emerged as chief executive officers and therefore faced accountability without any protection by superiors. Therefore, they may have seen less difference between the two sectors than they would have if their experience had been as CEO's in both sectors.

Moreover, it may be that the kinds of private sector agencies the CEG Principals seek out are the kinds that operate in the public eye to a far greater degree than most private sector firms, and that, too, may lead to exaggerated similarities in the basic structures of accountability in the two sectors. Nonetheless, the fact remains that, in the cases, and in the discussions, there seemed to be less difference between the two sectors in the number of people to whom managers were accountable than was initially assumed. The primary reason seemed to be that private sector managers were accountable to more people than was once assumed.

How Vulnerable to Exposure?

The view that managers were much more publicly exposed in the public than in the private sector held up a little better to reflective scrutiny. But that, too, eventually seemed to be more a matter of degree, with a high degree of overlap between the two sectors rather than a sharp difference in kind.

The Greg Coler case, coming first in the program, tended to emphasize the degree to which a public sector executive could become publicly exposed. In that case, Coler's personal conduct with respect to what hotels he stayed in, and what friends he had, became as important as the efficiency with which he ran his organization. To many, that fact symbolized what was wrong with public sector accountability, and particularly what was wrong with the press' role in holding managers accountable. The focus was both too intense, and on the wrong issues. Some press representatives attending the conference as participants as much as admitted this point:

> The press is attracted to situations where there's something wrong about the picture. The challenge is to put that before the public. What was wrong in the picture in Mr. Coler's case was that he was a flashy, arrogant guy who didn't act like a bureaucrat was supposed to act.

There were many in the group, however, who were much less sympathetic towards Coler. In their view, one simply had to accept the fact that the public expected public sector managers to be modest and retiring rather than bold and flamboyant, and to mold one's style and conduct accordingly. They did not view this demand as an inappropriate or unreasonable price to pay for working in the public sector. It was simply unprofessional to court trouble one did not have to face.

Similarly, in discussing the risks of innovating in the public and private sector, one group focused intensively on how different it felt to fail publicly as one did in the public sector, compared with failing more privately in the private sector. One participant observed, "The exposure problem may be worse in the public sector. You may be more pilloried in public for failure there than in the private sector." And everyone in that group at least seemed to agree that there was something worse about failing in public.

To the extent that public sector managers had to manage "in a fishbowl," then, the public sector's system of accountability seemed more demanding than the private sector's. Yet, as noted above, the Schaeffer case presented an anomaly. He was much more publicly vulnerable as a private sector executive than as a public sector executive, and faced much closer press scrutiny.

As in the case of the number of people to whom one is accountable, the unexpected overlap between public and private sectors in the level of public exposure could be the result of different positions, or the kinds of private organizations that CEG Principals join. But it also may be that the media's enthusiasm for investigative journalism has generally increased

the exposure of high level officials, and spread it from the public to the private sector.

The CEG Principals acknowledged that the presence of the press made them feel much more vulnerable. But they agreed with the press representatives that they were not, strictly speaking, accountable to the press. One observed, "You're not really accountable to the press. But the press are sort of auditors. They're there to investigate on behalf of the public. (Also on behalf of selling more newspapers!)."

They were also dismayed by the press' apparent focus on isolated incidents of their organization's activities, while missing the big picture of what the organization was actually producing overall. Len Schaeffer spoke for many frustrated managers when he commented:

> We had incredible press coverage (at HCFA) when we stopped paying for heart transplants...We had incredible press when we didn't come forward fast enough to save the Brooklyn Jewish Hospital... There was always stuff like that going on. But it was the smoke stuff. It was not about the fundamental integrity or performance of the agency. That came out in detail in administrative reports. These were given to people on the Hill so that they would know what was going on. But the press never covered them.

In sum, then, the managers felt relatively exposed in both sectors, but they experienced the press coverage in the public sector as very distracting because it was intense, and often seemed to be focused on the wrong issues. It also threatened to create new controversies and draw new players into the game. This made the task of negotiating reasonable and appropriate terms of accountability far more difficult in the public sector. It also made their failures much more public and upsetting.

For What Accountable?

Knowing to whom one is accountable is one thing, but that is not quite the same as knowing for what one is accountable. There is a relationship between these, of course. It is only by listening to the expectations and demands, both explicit and implicit, of the principals to whom one is accountable that one can learn what substantively one is accountable for. The difficulty, however, is that the more people one is accountable to, the greater the potential for conflict among their demands. And the more incoherent their demands, the greater the difficulty in producing what is expected. For these reasons, it is important to analyze the coherence of the substantive terms of accountability in public and private sectors.

The Conventional View. The entering presumption is that, on average, there is greater coherence in the demands of private sector than of public sector overseers. True, managers in the private sector must manage the tension between keeping costs low and the quality of goods and services high. But that tension somehow seems more familiar and easier to resolve than the confusion that seems to mark public sector mandates such as to house the poor, but to do so without financial risk, and ensure racial integration along the way.

For the most part, the cases prepared for the CEG/KSG Conference do suggest that managers in the private sector benefit from relatively clear, stable, and coherent mandates. Schaeffer is instructed to return Blue Cross of California to financial viability, and all his efforts can be focused on this objective. Dale is told by David Maxwell to "fix and expand" Fannie Mae's multi-family housing program. These mandates stay in place for the several years it takes to achieve the results. In contrast, the mandates in the public sector seem more confused and fickle. In the Dale case, it is reported that the mandate for HUD to establish a co-insurance program for multi-family houses lay unimplemented until the Reagan administration spotted the opportunity to develop effective public-private partnerships in this important market. Then, as one CEG Principal reports:

> HUD did not place very stringent demands on private lenders in the multi-family program. They imposed very small net worth requirements and produced very little monitoring. The reason was that the HUD officials lived in a very intense political environment. Those private lenders, encouraged by the administration, were in there every day banging on the assistant secretary and telling him how to write the rules for their benefit. I know. I was there. And the pressure paid off. The result of this effective lobbying was to establish a goal for HUD's multi-family program other than simply increasing multi-family housing construction at low cost to the government: it became responsible for guaranteeing a financial return, and reducing the risk to its private sector partners.

Similarly, Craig Fields' plans for repositioning DARPA in the post-Cold-War era by focusing on "dual use" technologies, and using these projects to help America become internationally competitive runs afoul of a bitter partisan political struggle over "industrial policy," and continued uncertainty about whether "dual use" technologies should be considered a particularly valuable or barely tolerable part of DARPA's mandate. By championing "dual use" technologies and "industrial policy," Fields suddenly found himself in public opposition to his political superiors in DOD and the White House, inadequately protected by supporters in Congress, and without any means for resolving the hot policy debate in which he found himself.

An Alternative View. Yet, the cases and discussion offered evidence for the alternative hypotheses as well -- namely, that mandates in the private sector are often confused and transient, and that those in the public sector are quite coherent and stable. For example, Paul O'Neill's mandate in ALCOA is by no means clear. The board obviously expected him to make his financial numbers in both the short and long run, but they gave him little instruction about how he should achieve these goals.

In the actual case, he shifted the basic strategy of the company. O'Neill's predecessor had committed ALCOA to a strategy of diversification, judging that aluminum was a "mature" industry from which little additional profit could be wrung. O'Neill made quite a different judgment. He thought that by refocusing the company's attention on aluminum production, ALCOA could set international standards for cost-effective aluminum production, and wring substantial profits out of what seemed to be a "mature" industry. As part of that strategy, he also committed the company to an ambitious effort to enhance safety in the workplace, despite the fact that ALCOA already enjoyed a comparatively favorable safety record. There are important value choices in these strategic decisions, which, at the outset at least, are not obviously coherent.

Similarly, Craig Fields' mandate at MCC is by no means clear and coherent. Here, again, he is expected to earn financial returns -- a task he confesses he finds more difficult than spending money. But exactly what path should be taken to successful financial performance remains unclear. He must satisfy the many different financial contributors to his organization, and trusts that "enterprise integration" will be the product that delivers satisfaction and financial returns.

And, our cases have at least one example of a fairly coherent and stable mandate in the public sector. Schaeffer is expected to integrate Medicaid and Medicare programs organizationally to achieve administrative economies of scale, and turn them into a potentially powerful purchaser of medical care that can use its market leverage to force important reforms in the delivery of health care in the United States. So, there is evidence for both sides of the proposition.

The Value of Politics. The discussion of the cases with the CEG Principals also turned up some unexpected support for the political process that produces mandates for public sector managers even though it often produces mandates that seem vague, incoherent, and fickle. Indeed, one CEG Principal in discussion offered a spirited defense of "politics" in shaping public sector mandates:

> HUD is a profoundly political organization. But it ought to be a profoundly political organization because much of what it deals with are profound political questions. When you're asking who should house poor minorities, and where they should be put -- those are political questions and ought to be discussed. This is political in a good sense. We've been using interchangeably phrases like "political environment," and "political pressure" when sometimes we mean politics in the good sense and sometimes we mean cronyism in the worst sense. I think part of our problem in the HUD conversation was that we didn't separate the two. Any solution that says that the way to promote innovation is to hide out from the legitimate politics of the country, I think that is just: a) unacceptable; and b) scary.

Another CEG Principal observed that frequent political changes were one of the few things that motivated public-sector innovations:

> There is a market out there. You just measure it differently. The American people go to the polls every two years and vote for their Congressmen. They don't think the business called the running of America is working well, and that's why they're dissatisfied. Whether it's health care, or pension, or welfare, people can see that it's not working. That's the marketplace. And it demands to be satisfied.

A second was bold enough to suggest that the politically motivated Congress was one of the most important sources of innovation in the public sector:

> About the most innovative body I know (and I'll get out a whole paragraph before anyone jumps on me) is the Congress of the United States. Now, what do I mean? Well, the Congress and its 30,000 staff, they're constantly coming up with new ideas and new thoughts and writing bills. Some of them get through and some don't. Some look like good ideas in retrospect, and some look like bad ideas. The point is that they are both forcing and creating innovations.

And Len Schaeffer described how diverse demands and interests among political overseers in the Congress, the Executive Branch, and outside interest groups could be integrated by fashioning and describing the proposed reorganization of HCFA in ways that provided a little bit for everyone:

> When our program was communicated, it was not communicated like, "gee, we'd like to do this one good thing." We said, "This is important. We're going to do it because it's important. But OMB was going to save money. Maryland was gonna get jobs. Califano was going to get future leverage over health care. You can go down the list (of overseers and stakeholders), and we had a story. We sliced the bologna.

Market Risk and Political Risk. Of course, the resulting program may not have been optimized with respect to any one of these diverse objectives, but it had enough value in these different dimensions to earn the support of the overseers. In this respect, the mandate could be made politically coherent and sustainable. It was also operationally doable. Upon reflection, in comparing the substantive coherence of mandates for top level managers in the public and private sector, it seems that we may have been making the comparison in the wrong way. In the private sector, there is broad agreement about the abstract goals of the top level managers: namely, to earn financial returns for the shareholders. That makes it seem like there is substantial agreement about what should be done.

But the reality is that there is far less agreement about the best concrete path to be taken toward accomplishing that (agreed-upon) goal. The important, concrete decisions are based on uncertain forecasts of market demands, responses of competitors, and technological feasibility. Because there is so much uncertainty, there is often plenty of room for debate about what particular business plan is likely to achieve the best financial results.

The implication is that, in the private sector, the disputes and disagreements are about operational decisions that commit the company to a particular business plan. Such plans, and the doubts they occasion, may be discussed on Wall Street by company analysts who advise investors about whether to buy or sell stock in a particular company, and their judgments sometimes reverberate in meetings between stockholders, Boards of Directors, and CEO's. But within the governance structures of the modern corporation, these forces are somewhat muted, and rarely become powerful enough to challenge the discretion and authority of the private sector executive. By convention, private sector CEO's are left with a great deal of discretion in devising business plans -- at least until they run into financial problems.

By contrast, in the public sector there seems to be less agreement about the abstract goals. Or, perhaps it would be more accurate to say that we are less satisfied with the control that agreement about the abstract goal provides, for, at a high level of abstraction, there is common agreement about the goals of public sector organizations. The abstract goal is to "serve the public interest," or, more recently, "to create public value." These are as abstract as the goal of "maximizing shareholder wealth" is in the private sector.

Unfortunately, public sector overseers are less satisfied with these abstract goals than their private sector counterparts. They want to move even more quickly to a concrete discussion of exactly what is to be produced, and how it will be produced. In effect, they are trying to reach an agreement about the "business plan" rather than the overall goals of management. The reason is partly that they want to know in advance more concretely what they are agreeing to, and partly that they need more concrete specifications about what is to be produced to allow some measurement of performance. For both reasons, overseers in the public sector need to reach a more concrete agreement about what is to be produced by particular public sector organizations than commonly occurs in the private sector. Or, put somewhat differently, more people will participate in the approval of the "business plan" of a public sector enterprise than of a private sector company.

Unfortunately, as noted above, the overseers who engage in that effort to become more concrete in the description of mission, goals and objectives are a large group with diverse interests and objectives. In principle, the political, legislative, and policy-making processes of the government are supposed to do the work of forging an agreement about organizational goals and objectives among the overseers of public organizations. In practice, these processes rarely perform this function well. Commonly, political disagreements are simply left unresolved and carried forward as dilemmas to be faced by the managers charged with implementing the mandated policies.

The situation is made even more problematic for public sector managers by the fact that the political world is inconsistent and changeable. Sometimes the attention of the overseers is focused on the general objectives to be achieved through the organization, and the conversation is cast in terms of public interest objectives. Other times, the political conversation drops the pretext of serving the general interest, and focuses more narrowly on the particular objectives of powerful political figures who want contracts, jobs, and other perks for their constituencies. And, even the general "public interest" objectives change over time as the political goals and aspirations of citizens change, or as objective conditions in the world change. The net result is that, viewed over time, managers in the public sector face an uncoordinated, changing set of demands from their overseers.

When we compare oversight and governance structures between the private and public sectors, then, it often seems that the managers in the private sector have it relatively easy. They are accountable to only a few people, have a clear idea about what they are supposed to do, and are delegated broad authority to do what they have to do. Public sector managers, in contrast, are accountable to many, have ambiguous or conflicting purposes, and are constantly vulnerable to having their authority revoked or curtailed. Thus, it is hard for public managers to get started on the tasks of managing. They have to keep looking over their shoulder to see who's backing them.

The situation looks very different, however, if we compare the private and public sectors from a slightly different vantage point -- not from the perspective of their accountability to principals, but instead in terms of their obligations to perform. Compared in these dimensions, it suddenly becomes clear where all the risks and uncertainties facing private sector managers lie. They do not face risks from inconsistent, varied and changeable overseers. But they do face wildly varied, inconsistent, and fickle demands from consumers. Just like public sector overseers, private sector consumers want high quality, low price, reliable service, and variety suited to their particular tastes. Moreover, their desires tomorrow will be different from what they want today. The integrative task facing private sector managers is not to organize their overseers' demands for performance (which is the problem that public sector managers face), but instead to organize their consumers' demands. They have to find products and services which will appeal to many different customers, now and in the future, and which they can produce at a profit with the means at hand. In doing so, they effectively organize an initially disparate and incoherent group of consumers into "supporters" of the organization. The customers support the organization financially by providing the financial wherewithal to continue in business. They provide political support by providing evidence showing that individuals need and value the product that the organization is producing.

Note that what is interesting is that the organization of customers into a group of supporters for the organization does not concretely occur until the private sector manager offers them something to buy. If the manager has good judgment about what to offer, his proffered products and services will organize and sustain an on-going operation. If his judgment is bad, the enterprise will fall apart.

Public sector managers, in contrast, have taken care of their most compelling risks and vulnerabilities if they have found a way to satisfy their overseers. There remain some important questions about the quality of the service government delivers to clients, and whether particular activities the public sector engages in actually produce the desired results over the long run. And, as facts become available about these aspects of public sector performance, the overseers' enthusiasm for the enterprise may wax or wane. But the immediate and real risks for public sector managers are much greater in organizing and satisfying overseers and authorizers than in producing things for clients.

What this suggests is that political oversight is to public sector agencies what market pressures are to private sector firms. It is in political oversight that key decisions about what constitutes public value are made. It is there that the public manager must exercise creativity in aggregating apparently diverse interests into coherent wholes. It is there that important changes that stimulate innovation and repositioning occur. And it is there that the important risks to public managers lie.

From this perspective, then, both public and private sector managers face problems of integrating diverse and changing interests in formulating their plans about what is to be produced, and how it will be produced. The only difference is that in the private sector this happens when consumers choose to buy proffered services and products, while in the public sector it happens when managers present their policies and plans to diverse overseers.

Measuring the "Bottom Line"

Some of the most interesting and heated conversations about the structure of public and private sector accountability focused on the question of how organizational performance could be measured. Often, the O'Neill case was at the center of these discussions. The reason was that in both the public and private sector, O'Neill devoted himself to the task of building measurement systems that would support the resource allocation and investment decisions of top level decision-makers, and operationally challenge line managers to improve the current performance of their particular divisions.

Importantly, however, he focused his efforts differently in the public and private sectors. In the public sector, he concentrated on establishing a functional equivalent to the private sector's "bottom line": a system that directly captured the value of what had been produced by government. In contrast, in the private sector, instead of relying on the traditional "bottom line" financial measures that were already in place, he sought to develop new intermediate "process" measures.

What is striking here is that O'Neill seemed to think both: 1) that it was possible to construct "bottom line" measures for government, and that these would improve performance in government; and 2) that it was valuable for private sector firms to eschew traditional "bottom line" measures in favor of developing the kind of "process" measures that had long been viewed in the public sector as inferior to outcome measures. If O'Neill was right in thinking that bottom line measures could be constructed for government operations and that private sector firms could successfully use process measures to improve their performance, then the problems of measurement would no longer necessarily divide public from private sector management. The two sectors would use both bottom line

measures and process measures to make policy decisions, and stimulate operational managers to look for potential efficiencies or quality enhancements in production processes.

O'Neill himself fired the opening salvos in this debate in the small group in which he was a discussant when he attacked the notion that profits were the only guide to value creation in the private sector, saying, "I just don't agree with the notion that the private sector world is about making a profit. Nor do I believe that somehow profit is an unerring guide to how you either create, or improve, or sustain an institution."

Another CEG Principal in a different group made the complementary point for the public sector: "Measures don't just have to be on profit. There are lots of measures the public sector can use. They just have to reflect the definition of the agency's mission, goals and objectives."

Other CEG Principals nonetheless insisted that there was an important difference between the two sectors, if not in the potential for developing technically meaningful measurements of performance, then certainly in creating behaviorally compelling measures. Consider the following exchange that occurred in one of the discussion groups:

> *Participant*: The big difference between the private and public sector environments in terms of factors that impede or encourage innovation is the discipline of the market in the private sector. I simply do not believe there is a market discipline in the public sector.
>
> *Participant*: I agree with that.
>
> *Participant*: There is little incentive to change in the public sector because there is no bottom line. As a result, it's hard to recognize when change is necessary or appropriate.
>
> *Participant*: In the government, you cannot really say to people as you can at ALCOA, "I'm working with you to make us the best so that we will prevail and save our job and save our company and prevail in this marketplace." I really think that difference sets up a totally different dynamic between managers and employees in the private sector than in the public sector.
>
> *Participant*: What Paul was saying, though, is that reducing infant mortality is the bottom line in the public sector. The goal is to reduce infant mortality.
>
> *Participant*: But the problem is that that's not a market-driven

problem, and the future of the organization does not depend on achieving it.

Participant: I disagree, you can create a market discipline in the public sector, can't you? Isn't that what O'Neill was trying to create at OMB?

Participant: You may be able to create a measure of value. But I'm not just talking about measurement. I'm talking about the discipline of the market -- the necessity of generating customers and revenues or having the enterprise fail.

Participant: The real problem in the public sector is a motivational one, and that is only partly solved by improving measurement. All of us are very well motivated, concerned about the public policy issues we've worked on, interested in reducing infant mortality, and so on. But I think it is really hard to keep the bureaucracy focused on the public policy objectives as opposed to other underlying objectives such as keeping this job, having other people work for them, having a larger budget, etc. And they can accomplish many of these other objectives through means other than achieving the desired public policy objectives.

Participant: But all that's true in the private sector, too. You know, I really disagree with the idea that public sector organizations are not disciplined by some kind of market pressures. There is a market out there in the public sector. There is a conception of value to be produced. You just measure it differently. The challenge facing the public manager is to try to cause the people who work in whatever the agency is to care about their customers, if you want to call them that, the people who are getting the benefits, the services. The problem is that doesn't happen much anymore.

There is much that is interesting in this exchange, but one point seems especially important: in developing and using a measurement system, it seems important to distinguish between the technical aspect of a measurement system (which concerns its ability to reflect reasonably accurately some definition of value), and a managerial aspect (which concerns its ability to focus and stimulate organizational effort). A measurement system that is technically very good, but is not linked in any important way to an organization's hopes for survival cannot do the managerial work of focusing and motivating effort. On the other hand, even bad measurement systems can be behaviorally powerful if they are linked to an organization's survival. The key, then, in using measurement

systems is not only to solve the technical problem of accurately defining value, or processes that are consistent with value creation, but also to wire them into the systems of accountability that affect the organization's capacity to survive and flourish. Both problems are solved fairly easily in the private sector; both take managerial work in the public sector.

An equally sophisticated discussion of these same difficult issues occurred in a different discussion group:

Participant: So you don't buy this notion that the private sector's got a clear purpose, and a clear bottom line, and that the public sector's goals are far more amorphous and difficult to measure.

Participant: I guess it depends on your prior experience. Having been with the IRS, there really was a bottom line. It could even be measured in financial terms. It's hard to see the financial bottom line in entitlement agencies where you're giving money away.

Participant: In the private sector, you have a generally accepted measure of performance. At the end of the day, if Blue Cross is making money, that's good. And if we're making more money than anyone else in our business, then we're sort of ipso facto the best. We may not really be the best, but there's a generally accepted measure.

Participant: I think profitability is an entirely ambiguous measure in the private sector. It's quantifiable, but it may not measure anything important. Just speaking of my business, we're continuously making judgments that reflect the claims of competing interest groups on our bottom line. We're making judgments about how much to invest in the quality we deliver to our clients, which we can squeeze tighter and show a better short-term bottom line, but which we judge is not good for us over the long run.

Participant: I hear all that about the ambiguity of the measure. But I tell you, if you lose money three years in a row, it's hard to tell those overseers.

Participant: Oh, you can't lose money. But I think there are degrees of success and profitability. There are companies with whom we compete that have much higher returns on sales than we do. But it's not our judgment to do that at this point for all kinds of reasons having to do with the interplay of the various groups and our sense of strategy for dealing with them. Yeah, you can't lose money. But there are degrees of pricing aggressiveness, and decisions about investments to be made that also go into your calculations.

Participant: Are you publicly held. Does the stock trade?

Participant: No.

Participant: But if you were, then there's a market price for the value of the enterprise. And my only point is that in government, there are not generally accepted measures out there that end conversations. Not forever, admittedly, but they answer the question of whether you're doing a good job. The stock has been going up for the last couple of years, and so has profitability and sales. And that's sort of shorthand for doing a good job, whereas in government, I think it's real hard to tell in a way that ends conversations.

Participant: But we're being cautioned about just what is measurable in the private sector. Sure, you can get your quarterly results. But in a situation where you're publicly held, you may be driven to produce quarterly results, and that may be a problem because the quarterly results are not necessarily the best indicator of where you'll be in five years.

Participant: I think the measurability is over-rated. If you've ever been in a merger and acquisition fight, the public relations effort is just like government. You know, are you or are you not doing a good job. There's always a lot of debate about who's doing well.

Participant: O'Neill is onto this. For him, the financial measures of performance are not important. It's the non-financial measures that are important. And I can tell you that in our business that is also true. The quality of the service, which is non-financial but nonetheless quantifiable. Of the non-financial but quantifiable measures of employee relations, and so forth. Those are really at the heart of business... (T)he fact is that financial measures are very, very ambiguous.

Participant: But the point is that the financial measures are there, and everybody agrees about them. I think the measurability issue in the public sector is you both have to create the measures and convince people that they're valuable. And then you have to achieve them! And you can't achieve them unless you've persuaded people that they're important.

Participant: They are there and they are not. The fact of the matter is that any properly run financial department in any company I've ever been associated with makes decisions about reserve accounts, and those decisions affect bottom line financial measures.

Participant: I agree that those financial measures can be manipulated. But in a large corporation, somebody at some point agrees on the numbers, and the corporation below takes action, and has to make the numbers they agree to. That drives how you do business.

Participant: But let's look at the public side. On the public side, you don't start with that general agreement about a way of measuring. At least in everything I was involved in, you have to first create a mission, or hope that there's one out there. Then you have to create goals and measure against them. And you've got to convince the people you need to convince in the outside world that these goals are meaningful. And frequently, when you're trying to manage people -- hold them accountable -- and some of the larger goals are so diffuse, are so public policy, you end up with people being assigned interim process goals -- e.g. get the checks out on time. (This happens in the private sector as well, but more so in government.) So getting them out becomes important, but it's really irrelevant.

The conclusion, then, seems to be that measurement is a powerful tool in both sectors for satisfying the demand for accountability, and for focusing the organization's attention on value-creating performance. But to fully exploit the potential of measurement systems, managers in both the public and private sectors must use both process and outcome measures, must find ways to wire those measurements into the systems of accountability that determine the organization's future, and must be sure that whatever process measures they use are powerfully connected to the processes that actually allow the organizations to create value.

Incentives for Innovation

A key question for our project was to what extent the systems of accountability in the public and private sectors created incentives for managers to innovate. The entering hypothesis was that the incentives for innovation would be weaker in the public sector than in the private. The assumption was that the implacable demands of the market, revealed by the measurement systems routinely recording the financial performance of firms, would quite naturally stimulate demands for change when that was necessary. Further, private sector managers would find it relatively easy to gain support for innovations from their overseers who were united in their purposes, and agreed with the need to change. In contrast, weak measurement systems in the public sector would make it impossible to tell when change was needed, and public sector managers would have to confront overseers who were divided on the need for change, and skeptical about innovation and experimentation.

The way that we chose the cases made it difficult to use them for evidence on the question of whether incentives for innovation were weaker in the public sector than in the private. After all, we wrote about CEG principals who had been successful in innovating in both sectors. Presumably, they had found at least some incentives to innovate in both sectors. What evidence existed of differences between the two sectors would be revealed only in the relative difficulty of launching innovations in the two sectors. And that was hard to discern and make quantitative.

Still, as one reflects on the four cases, it does seem clear that the implacable demands of the market do play an important role in stimulating innovation in the private sector. Schaeffer's innovations at Blue Cross are both occasioned and facilitated by the financial crisis facing the organization. But for the terrible financial results, Blue Cross would have continued with the strategy of "being Blue Cross" and never made the transition to the new strategy of "supplying 'managed care products' to selected market segments." Similarly, Fields' innovations in MCC are being stimulated and guided by the financial objectives of the supporting companies in the consortium who are simultaneously shareholders, overseers, and customers. And both Larry Dale at Fannie Mae and Paul O'Neill at ALCOA are guided by judgments about where market opportunities lie: in multi-family housing and aluminum, respectively.

Moreover, in responding to the challenges and taking up the opportunities, the case protagonists do seem to find it relatively easy to gain and maintain the backing of their overseers. Schaeffer's board at Blue Cross grants him wide latitude to alter the organization's basic strategy. O'Neill's board also gives him wide latitude and continuing support as he refocuses ALCOA's attention on its core aluminum business. And Dale is given the strong backing of his superior, David Maxwell, in developing the multi-family business for Fannie Mae. Only Fields seems to face some problems in keeping his overseers behind him, and that seems to be caused by some worries about the value of the innovations he is, in fact, producing.

It also seems important that the case protagonists react subjectively to the challenges and opportunities in the predicted ways. They like the fact that they are given the responsibility to carry out a complex project, and that they can concentrate on performing without having to constantly

defend and justify their actions. They enjoy the freedom and creativity that goes into making their private sector innovations. They like the clarity of the results they can achieve. And they like the financial rewards. Thus, if one is the kind of person who likes to take a risk and make something happen, which all of our innovators seem to be, then the structures of accountability in the private sector do seem not only to tolerate but to actively encourage innovation.

What is surprising in our cases, however, is that the public sector, too, seems to produce incentives for innovation -- at least enough to produce some degree of innovation in the government. The difference, however, is that instead of emerging from the inexorable financial logic of the market, illuminated by the telltale signals of financial measurement, they emerge from a much more idiosyncratic process in which individuals envision a valuable change in the public sector, and then pursue that vision using the considerable political and managerial skill required to produce innovations in the public sector.

Schaeffer's public sector innovation, for example, emerged from Califano's conviction that he could use the purchasing power of the federal government's health care programs to leverage medical care systems throughout the United States to produce a more economical and fairer distribution of health services. As Schaeffer observed, "I think I had a great luxury (in trying to innovate)...That is that Califano had an agenda...He provided the inspiration."

O'Neill's innovation emerged from presidential aspirations to enhance the rationality of budgetary choices. And Dale's small innovation early in his career came from his conviction that greater public value could be wrung out of HUD programs if they allowed mixed income housing.

Obviously, individual insight and creativity plays an important role in producing innovations in the private sector as well as the public. But the difference seems to be that the innovators in the public sector are rarely carried on a tide of shared agreement that something must be done to deal with a problem. More often, it seems to emerge from individual conviction that gains either weak assent or grudging tolerance from others.

It is also potentially significant that the case protagonists all claimed that they found more room for initiative, creativity and innovation early in their careers (when they were at relatively low levels of the bureaucracy) rather than later (when they had achieved higher offices). Schaeffer, Dale, and Fields all testify to this fact in the cases. Of course, that could be due to the fact that they were younger and had more energy and enthusiasm early in their careers. Or, it could be because the innovations were smaller, and therefore required less authorization.

But it could also be that public sector organizations, and the political oversight that guides them, are structured in such a way that as decisions get bigger and more significant, they are forced through an extensive process of consultation, and dramatically slowed. Most government organizations are functionally organized. That usually means that a great deal of high level coordination is required to make any significant change because programmatic changes usually have operational implications that cut across functional boundaries. And, as one gets higher in organizations and decisions become more important, external oversight typically becomes much more rigorous.

In discussion, the participants tended to support the notion that the pressures for innovation and change tended to be more systematic and compelling in private sector accountability than in private. One observed:

> If you're in a business, you know when you better change because your sales are way off, or your technology's been bypassed. Government is different. We got a whole lot of things that need changing, but we don't really know that that's true, or where it's true, because there's no bottom line. There are also relatively few places from which ideas about what should be changed can come from.

Another Principal echoed the same theme: "It's tougher to change when you're successful than when you're in trouble. And it's hard to know you're in trouble in the public sector -- at least in terms of performance."

They were also convinced that, once having been authorized to innovate, it was far more difficult to manage the process of innovation in the government. The principal problem was in persuading public sector bureaucrats about the need to change, and finding ways to motivate performance. One Principal expressed his frustration quite directly:

> In terms of innovation in the public sector, you can't touch the people. So you play games and hope to motivate them by moving them around. In the private sector, you have much more freedom, at least in playing around with the people.

Another made the same point more analytically: "The civil service system does stand in the way of many innovations in the federal government."

Finally, the CEG Principals judged that the personal risks of innovating were greater in the public sector than in the private. The risks that counted, though, were those that were associated with the experience

of public exposure and humiliation rather than with economic losses or diminished professional stature.

> *Participant*: I think it's pretty clear from these cases (and my experience) that the risks of innovating, and the difficulty of achieving one's goals are both much greater in the public sector than in the private.
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> *Participant*: What is the character of the risk in government?
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> *Participant*: Getting fired! But there's also more public exposure in government. You're far more exposed to the media, far more exposed to whatever oversight there is, whether it's Congress or your own boss or public. And it's much harder to succeed in government... At the same time, it's probably more satisfying than the work you do in the private sector.
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> *Participant*: Don't you lose your job when you fail in business?
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> *Participant*: No, you get insulted.
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> *Participant*: Public and private exposure of failure are two quite different things.
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> *Participant*: Another reason it's riskier to innovate in government is that you have less time to be successful. You also have to work under greater scrutiny, which makes it more difficult to achieve your objective because the scrutiny eats up all your time, and you have to keep making changes in the program.
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> *Participant*: I'm not sure it's any riskier to innovate in the government. It may be more difficult, or more complex, but I don't think it's any riskier.
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> *Participant*: Are the risks the same?
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> *Participant*: Well, I would have said that you run a larger risk in the private sector of getting fired than you do in the government. The exposure problem may be worse in the public sector. You may be more pilloried in public for failure there than in the private sector. And that makes a big difference.

Chapter IV

Innovating in the Context of Capricious Accountability

Despite the complex structures of accountability and the lack of incentives for undertaking innovations in the public sector, they nonetheless seem to occur. As one CEG Principal sardonically observed, "The image of an accountability structure that ties everyone in knots might have some justice to it... But that structure doesn't seem to stop Len Schaeffer!"

The question for this section, then, is what do managers do to innovate successfully in these relatively unfavorable circumstances.

Taking the Lead and Accepting Responsibility

The cases and discussions with the CEG Principals suggested the truth of a familiar cliche: innovation seems to depend on individual initiative and leadership. When venturing into the unknown, someone has to be brave enough to take the first few steps. Then, they have to be sufficiently determined and skilled to carry the project through to completion. Having said this, however, several qualifying observations must be added to avoid the implication that there is something extraordinarily rare or magical about those who succeed in innovating.

First, to lead, it is not necessary to work out the answer oneself; it is often more important to stimulate others to be innovative. Thus, one CEG Principal observed that David Maxwell should get as much credit as Larry Dale for Fannie Mae's success in multi-family housing because he had the sense to see the opportunity and hire Dale to develop it for him! Similarly, it is clear that Fields and O'Neill, who lead organizations committed to continuous innovation, succeed not by having all the ideas themselves, but by creating conditions in the organizations in which others can be innovative. Managerial creativity lies in encouraging and using the substantive creativity of others as well as one's own.

Second, many different talents and styles can form the basis of innovative leadership. Schaeffer, Dale, Fields and O'Neill are very different kinds of people, with quite different talents. Schaeffer's commitment, determination and energy contrast with Dale's quiet but no less determined technical competence. These, in turn, contrast with Fields' somewhat bemused search for an "adequate" or "substantial" consensus, and O'Neill's persistent analytic challenges to his organization. The point is simply that there is no one style associated with effective leadership and innovation. For every successful hard-charger, there is a reflective facilitator. For every substantive expert obsessively committed to a particular idea, there is someone whose creativity lies in his or her openness to new ideas and inventions.

What successful leaders and innovators may have in common, however, is their willingness to accept personal responsibility for an experimental initiative -- either to authorize and support it, or to carry it out. They do not necessarily court this attribution. Indeed, if the enterprise is successful, they are often generous in sharing the credit. What seems key is that they are willing to step forward and accept the responsibility -- particularly at the tough spots, for example, when launching the innovation, or keeping it going when it seems to be failing. They take personal responsibility even though they recognize that it is never entirely accurate to attribute the initiative only to them, and that the innovation cannot be successful if they are the only ones who are committed to it.

The willingness to take responsibility is important partly because it goes along with a certain kind of temperament and personality. But it may also be an important tactic in introducing innovation. If one person is willing to take responsibility for an innovation, everyone else can be relieved of the responsibility, and their potential opposition converted to mere watchfulness. Upon reflection, Schaeffer thought this was key to his success in both public and private sectors:

> *Schaeffer*: One part of what made the HCFA innovation successful was that we (Califano, Champion, and I) said up front that we would take responsibility for the invention. We promised that if it didn't work, nobody else would get in trouble... That's a big part of succeeding in the public sector. The deal we offered was: "This is what we want to do, we're gonna do it, you can trust us, and if it doesn't work, we'll be in trouble, you won't."
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> *Participant*: So you limited the exposure of other folks.
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> *Schaeffer*: Yeah... I haven't really thought this out, but the same thing happened at Blue Cross. The deal was, "I'm doing this, and if it doesn't work, I'm history." But then 30 percent of the way down the road, it's "I'm doing this, but if you want to join, we're gonna look pretty good." And some people decide to join. Then 75 percent of the way down the road, everyone says, "We're doing it." Then, you've got it made.

The importance of personal leadership and responsibility in public sector innovation creates an interesting paradox. On one hand, because personal leadership and responsibility seem to be key to successful innovations, they should be valued. On the other hand, the arrogance and flashy style that often accompany personal leadership often attracts hostility and suspicion in the public sector. Of course, I may have exaggerated this tension. There are many who can lead and take personal responsibility without becoming arrogant or flashy. Indeed, our case protagonists revealed subtle and interesting combinations of boldness and initiative on the one hand and openness and humility on the other.

Still, it is probably both important and accurate to observe that while success in both sectors may depend crucially on an executive's willingness to take the initiative and accept responsibility while remaining modest about his or her contributions and generous in crediting others, executives in the public sector must err even more on the side of modesty. Otherwise, as the case of Greg Coler suggested, they will trigger close press scrutiny and antipathy. The resulting coverage, focused on questions of arrogance and self-promotion, will distract attention from their significant accomplishments and weaken their ability to achieve them.

In short, the paradox is that the public expects a style of management in the public sector that would be ineffective if managers actually engaged in it. The simple fact is that we need more initiative and leadership from public sector managers than we are now prepared to acknowledge.

Developing Good Ideas

By definition, successful innovations depend not only on drive, and on the willingness to take personal responsibility, but also on having good ideas. Yet, in our discussions, it proved to be easy to pass by the question of whether the particular innovations being introduced were good ones, and if so, where the ideas might have come from. Also neglected was the issue of whether the demands for accountability were valuable in screening out bad ideas, or developing weak ideas into better ideas. Some CEG Principals noted the absence:

> What's bothering me is that in both these cases (Schaeffer and Dale), a significant policy decision was made. Yet we just ignored the quality of that decision....We never even talked about whether either of these public sector policy decisions were correct. In the two cases tomorrow, we have these naive people (Fields and O'Neill) who think that the truth matters. They seem to think that if only you have the right bases for your decisions in the public and private sectors that you'll be successful...I would think that if you're trying to justify something in the public sector where you have no bottom line, the very first thing you have to do is to have a rationale, and probably even try to sell it, at least to a few people, before you go ahead and start moving everyone to Pittsburgh.

Another CEG Principal expressed her confidence in the central importance of the quality of the ideas that are developed in determining whether those ideas will make it through the oversight process: "Ideas are the engine that makes everything go. If you've got a good idea, people will get excited about it."

No doubt, the reticence about discussing the quality of the innovations presented in the cases reflected diffidence about judging the performance of fellow conferees. But the reticence can also be explained by the simple fact that it is hard to evaluate innovations objectively, even when one has the benefit of hindsight. The problem is partly measurement. But there is also a conceptual problem. Innovations look different in different time frames. Some innovations that initially seemed quite valuable, turn out to be problematic in the long run. Others, that start off looking like failures become quite valuable later. Particularly important in this last category are innovations that fail, but teach a valuable lesson about how to do it right the next time. For example, one of the reasons that Larry Dale succeeded with multi-family housing in the private sector while HUD failed was that he had the unsuccessful experience of HUD to draw on in designing Fannie Mae's version of the program.

Because it was difficult to evaluate the innovations, the discussants may have tacitly decided to avoid this issue, and focus their attention on the managerial techniques used to propel the innovations forward. Assuming, with the discussants, that the innovations introduced by the case protagonists were valuable, it is interesting to note the different sources that the innovators used for inspiration for their ideas. Schaeffer seems to rely on a long-run institutional vision that the major challenge facing the government's health care programs is to show that they can be effectively managed, and the most important opportunity they can exploit is to use their combined purchasing power to leverage changes in the private health care system. Dale seems to use his own in-depth knowledge of housing finance, and his particular knowledge of the failed HUD multi-family housing co-insurance program to design a superior approach to be undertaken by Fannie Mae. Fields seems to search for ideas through the process of managing an "adequate consensus," and through reliance on his own active imagination. O'Neill doesn't so much look for particular ideas as he tries to invent methods that focus peoples' attention on finding and exploiting opportunities to create value.

It is surprising that, with the exception of the Dale case, there is little in the cases that resembles a formal "strategic planning process" that defines the need for innovations, and then stimulates the development of a plan for carrying them out. The process surrounding the initiation and authorization of innovations generally looks much looser and less formal. The closest we come to a classic planning process is Dale's development of a "business plan" that draws heavily on his own technical knowledge, and is submitted to Maxwell for approval as part of Fannie Mae's overall strategic planning processes.

In contrast, the rationale and techniques for the reorganization of HCFA may have been worked out in detail by Califano, Champion and Schaeffer, but it is not developed in the context of formal planning, nor fully explained. Fields and O'Neill both create organizations within which people are challenged to think about how to achieve the organization's long-run goals, but one doesn't have the sense that particular projects are initiated, designed and approved for implementation through a centralized, staff-dominated decision-making process. Thus, these managers seem to create organizations that "grope" towards success, guided by a general idea whose details are adapted as needed, rather than do all their thinking in advance, and commit themselves to a detailed course of action.

In the public sector, a great deal of emphasis is placed on planning and analysis in advance of taking action. As one CEG Principal observed: "In government, there are better analysts, and analysis is highly valued -- much more so than in the private sector. But in the private sector, the question is, "Did you get it done?" This same participant went on later to add to this observation:

> I think there is less value placed on management in the public sector than in the private sector. I don't know why that is. But many people who are put in management jobs in the government suddenly change their stripes, and become less interested in management. (They get more interested in "philosophy" and "policy.")

In short, in innovative organizations, planning is done in the line operations rather than in staffs, and central decisions are importantly influenced by operating results rather than the predictions made by analysts and planners. The innovations are not developed by a staff and turned over to the line for implementation; they are invented by line managers facing operational problems.

None of this implies that planning and analysis is not important. The O'Neill case gives clear evidence of the potential power of analysis. The point is simply that the analysis must be oriented toward improving decisions and operations, and done by and with those who are responsible for implementing the plans if the analysis and planning are going to make any difference in the organization's performance.

Consulting with Overseers

One of the most commonly identified obstacles to innovation in the public sector is the difficulty of persuading the many divided and demanding overseers of an enterprise that an innovation would be desirable. The cases made it clear that this was, in fact, an important problem for public sector executives. The cases also revealed that managers had different attitudes towards this problem, and different methods for dealing with it. The sharpest contrast, perhaps, was between Len Schaeffer who seemed to challenge his overseers to keep up with what he was doing, and Craig Fields who engaged in a "constant conversation" with his "boss, his boss's boss, and the 535 members of Congress" searching for an "adequate" or "substantial" consensus about DARPA's purposes.

Contrasting Styles: Schaeffer and Fields. The Schaeffer case, in particular, seemed to provoke a great deal of discussion. At issue was the propriety and efficacy of his methods of consultation with overseers to whom he owed some degree of accountability. One CEG Principal who had also been involved with the creation of HCFA went beyond the case to explain what had happened:

> Califano set up a secret task force. It was very small. It met off campus. No minutes were ever published. He got the President's approval and OMB's presumably...But then one day he called in the press and simply the announced the whole thing. It wasn't that "we're going to do this and we'll work out the details later"; it was carefully thought out...The reason he gave (for relying on this closely held process) was that there were so many embedded constituencies that if they had gone with study groups and commissions, it would never have gotten done.

Another CEG Principal took strong exception to this way of proceeding:

> I found the whole HCFA story depressing...Schaeffer decided that the only way to accomplish what could only be described as a major change in domestic policy in the United States had to be accomplished without talking to anyone.

In subsequent discussion, Schaeffer clarified the techniques used for authorizing the change:

> In the beginning, I spent a tremendous amount of time out talking to people... We visited all the regions and places before we got them together...This thing was not done as a secret. But it was the reverse

> of what you would normally do. It was done without fanfare...It was just kept very low key...What we did not do was hold a press conference telling everyone what we were going to do. What we didn't do was go over to Congress and try to get a bill through...None of what we did was secret. They were packaged when we went to see people...It was sold to the politicians as "jobs for Maryland." Externally, there was none of the policy spin on it.

Craig Fields seemed to embody a much different approach to the challenge of political management. In the case, he talked a great deal about the need to develop an "adequate consensus." He explained as follows:

> There's one person who's the formal boss, but that's not germane to the issue. The issue is you have a lot of informal bosses, because DARPA is and was popular enough and visible enough that your boss's boss, and your boss's boss's boss, also thought they were your boss. And 535 people called congressmen think they're your boss. And a lot of people in the military services think that they're your boss, too.

In his mind, he thought he had a great deal of authority to set the direction for DARPA, but he judged it both prudent and proper to exercise that discretionary authority only with a high degree of consensus. He distinguished between an "adequate consensus" which was enough to justify innovations that were well within his statutory authority, and a "substantial consensus" which was necessary to allow him to operate at the edges of his statutory authority.

To produce either kind of consensus, he relied on the same techniques: listening, reading, and talking to his overseers. As the case reports, to be allowed to increase DARPA's emphasis on manufacturing technology, Fields engaged in an elaborate process of consultation.

Looking to the Congress, he could narrow the field from 535 down to a manageable number of members and staff, and then go about 'finding out what they think, and reading what they write, and communicating at hearings what you're trying to do, and getting their questions and feedback at the hearings.' Within DOD, he used similar tactics, starting with his 'direct line and chain of command within the Pentagon,' and expanding to other key players, including the director of Defense Research and Engineering, 'a whole gaggle of assistant secretaries,' the research assistant secretaries in the services, the service secretaries, the chairman of the Joint Chiefs of Staff, the director of Policy Analysis and Evaluation, and the comptroller.

Fields did not believe in winning consensus approval through anything more than simple negotiation, and the force that he believed was inherent in his ideas. "I'm not a calculating person," Fields says. "Basically, it's the content of your ideas that causes you to get what you want." His process of trying to garner, and keep, a consensus was ongoing: "It's like pumping up a leaky balloon, you have to just keep pumping it continuously." One might have thought that this elaborate process would guarantee that Fields would work only on mainstream projects, and remain comfortably in his position. Yet, he eventually found himself taking what was viewed by many as an extreme position on "industrial policy," and the role of DARPA in supporting that policy.

It was difficult for the discussants to resolve the substantial issues raised by these two different approaches to the process of consultation. Schaeffer went at the problem in a way that seemed wrong, but also seemed to be successful. Fields seemed to do what was right, but lost his job nonetheless.

The Importance of "Political Management." Everyone seemed to agree that the cases made it clear that "political management," or the management of relations with overseers, was a key part of a manager's job, and particularly important in the public sector. When asked to give a summary of what he had learned from the cases and discussion, one CEG Principal offered an eloquent statement of the importance of this function of public sector management:

> Part of a manager's job is not just to set goals (within an agreed upon mandate) like the textbooks tell us. They also have to aggressively manage the accountability structure (to help define purposes). The overseers are not just a sleeping dog (that one has to step around to avoid disturbing); they're the source of your mandate. So, you can't just sit there and wait for them (to tell you what they want). You have to rush in to manage that whole accountability structure. That's your job. You manage it, and it manages you. It goes both ways...This insight seems revolutionary to me. The people in our cases have different styles, but they all manage their authorizers. Sometimes they win and sometimes they lose. But they all work their structure of accountability.
>
> That is not the model of traditional executive. That's not the norm of the executive in government I've known. In the traditional model, I see a lot of people end up in executive jobs, career people by promotion or political by appointment, and then when they're there, they decide not to be executives. They have the executive jobs, but they say, "I'd like to do something else." So, they don't set goals, and they don't manage the accountability structure...We really have a

new professional ethic that we should be discussing as part of the job of the government executive.

There seemed to be widespread agreement, then, that the willingness to engage the "accountability structure" in serious dialogue about purpose was important to a public sector executive's job. Nothing else was consistent with the moral requirements of democratic governance. Nothing else could be expected to produce appropriate authorizations for innovations. And such consultations could be an important source of ideas about what kinds of changes were important and valuable to carry out.

Yet the groups continued to struggle with at least two key questions about how to engage overseers in the process of developing mandates and authorizations. One concerned the spirit in which a manager entered the process of consultation: whether one entered with a firm conviction about what the right answer was, and then sought to "sell" the preferred solution; or whether one entered with a much more open mind and was prepared to be instructed and learn from one's overseers about what was worth doing, and the best way to do it. A second concerned the question of when the process of consultation could end because it had achieved its goals, and one could then turn his full attention to producing what had been agreed upon.

"Selling" or "Facilitating Consensus." With respect to the first question, the small discussion group of CEG Principals that included Craig Fields had a fascinating exchange:

Participant: What do the managers in these cases do that seems to be essential to innovating successfully?

Participant: They do "consensus building."

Participant: I'd use a different word. I'd call it "selling."

Participant: But what do they build a consensus about?

Participant: About the need to innovate; more specifically, that there's a problem if we don't innovate.

Participant: Well, I would say they tried to build a consensus behind the manager's objectives (I'm assuming the case study victim had an idea that he thought should be pursued!)

Participant: Do you think Craig's goal was to get everybody lined up behind his purposes? Is that how you heard him?

Participant: I think his goal was to get something done which he thought was good.

Participant: Or, maybe it was to help define the consensus for what needed to get done.

Participant: I agree with that.

Participant: Craig, during the process of consultation, did you change your view about what needed to get done?

Fields: Always.

Participant: Why?

Fields: New data, new information.

Participant: This is an important point. The question is how open should an innovator be to new information about what's worth doing?

Participant: Well, that may be important, but I think the key thing that allows innovators to succeed is that they have a sufficient consensus on their aims to drive it home to success.

Participant: We're using the word consensus in a misleading way. The right word is selling. I introduced that word because when you're trying to develop a consensus, you're trying to draw people into your thought process. If more public managers recognized that what they have to do is sell, then things would improve.

Participant: What does selling mean in this context?

Participant: Selling means translating your ideas in terms that are persuasive to others.

Participant: That's leadership.

Participant: You recognize that you're out to persuade. Now, there may be a semantic difference between: 1) somebody coming into a group of people and building a consensus where they play a neutral role; and 2) somebody coming in with an agenda and trying to get that group to support their agenda at the end.

Participant: But good salesmen listen to their customers!

This discussion did not resolve the question of whether effective political management and leadership consisted of having an idea and persuading others that one was right, or of listening carefully to what others wanted, and then articulating a purpose that could accommodate the others' purposes. But it seemed clear that this was more than a semantic difference. It may be importantly linked to managerial style and personality, perhaps even to gender. It may also be important to normative virtue and practical success as a public sector executive. We will leave the issue for further research.

Another participant observed:

I think innovation is dependent on: 1) personality; 2) the task at hand; and 3) the support of superiors. We didn't really talk about the third, but I think it is really critical. Any mix of those three things in the right order and you'll get innovation. The wrong mix of that -- a superior who won't support you, for example -- then you're not going to get innovation.

Beyond these observations about the crucial importance of having the support of one's bureaucratic superiors, the question of exactly what constituted an "adequate" or "substantial" consensus remained unclear.

Negotiating Terms of Accountability

What was discussed in consultation with overseers was the manager's mandate for action. A mandate is usually understood as a set of substantive goals or objectives which the manager was expected to achieve. As such, they became the manager's substantive terms of accountability. Thus, the process of consultation was the concrete way that a "bottom line" was developed for public sector managers.

Agreed-Upon Goals as the Essence of Management. For many CEG Principals, the challenge of developing a political agreement about the goals and objectives of a governmental enterprise was the defining essence of effective management. For some, the link was definitional. As one put it, "In both public and private sectors, good management means specifying objectives, being efficient and effective, having measures of performance."

Others thought that having clear goals and objectives was important because they could help the manager communicate, both externally and internally, about what was valuable or central to the organization's mission. That would, in turn, actually help to produce the intended results. Still others thought goals and objectives were important because

they helped managers be consistent in resolving the particular issues that came to them. In one Principal's words, "You need to have objectives and work within those objectives on every issue you face." Whatever the particular reason, it seemed that everyone at the conference agreed that goals and objectives were essential to good management. As noted above, the difficulty was in getting agreement about what those goals should be.

The issue in the public sector is that you both have to create the measures, and convince people that they're valuable. And then you have to achieve them. Despite the difficulty of forging these agreements, many CEG Principals nonetheless seemed to believe that this was important, even critical to success.

Participant: I firmly believe that the goals have to be articulated publicly. You then have to be able to manage that message...If you can't get your message out, and if it can't keep the most critical part of your constituency behind it, you're probably gonna lose. You'll always have enemies, so you need to have some support. And when goals come together with support, you will succeed.

The Difficulty of Producing Agreed-Upon Goals. They were also clear that combining goals with political support was an extremely difficult task. What made it difficult was not principally the technical problem of developing appropriate measures, but instead the problem of continuing political controversy and vacillation. Consider the following long discussion about goal setting in political contexts that occurred in one of the discussion groups.

Participant: Take a program like Medicare or Medicaid. You would think, starting out, that the best measure of success would be how many recipients there are: the more recipients, the more good is being done. But now that has been turned around. Our biggest current problem, apparently, is that too much money is being spent on these programs.

Participant: That's an interesting point. For some indicators of government performance, it's not even clear whether society agrees on the signs of improvement. We don't even know which way is up! Do we want more or fewer welfare recipients? Well, it depends on what you think the problem is. If you think we haven't reached enough people, you want it to grow. If you think we've lost control of the program and included many who are not eligible, then improvement lies in reducing the number on welfare.

Participant: That is not unique to the public sector. General Dynamics has decreased by 40% and that's supposed to be a great success story.

Participant: But what the welfare example indicates is that people differ on the proper goals of public agencies. There is not even a consensus on how "customers" or "clients" of an organization should be treated. For example, many people think it is a good idea to treat welfare recipients in a degrading way when they come into a welfare office...Education is another good example. Do you want to maximize the performance of the top 10%, or the average performance of the entire class, or do you want to increase the performance of the lowest 10%? I think it is unavoidable that we will lack general agreement about the proper goals of public enterprises. But if we give up and say, "Well, there's not going to be any general agreement, so therefore we can't do a better job of managing in the public sector," we're going to be in bad shape. I think what we have to consider is how within the context of the lack of general agreement, we could nonetheless move forward.

I'm inclined to think that the best we can do, although it's far from perfect, is to measure all the different dimensions that are of interest to overseers. In other words, in the education domain, measure the performance of all the segments of the class. Same with the welfare system. Present data on total costs, populations left unserved, the generosity of the benefits, etc. Simply serve them all up for political discussion. See if the reaction you get from the political system gives you any guidance about what the real goals and objectives should be. If you don't get any guidance, pick the goals you think are important. I think that approach might work.

Participant: But it isn't just that there's no general agreement on the goals, it's that, in a democracy, everyone's an expert. Everybody's supposed to have an opinion on these big questions, and everyone gets a right to vote. So, in some very direct way, they have some authority over you. That's number one. Number two: if you're trying to run an agency, and if it's a big and complicated one that's highly visible, the process of serving up alternatives and trying to find out what people want is endless. So, I think what you do (or at least what I did with my life) was say, "I think I get what the Medicare and Medicaid Programs are supposed to be overall." We came to the conclusion that what they were about in 1965 was not what they were about in 1978. We said it's time for the next go-around. We sort of told our media process. We told a few other people. And then we just went to do it. When it was all done, I think we felt pretty good about it. But as I said in the case, there aren't more than 50 people who understood what we did. And there aren't more than 10 people now who would agree today on measures of whether we're successful or not.

Participant: There's something really important in the distinction you guys are making. The standard story we hear about the public sector is that we can't get a good measure of what we want -- of what's valuable. But what Steve's pointing out is that's at least partly because we want different things. That's because there's no general agreement on what the overall goal is...It's not just that the measures are imperfect, it's that we disagree about what it would be valuable to do.

Participant: The Paul O'Neill case tells us to think about some of the other non-financial measures that might supplement in situations where you needed to worry about a lot of different attributes simultaneously... But the problem is that when you write down those measures and say that's what you're managing for, then that makes it very clear what your values are. And that's when you get yourself in hot water, because you're an easy mark for those who disagree.

Participant: And other people have a right to their opinion. It's perfectly appropriate. But if you were to spend all your time going around and asking what they thought instead of what I think you have to do, telling them what you're going to do and why it's the right thing, you don't get much done.

Participant: Well, that's an interesting hypothesis, isn't it? That in order to manage well, you need measurable goals. But when you get around to stating measurable goals in the public sector, you end up making clear what your values are about. And when you do that, that's when the sleeping dogs wake up.

Participant: And you line up your opposition.

A little later in this same discussion a CEG Principal voiced his frustration at trying to manage with goals and objectives in a political context:

> You may succeed with one measurable goal, and then the next measurable goal may not be yours. It may be your governor's. And you may be set up for failure on that goal. Or, circumstances, public

> interest groups, or the Congress, state legislators, press, etc. can help establish a measurable goal and you could succeed or fail. Or, you can be in the middle of (achieving) a measurable goal and fail at it because it changed over the course of a year.

There may be a solution to the problem of developing goals in political environments hiding in this dialogue. It seems to lie in recognizing and exploiting a couple of important points.

Picking the Right Level of Abstraction. First, goals can be set at different levels of abstraction. This presents a choice to managers in defining their goals and objectives.

> *Participant*: The more specific the goals are in government, the more you're gonna wake up the sleeping dogs, because everyone's going to have a piece. The more general...the goals are, the more you can get agreement. (The general goals) work fine in the short run; over time (when you start trying to manage to achieve them), they're going to be a problem.

One of the CEG Principals thought this apparent dilemma could be resolved in a way that was useful to managers:

> I don't think it's a choice of either clarifying or leaving murky. I would suggest that there are a few broad goals that help to define the overall mission of the organization in utopian phraseology. But then there are 53 or 81 more specific goals that define what the manager is trying to accomplish more particularly. Some of the objectives could be sharpened and clarified (to get a managerial focus). Others could be left a little murky. I think if a manager clarifies everything, she'll get stuck. If she leaves everything murky, nothing's going to happen.

Perhaps managerial skill in negotiating terms of accountability lies in negotiating both broad and narrow goals, and organizing them in some kind of uneven hierarchy adapted to particular situations.

Establishing Multiple Goals and Objectives. Second, it seems important to recognize that there need not be a single goal, and that it need not focus on outcomes. The O'Neill case made it clear that process goals could be very important in guiding managers toward value. It focuses their attention and curiosity on aspects of performance in a way that outcome goals do not. This is the value of multiple goals operationally and internally.

Multiple goals may have political as well as operational value. Allowing the possibility of multiple goals would allow overseers with quite different aspirations for a program to be able to look at the program and feel reassured about its performance in the terms that mattered to them. This is the force behind the observation that "the best we can do, although it's not perfect, is to look for measures on different dimensions that seem to be valuable or important to our overseers. If they're interested in any particular aspect of our performance, the manager might be well advised to measure it. One way to produce agreement about what's worth producing is simply to let anyone who has a view have their own measure to monitor."

One can object to this conclusion by saying that the multiple goals will be conflicting and confusing. That may well be true. But it is also possible that they conflict operationally less sharply than we now imagine when we are thinking about the issues in the abstract. And, in any case, we cannot be sure to what extent they conflict operationally until we start measuring performance with respect to them. It is only then that we will be clear how much it would cost in total to deliver promised medicare benefits to all who were eligible, and how that number could be reduced by further rationing the supply of health care. Because we are not now measuring performance on many different attributes, we continue to have policy discussions that are informed by political ideology and analysis, but not by actual operational experience.

Sustaining Mandates

Beyond the problem of creating a mandate (in the form of agreed-upon terms of accountability), lies the challenge of maintaining or adapting it. One of the discussion groups was quite eloquent in exploring the issue of how managers could sustain or lose their backing in managing an enterprise or undertaking a particular innovation:

> *Participant*: This discussion reminds me of a point made by a friend of mine who was a CEO. In his view, every CEO has 10 years of good will... That comes with the job. And if you just kind of sit there and ride along, you can have good will from all the constituencies for 10 years. But if you try to make a change, the more change you make, the more good will you will use up. He told me that I had used up my 10 years of good will in the first 18 months!
>
> *Participant*: How much good will do you get as a public manager?
>
> *Participant*: You don't get 10 years!

Participant: I would argue that 10 years as a CEO in my corporate experience is unrealistic.

Participant: I didn't mean to be taken so literally. The point is that you only get so much good will...I think the amount of good will that anybody is given today, by virtue of being put in a job, is much less than it used to be. And the degree that you change things and stir opposition up in either the private or public sector, you chew up that good will very fast. What you have to do is create new good will by getting results. Now, in the private sector, if you get the macro results people are looking for, that generates new good will. In the public sector, I think it's more difficult to generate new good will in terms of results. It's more interpersonal relationships. It's more managing the media.

Indeed, that may be an interesting way to think about it. I always thought of it as a joke, but, you know, do you manufacture good will? I mean, I'm trying very hard to manufacture new good will from a constituency that's very unhappy on Saturday. I'm going to a meeting of hospital administrators because it's very important that they feel good about us. That's not a financial bottom line that I try to generate good will.

Participant: It's an interesting observation...Maybe we should think that the task of a manager in any kind of organization is not just to use assets to produce results, but to take a set of assets and produce a set of results that regenerates the assets. You don't just draw them down and use them up. You generate some continuing flow. Usually we have money in mind. But in the public sector it's support and politics and the continued willingness of people to let you do what you're doing.

Thus, the need for sustaining a mandate becomes another reason for solving the measurement problem in the public sector: it is performance, revealed by objective measures negotiated in advance, that helps sustain managerial credibility.

Changing Organizational Cultures

Eventually, if innovators are to succeed, the preoccupation with politics, authorization, and accountability must yield to concerns for making the innovation happen. As one CEG Principal put it, management is ultimately about "changing the physical reality of how things happen." And that, according to the CEG Principals, was no easy task. The

difficulty was partly in motivating and persuading one's subordinates to go along. Unless they changed how they thought and acted, the innovation just did not occur. As one conference discussant observed, "What (the Schaeffer) case seems to be talking about is organizational change -- changing the cultural values that exist." This theme was echoed by another participant:

Just as Len Schaeffer had to get the people at HCFA and Blue Cross to think of themselves as being in a totally different business, what Larry Dale had to do was not so much invent a new idea as to introduce an idea into a culture that didn't see itself in that new business.

The question before the group, then, was how to change the culture of an organization and get it focused on new goals and new methods of accomplishing traditional goals.

Contrasting Styles: Schaeffer versus O'Neill. Just as there was a split in the group in considering how best to manage politically with some favoring charging ahead until one was stopped and another preferring a slower and broader consultative approach, a split also appeared in the group's general approach to producing organizational change. One group emphasized determination, speed, and aggressive reorganization efforts. The other tended to emphasize more incremental efforts to induce the organization to go along. The argument for "permanent revolution" and frequent reorganization was articulated as follows:

I once asked an experienced CEO friend of mine which was the better way to organize: centrally or decentrally? He said, "Neither." I said, "what do you mean?" He said, "It's the tension between the one and the other that keeps the constructive tension going."

This observation reflects the conclusions of some of the academic literature on what makes for innovative organizations.

Reflecting on the Schaeffer case in which an important cultural change was effected through a combination of administrative reorganization and physical relocation, one participant observed:

You change the cultural values that exist by changing the physical places in which people work. All the fundamental values that habit, history and past practice in those environments provide (is undermined). You develop new rules and new values. (By administrative reorganization) you develop a whole new set of functional roles and working relationships. The folks who used to define rituals are no longer there to define that ritual so new ones

> have to be developed. You bring in these outside gods -- consultants -- and substitute them for the existing gods. Then, when they've done their work, you banish them from the organization to reclaim the sense that old values are still honored.

Others disagreed with this approach. They found it insufficiently respectful of the traditions and motivations already present in the organization that could be mobilized to help achieve the manager's innovative goals. One Principal asserted, "I think before you try to add value, you have to assess the value you already have and try desperately to protect it." Another making a similar point observed:

> How you get efficiency is (to find out) what other people are doing that we might learn from; tease the character and qualities out of the people who are there, and get them organized and motivated and give them a vision. We're not starting in the right place, with a sense of what it is we want to create.

A third noticed a contrast in the four cases prepared for the conference:

> Both Paul (O'Neill) and Craig (Fields) make enormous positive assumptions about the character and capabilities of individuals, and I think that's less apparent in the other two cases.

These large questions about how aggressively to challenge and attack one's own organization in efforts to change it remained unresolved. No doubt, how aggressive one must be depends at least a little on how urgent the situation is, and how far from the ultimate goal the organization seems to be. The more urgent the need for change, or the further from the ultimate goal, the more desperate must be the managerial methods employed. Thus, Schaeffer could (and did) argue that he had to move quickly in dealing with Blue Cross because the firm was about to go bankrupt. He also argued that he had to move aggressively in dealing with Medicare and Medicaid because, even though he had a long time to make the changes and the purpose of the changes was a long term result, the personnel operating the programs were so inbred and complacent that dynamite was required to make any progress toward the long range goal.

Yet, it might also be that how aggressive one opts to be is determined at least partly by temperament and style, and less by any objective diagnosis of what the situation requires. It is interesting in this regard that those who are aggressive in one situation tend to be aggressive in the next; and that those who are more protective in one situation are that same way in the next. This may be because managers are selected, or naturally gravitate towards, situations that make use of their particular

orientations and styles. Or, it could be that managers simply do what they feel comfortable doing no matter what the situation.

Using Goals for Inspiration and Feedback. Participants did agree on some of the things that make for success in driving an innovation through to an important organizational change. One, not surprisingly given its prominence in virtually all phases of the conversation, was developing widely agreed upon, explicit goals. Indeed, it seemed to many CEG Principals that if one could win substantial external support for the importance of achieving an important goal, that in itself would be tantamount to achieving it. The reason is that the goal, backed by political support, would become as compelling a reason for public officials to act as the obligation to produce profit is in the private sector. Thus, all the work described above that goes into building and sustaining mandates for action in the external environment will create a very favorable context for internal, operational innovations.

Beyond this, however, having a goal was judged to be operationally valuable in motivating and guiding one's subordinates:

> You can't motivate those working for you with money (in the public sector). It seems to me, realistically, that the only thing you can motivate them with is purpose -- infusing your purpose into their own thinking so they become, effectively, supporters, and people who want to be part of making a difference.

And:

> Most of the people I worked with in government were pretty highly motivated to perform their mission. They had a strong sense of values related to making health care available to the elderly and the poor...Therefore, someone who expresses a fundamental loyalty to the essential values and mission of an on-going enterprise, even if they have some differences with how that goal is being pursued, is going to get a lot of loyalty.

And finally:

> We thought we had a noble goal. I think a lot of people were inspired by the goal. We spent a lot of time working on it....We thought we were going to change America.

Having widely agreed upon, articulated goals was important for more than inspiration and motivation: just as it was important to sustain a political mandate for action by producing results, it was important to sustain the internal commitment to the changes needed by providing constant feedback on internal operational accomplishments. To some degree, formal measurement systems, tied to strategies of change, could produce that result. That is what O'Neill's two year benchmarking process at ALCOA achieved. But some informal mechanisms, such as newsletters or reports from the administrator can also be useful:

> The Administrator's Report came out every three weeks or every month. It was a big deal, because in the beginning it said, "We're gonna do some stuff." And then we actually did it. And that's unusual in government. So, people began reading it and taking it seriously.

Building Innovative Organizations. Much of the discussion of managing change was implicitly focused on the question of how a manager might successfully implement his vision of how the organization needed to change. That vision might have been developed through a broad process of external and internal consultation, and it might have been a long-term vision. That substantive vision could be a new program or product (e.g. a multi-family, co-insurance program; or high density television). Or it could be a basic shift in the overall strategy of an organization (e.g. from "being Blue Cross" to "providing managed care products;" or from "military technology to support national security policy" to "dual-use technology to support industrial policy;" or from "diversified products" to "low-cost producer of aluminum"). But the point is that the vision that was developed was a particular substantive vision of what changes in mission, goals, objectives, or methods were important to achieve.

Every now and then in the discussion, however, we could catch a glimpse of a slightly different challenge facing public sector managers: not to introduce a particular substantive change in program, policy or strategy; but instead to create organizations that were innovative, adaptive, value-seeking organizations.

> *Participant*: I guess the great problem is that nobody has a good idea right now about how to create an innovative organization in the public sector --- that is, one where people are innovative in spirit from top to bottom.

There were also some intriguing observations about what the problems in creating such organizations might be.

> One of the major mistakes in public management is to assume that one always wants hard-nosed program advocates competing for scarce resources so that the managers at the top can choose from the competing claims. You also ought to have people who will say, "Look, I've got a mission that's no longer needed, and I don't want to take the heat for saying this, but we ought to do away with this...We simply can't afford to have outmoded missions and pay for them.

Having mid-level public sector managers talk about where value lies in their organization's operations rather than in terms of defending their own turf would be as radical a change in our implicit view of what the functions and goals of public sector managers should be as the view that they have an important role to play in engaging the political discussion about what would be valuable for their organizations to produce. What is interesting, is that there might be an important relation between the two.

If public sector managers committed themselves to trying to produce value, and to accepting the notion that value would be defined (and redefined!) by political overseers rather than trying to guarantee the survival of their organization with its current mission and practices intact, they might be more welcome in the political dialogue. It is at least partly the worry that they are only advocates for their organizations that makes the political overseers view them with such suspicion.

It is also worth noting that this shift in focus would have an important impact on the ability of managers to motivate their employees. The CEG Principals observed above that one of the principal motivational tools available to them was to declare themselves in favor of the fundamental mission of an organization, and to garner the loyalty that came from their subordinates' commitment to that mission. If, on the other hand, they commit themselves to changing the mission -- to saving tax dollars rather than continuing a past enterprise, or to shifting the substantive focus of a mission from one goal (such as the development of military technology) to another (such as the development of dual use technologies) -- then they might well earn the enmity and distrust of their employees rather than their loyalty. Then, their need to have political support for the achievement of their goals will be particularly urgent.

This all puts into quite sharp relief the intriguing question of the extent to which a manager is accountable to his employees. It is clear that employees are important "stakeholders." But sometimes the crucial question is how much their views of "public value" should count in managerial calculations. It is an easy question if they want to produce what the political and task environment are telling them would be valuable to produce. In those cases, the manager can articulate a consensus goal. It is a far more difficult question if the political or task environment seems to be demanding something different than what the manager's employees would now like to produce -- such as a reduction in cost or scale, or a troubling shift in operational focus. Then, the manager must decide whether and how to challenge the organization. In such situations, it would be much easier for managers if the organizations they led were accustomed to change, and were not passionately committed to a particular view of their mission. That is another reason to be interested in producing innovative rather than efficient organizations in the public sector, for innovative organizations are less likely to become firmly and irrevocably committed to one way of doing things.

As to the task of creating innovative organizations, the cases and discussion suggest two interesting possibilities. One is that insofar as the cases suggest the importance of actively engaging the political environment, and recognize the volatility of that environment, one might conclude that a key to making organizations innovative is not to insulate them from politics, but to wire them more closely to the political environment. Just as getting private sector organizations "closer to their customers" tends to make private sector organizations more innovative and responsive, making public sector organizations more accountable to their diverse political environments may make them more flexible and adaptable.

A second is that techniques of analysis, focused on both outcomes and processes, may help to make the organizations more adaptable and innovative. Analysis helps to stimulate the question of what is valuable, and to chart paths toward the production of greater value. It provides a window on what is demanded by the task environment, as well as what is desired by the political environment.

Summary: Lessons for Managers

At the end of the conference, rapporteurs from each of the discussion groups were asked to summarize the observations and conclusions of their groups. They were also encouraged to develop any lessons that managers might learn from the discussions about how to manage the process of innovation in the public and private sector. Perhaps surprisingly, they concluded that while there were important differences between the accountability structures that managers faced in the public and private sectors, the techniques that leader/managers used to introduce or stimulate innovations were remarkably similar. Based on these reports, Frank Weil, one of the chairs of the conference, developed a "toolbox" for innovators in the public and private sector that stands as a useful summary of the "lessons learned."

1) Have a well defined idea of what you want to change and how you want to change it. In justifying it, stress values as well as process and data.

2) Make sure your immediate superior is comfortably on board before you make move one.

3) Be prepared to communicate your idea completely, graphically, and with human interest.

4) Develop at least an "adequate consensus" among your vital constituencies before sticking your neck out.

5) Prepare for the possibility of failure by conducting yourself in ways that avoid collateral attacks on your behavior, and by having the right friends to dampen the attacks from your natural enemies if that should occur.

6) Be open to new data, and be willing to adjust your plan and admit mistakes as you proceed.

7) Expect obstacles that cannot be anticipated and stay the course even when it may take longer and cost more than you planned.

8) Be as open and complete with the press as you can be. Do not try to use, deflect or mislead the press. If you have a good story, make it interesting and the press is likely to see it and report it your way.

9) Identify all the entrenched interests and their normal allies who will perceive threats to their economic, social and personal concerns. This will almost always include your own bureaucracy and staff. Keep a close eye over your shoulder on what they do, not only what they say.

10) A little bit of guile in making your case may sometimes be necessary and useful. If you want to achieve X, and person A will encourage the person you need to persuade about the value of X, then use A as a medium to carry your message.

11) Do not let yourself become the issue. If you do become radioactive, you may be better off getting out of the way.

12) Useful innovation often comes in small packages.

CHAPTER V

Conclusion: Innovation and Success in the Public Sector

In the short run, levels of innovation in the private and public sector may be importantly influenced by the particular structures of accountability characteristic of each sector, and by the opportunities for innovative leader/managers to innovate despite the obstacles. Over the long run, however, the level of innovation may be importantly influenced by the kinds of people who are attracted to each sector.

Eventually, the different sectors get the kinds of managers they want and arrange to have. If the private sector offers more opportunities for the kind of self-expression that innovative managers enjoy, and offers greater rewards for accepting the risks of innovating, then that sector will end up attracting more innovative managers than the public sector, and there will be more innovation in the private sector. If, on the other hand, the challenges of meeting the nation's most critical problems through public sector operations remain attractive to managers, and they have the sense that they can make a difference despite the politics and bureaucracy of the public sector, then the public sector will also attract innovative managers.

At least two things seem essential to attracting and encouraging innovative managers. One is to make sure that the managers have the room to innovate in what will undoubtedly remain a particularly exacting structure of accountability. The other is to have a proper idea of what it means to succeed as a government manager.

The CEG Principals who innovated in both the private and public sector enjoyed the stimulation and the freedom that they felt they had in the private sector. What gave them that opportunity was the simple fact that they could be held accountable for their performance not by clearing things in advance, but by producing results over time. They liked the clarity and focus that the "bottom-line" provided.

In contrast, it was hard to be sure that they had accomplished something valuable in the public sector. There always seemed to be doubts and debates about the value of their contributions. They could tell themselves stories about what was valuable about what they had done, but there was nothing that clearly established and broadcast their successes. Nothing "ended the discussion" conclusively. One protagonist complained that his accomplishments were known to fewer than 10 people and valued hardly at all.

When one thinks about it, there really are very few images of what it means to be a successful manager in the public sector. One image is simply that one goes on to higher jobs, and manages his career successfully. Such a trajectory may be an indication that one has done a good job. But it is also possible that such promotions indicate only powerful connections or assiduous self-promotion rather than actual

managerial accomplishments. Good managers yearn for tangible evidence of accomplishments as well as personal success.

A second more satisfactory image is of a manager who achieves particular policy or managerial objectives. He (or she) succeeds in passing some piece of legislation that embodies his (or her) policy convictions; or successfully implements a program that had been mandated; or introduces some important administrative changes that improve the operations of a public sector organization. This gets closer to a satisfactory image of success, but it has the liability that it gives managers credit for changes that are potentially too narrow, too small, or too short term. As one Principal observed, "There needs to be a more important purpose than just savaging an organization so you can make a short term hit and then go on to something else."

To be fully satisfactory, one would have to couple this definition of success with additional criteria that looked at the impact of the particular innovation introduced by an individual manager on the overall, long-run performance of the organization. This leads to a third definition of managerial success in the public sector: a successful public sector manager is one who builds an enduring, powerful organization. This seems close to the private sector ideal, since it is clear that one of the important goals of managers in the private sector is to build organizations that can survive in the market place. The difficulty with this idea in the public sector is that it is often equated with building organizations that survive because they become powerful and deeply rooted as institutions. Thus, one thinks of J. Edgar Hoover's FBI, or Hyman Rickover's nuclear program, or Robert Moses' New York Transit Authority. These organizations are envied for their stability, and their ability to achieve large purposes over a long period of time. But they are also quite properly criticized for their rigidity, and their inability to adapt to changing public sector priorities and needs.

The right idea of managerial success in the public sector may be the same as it is in the private sector. In the private sector, managerial excellence is not assessed only in terms of short-run profitability, or introducing new products successfully, or properly repositioning an organization in its market environment -- though all these things are important. The most important accomplishment of private sector managers lies in their ability to create adaptive, innovative, value-seeking organizations -- enterprises that can, on their own initiative, look for and exploit value-creating opportunities; and that can do it not just now, and every now and then, but consistently over time.

Building such organizations might be the proper goal of public sector executives as well. And if we saw the public sector as a value-creating enterprise, those who are capable of creating such organizations might turn to the public sector to set standards of excellence. That, at least, is the hope of those who see the public sector as a place where value can be created through managerial excellence.

It is a challenge that the incoming administration cannot ignore. If our new leaders do not succeed in making the government a place where initiative, creativity and managerial excellence are rewarded, its hopes for increased governmental effectiveness in dealing with urgent national problems will be dashed. On the other hand, if the Clinton administration succeeds in this, it will have taken a great step forward in dealing with today's problems and will restore the government's capacity to deal with future problems, as well.