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JOHN D. DONAHUE

Market-Based Governance and the Architecture of Accountability

ACCOUNTABILITY UNDERPINS CIVILIZATION. It defines a virtual nervous system for an interdependent community composed of discrete individuals. Separate minds conceive and carry out actions with shared consequences. Thus any prospect for something better than solitude, subjugation, or chronic conflict depends upon and has always depended upon devices for taking into account the interests of others. We manage interdependence through mechanisms of accountability.

There are a great many such mechanisms. Some (such as family, friendship, and empathy) are elemental antecedents of organized society, not its constructs. Some (such as religion) are partly constructed, partly not. Still other mechanisms of accountability are clear-cut artifacts, rather than preconditions, of civilized life. One broad model of accountability is governance—the rules and institutions for the authoritative organization of collective life. Another is the market—cooperation arising out of voluntary exchange based on individual assessments of value. Each of these generic models has taken on countless different forms through human history ranging from primitive to intricate in their construction, from crude to sophisticated in their operation, and from calamitous to triumphant in their consequences.

Governance and markets also tend (to varying degrees and with varying results) to be entangled with each other. History displays the two generic

mechanisms in a nearly infinite array of hybrids, alloys, and combinations. In this book we are concerned with one particular kind of entanglement—the use of the market as a means for pursuing the goals of governance. There is nothing new about market-based governance. When a Wall Street broker was elected mayor of Jersey City in the 1990s and launched a purportedly unprecedented tax-collecting partnership with private firms, he was merely reprising (in essence, and in many of the details) arrangements that were routine in the Roman Empire.¹ Mercenary soldiers (who kill and die for the state not out of a sense of obligation or patriotism but for a fee) antedate Rome and are with us still.

The final quarter of the twentieth century, however, was marked by a surge of experimentation with new forms of market-based governance (especially, but not only, in the English-speaking world). The administrations of Margaret Thatcher in Great Britain and Ronald Reagan in the United States provided sharply etched mileposts for the trend's early stages. Openness to market-oriented styles of governance both endured and diffused, however, until by century's end it was an unremarkable mainstream sentiment. It may have been George W. Bush (Reagan's would-be political heir) who bluntly declared that "government should be market-based," but Bill Clinton's views were only slightly less sweeping.²

This burgeoning enthusiasm for the market as a means toward public ends has two sources, each displaying both sounder and shallower manifestations. One source is the comparative performance of markets and government; the other is change in the perceived legitimacy (among both élites and the general public) of market-based arrangements. The two are related, of course, as perceptions of relative performance reshape relative legitimacy. Babe Ruth, asked why he should earn more for hitting baseballs than Herbert Hoover earned for leading the country, explained, "I had a better year than he did."³ It is hard to deny that markets have had a better half century or so than governments. In the United States and in most other Western economies, the period after World War II witnessed a preponderance of success in the market realm. Incomes rose. Wealth grew. Technology advanced. Corporations expanded and evolved.⁴

There were failures, too (and, just as important, sharply uneven rewards from market success), but compared with the first half of the century, the market stood in triumph. Over the same period, communism—perceived, fairly or not, as one extreme on a market-to-government spectrum—was unmasked as an apocalyptically bad idea. Even Western democratic governments, meanwhile, seemed plagued by scandal, sclerosis, misjudgment,

and lame performance. As trust in government decayed, the market gained legitimacy (at least in relative terms).⁵ Especially in the interval bracketed (at its start) by the fall of the Berlin Wall and (at its end) by the dot-com collapse and the September 11 attacks, the reverence for markets and disdain for collectivism that has always figured in America's *weltanschauung* was at full flood tide.

Four cautionary observations are warranted, though, before any further inquiry into the potential and limits of market-based governance. First, the lessons of the late twentieth century are considerably more complex than simply "the more market, the better." A good deal of the market's gratifying performance (in the United States and elsewhere) can be attributed to astute public policy. Government's contributions to economic success have been pervasive (if admittedly hit-and-miss), including interventions as esoteric as nurturing technological progress and fine-tuning the macroeconomy and as elementary as building roads and maintaining the rule of law. By century's end, several countries (including Russia) were demonstrating that too light a governing hand—not just too heavy—could have regrettable consequences.

Second, a prudent respect for the market can degenerate into sterile orthodoxy. Ideological fashion sometimes inspires a universal and unreflective faith in market solutions, rather like the enthusiasm for speaking French among nineteenth-century Russian aristocrats—not because of any reasoned assessment of the merits but because it has become *de rigeur* among right-thinking people. This phenomenon may have reached its apotheosis (if that is the right word) in the first of "Armey's Axioms" promulgated by Representative Dick Armey: "The market is rational and the government is dumb."⁶ When the case for market-based approaches rests on axioms rather than analysis, the conversation becomes at once dull and dangerous.

Third, turn-of-the-century enthusiasm for market approaches has been largely informed by performance on the market's home turf—the production of goods and services paid for by and tuned to the tastes of individual consumers. It requires a daunting logical leap to extend into the public realm the advantages markets display in private production. The evidence is decidedly more mixed about the merits of markets as a means to public ends—consider Nixon-era experiments with education contracting; federal sales of timber, grazing rights, and electromagnetic spectrum; or any number of sobering stories from military procurement. There are more ways to fail in the public realm or (put differently) a larger and more

demanding set of things that must go right if market means are to efficiently serve public ends.

Fourth, market ascendancy may prove fleeting. At least some of the factors behind the growing legitimacy of market solutions will turn out to be cyclical, not secular, and we may have already reached the trend's inflection point. It is too early, as of this writing, for any confident predictions about the impact of new economic tensions, the events of September 11, 2001, or Enron's abrupt implosion. Most of this book's chapters were drafted in sunnier times, and we have not asked authors to hastily speculate about the shifting context for market-based governance. There are some signs, however, of a turning tide. Railtrack, a major component of Great Britain's privatized railroad system, suffered financial collapse in 2001 and went into receivership.⁷ Airport security in the United States has been wrenched from a heavily market-based system to one closely controlled by classic instruments of governance. The American public's level of trust in government has sharply (albeit perhaps temporarily) spiked. A *Washington Post* survey taken two weeks after the attacks found that nearly two-thirds of respondents trusted "the government in Washington" to do the right thing most of the time or nearly always—more than double the levels of trust prevailing in recent years.⁸

Yet whether the reigning predisposition toward market-based approaches proves enduring or ephemeral, it is our task, as analysts of public policy, to separate the promise from the perils of market means toward public ends. How can we engineer the most favorable balance between the upside and downside of market-based governance? Which collective missions are best pursued by market means? Where, in short, does engaging the market offer the most promising blueprint for accountability in the pursuit of particular public goals? For some purchase on these questions, and as the overture to the coming chapters, consider the distinction between two dimensions of accountability, which we can label intensive and extensive.

Intensive accountability is circumscribed but concentrated—in terms of the spectrum of values that must be taken into account or the constituencies whose interests must be taken into account or both. A type specimen of intensive accountability is described, interestingly enough, in the New Testament. Jesus tells of three stewards, each entrusted with a quantity of capital to manage for their traveling master. On his return, the master demands an account of each steward's investment. The two who report healthy returns are handsomely rewarded; the last we hear of the

third involves “wailing and gnashing of teeth.”⁹ This parable illustrates a highly intensive form of accountability. There is a single entity to whom the stewards are answerable—the master. There is a single metric of accountability—return on capital. (This was a parable, not a case study, and abstracts from complications like tax treatment, environmental rules, or compliance with the Aramaeans with Disabilities Act.)

In its simplest and most stripped-down form, capitalism is constructed on this blueprint of highly intensive accountability. The metric of faithful stewardship is the growth of capital value through adroit commercial moves. The steward is answerable only to owners—and if he is the sole owner, only to himself. Success and failure are unambiguous. This clarity allows for simple, sturdy measures to manipulate agents’ motivation and to invoke whatever consequences their performance merits. Deviations—a lost contract, a surge in costs, a dip in profits, a slip in capital value—are rightly seen (absent a compelling excuse) as conclusive evidence of bad performance.

Extensive accountability, by contrast, involves multiple metrics or multiple masters or both. For an illustrative example here, consider the principal of my children’s elementary school. He is answerable to the children, to their parents, to the teachers and administrators, to the school board, the selectmen, members of the town meeting, the town manager, a large cluster of state agencies, a larger cluster of federal agencies, neighbors upset about traffic, and so on. Not all constituencies have equal standing, to be sure, nor are all goals equally important. It is reasonably clear that teaching the children well while using taxpayers’ resources efficiently is the basic idea. Notice, however, that neither of these goals—good education and parsimony—is clearly subordinate to, or instrumental of, the other. There is no simplifying story like “customer satisfaction equals shareholder value.” The mission is (at the least) bipolar, not unipolar.

Neither pole, moreover, is cleanly defined. There are many plausible versions of “teach the children well.” (Think of the trade-offs between mainstream and special-needs kids; between social and academic development; between math and reading; between kindergarten—where the leverage may be greatest—and the upper grades—where the stakes are higher.) Even if the definition of good education is reduced to standardized test scores and nothing else, it matters greatly whether the metric of success has to do with the mean, the median, or the range of student scores. Nor are taxpayers’ interests unidimensional. Some voices call for minimizing local taxes by keeping costs as low as possible; others call for maximizing property values

by maintaining excellent schools; still others play down economics and emphasize one generation's duty to the next. Meanwhile, constituencies aside from families and taxpayers—teachers, staff, public officials at local, state, and federal levels, neighbors, unions, and all the rest—cast their own interests, with a fair degree of sincerity, as instrumental to advancing some version of either, or both, of the central goals. This is not a particularly complicated example of public stewardship. Nor does the principal seem daunted by the thicket of criteria he confronts; it goes with the territory. Compared with almost any business leader running a similarly scaled operation, however, he operates within a strikingly extensive structure of accountability.

We rarely—indeed, never—encounter in practice either exclusively intensive or exclusively extensive accountability. The closest approach to a pure form of intensive accountability may be the commodities trader scrambling in the pit to get the best price for her client, and even she is bound by constraints of law and custom, must worry about her reputation and that of her firm, and cannot seek a trading advantage by slipping a stiletto into a competitor. The purest real-world example of extensive accountability may be the secretary general of the United Nations, who is answerable (at least in principle, and in a mediated way) to most people on the planet. Yet even he puts a different weight on the concerns of members of the Security Council, and he owes no allegiance to stateless people.

In a perfect world, all human relationships would feature full measures of both intensive and extensive accountability. In the same perfect world, of course, everyone would reach full wisdom in robust youth and never misplace keys. Given the imperfections of the world we inhabit, there is typically a trade-off between intensive and extensive accountability. This is not always so, of course; a truly broken structure of accountability can be made both more intensive and more extensive simultaneously. In general, however, we must be ready to sacrifice some extensive accountability to obtain more intensive accountability (and vice versa).

Intensive accountability requires sturdy measures to induce fidelity to some goals and (less obviously) also requires shields and filters that make it possible to ignore or grant lower priority to other desiderata. Extensive accountability requires, as an ineluctable entailment of multiple missions, continuous balancing of obligations and the capacity to grant something short of maximum fulfillment to any claim so as to give due weight to all. The central design challenge, for institutions of accountability, involves

this trade-off between extensiveness and intensity. Mechanisms of accountability that tilt toward extensiveness we tend to call “governance.” Mechanisms of accountability that tilt toward intensity we tend to call “markets.”

To be clear, extensiveness and intensity are only characteristic of, not exclusive to, the public and private spheres respectively. Every market institution has concerns beyond the bottom line—not just the general constraints of law, custom, and conscience but sometimes deliberately structured measures such as the “balanced scorecard,” social investment criteria, and some of the innovations discussed in this book. The public sector has pockets of accountability at least as intensive as anything in the private sector; consider, for example, the tight focus that characterizes a healthy military organization.¹⁰ Nevertheless, the statement of general tendency holds up reasonably well.

Each model of accountability can fail. A critical tradition going back at least to Adolph Berle and Gardiner Means charges that the capitalist story of intensive accountability to owners has become a sham and a shield for stewards’ self-dealing.¹¹ Similarly, an influential school of economic thought holds that breakdowns in governments’ extensive accountability are the norm, not the exception. Politicians and bureaucrats invoke obligations to Peter to evade obligations to Paul, in this argument, and exploit the confusing multiplicity of goals to dodge accountability entirely. The failure-proneness of particular structures of accountability is an important matter that arises in several chapters of this book. Beyond the debate about the probability and consequences of design failure, however—and in some ways logically prior to that debate—there is an important conversation about design fit. For each particular task, at some particular time, within some particular context, what is the best-suited structure of accountability?

“Market-based governance” can be characterized (at a high level of generalization) as engineering into public undertakings a greater degree of the intensive accountability that typifies markets. It succeeds where it makes possible a better balance of the two styles, delivering an increment of intensity without an undue sacrifice in extensiveness. This basic logic of market-based governance—surrendering some extensive accountability to gain some intensive accountability—clarifies analysts’ obsession with the precision and “tightness” of public mandates delegated to market agents. Intensive accountability is both narrow and powerful. Any uncertainty surrounding the relation between market means and public ends, any range of

discretion or ambiguity, will result, we must anticipate, in effort gravitating toward the focus of intensity—where profit is the driving motive, for example, toward higher net revenues.

This is not because market actors disdain broader goals; as individuals, they may honor other dimensions of value as much as or more than do public officials. Nor is this to predict crude opportunism in every case of discretion. Arrangements that take reputation and past performance into account can and do motivate private actors to employ discretion and resolve ambiguities in ways that are extensively accountable, even if profit is their only ultimate motive. (Such arrangements, indeed, are classic examples of good contractual architecture.) Intensive accountability, however, tends to subordinate everything—not just waste and muddle but also the personal values of agents and any dimensions of public value that are not explicitly and deliberately built into the relationship—to the pursuit of the primary goal. That is what structures of intensive accountability are *supposed* to do.

The chapters of this book explore—from varying perspectives, in varying ways, with varying alloys of generality and specificity—the merits of market-based governance. When is it advantageous to ramp up the intensity of accountability for a collective endeavor, whether by revising the structures of stewardship within the public sector or by delegating duties to agents already enmeshed in systems of intensive accountability? When can restructuring the architecture of accountability make the pursuit of public missions more flexible, or more transparent, or defter, or more parsimonious? When, conversely, is it too hard to harness the potent instruments of intensive accountability? When does a diminution of extensive accountability necessarily entail (or clearly threaten) the unwarranted surrender of shared value, masquerading as a simple shift in means?

The first cluster of chapters deals with the “demand side” of market-based governance, with issues surrounding government’s role as a customer. Karen Eggleston and Richard J. Zeckhauser set the tone with an inquiry into health care. They stipulate (for present purposes) that health care will be largely paid for collectively. The question is how it should be delivered—publicly or privately and (when private) by for-profit or non-profit suppliers. To clarify this question, they weave an analytical fugue of ideas and evidence featuring three central themes. The first is a general answer about the private sector’s proper role in delivering health care: It depends. The second is the good news: We can say, with some precision, on what it depends. The third is the bad news: There is little reason to

think we will stumble by accident onto the right pattern of market-based health care.

What makes their work both rewarding with respect to health care specifically and of more general relevance as well is their disciplined examination of incomplete contracts and their consequences. Suppose contracts were always complete—in other words, that we could routinely build structures of accountability that are at once sturdy, clear, and richly detailed, specifying the agent's duty to every legitimate stakeholder in every possible contingency. Accountability could be both fully intensive and fully extensive, with no impediments to reaping the benefits (focused incentives, competition, flexibility) of market-based delivery. As economists have long recognized, however, such complete contracts are vanishingly rare. In practice, contractual architecture (in health care and elsewhere) tends to be marred by gaps and flaws, forcing a choice between intensity and extensiveness. The crucial point, for Eggleston and Zeckhauser, is that tasks differ in both the nature and the gravity of contractual incompleteness. Providers differ, too—public, nonprofit, and for-profit institutions should vary in the way they respond to incomplete contracts. These two observations define the context for an intricate, high-stakes matching game, for which Eggleston and Zeckhauser lay out the rules.

They first review the evidence on the behavior of public, nonprofit, and for-profit health-care providers, finding it generally consistent with (but considerably less tidy than) what theory would predict. Next they elaborate their analytical framework, which hinges on the incentives hard-wired into an organization's structure by the way property rights are defined. They develop decision rules for which category of provider, and which kind of contractual structure, is the best match for particular types of functions. Their focus, significantly, is *comparative* advantage. They sidestep the fervent and murky debate about the overall role of the market in health care and anchor on a seemingly humbler but far more productive question: "In what order should services be placed in the for-profit, nonprofit, and government sectors? In theory, Republicans and Democrats, Labourites and Conservatives, Socialists and Christian Democrats should be able roughly to agree on this question, even though they might be bitterly divided on the amounts they would like to place in each of the three sectors."

Although they are fully aware that historical accidents, inertia, ideology, and the interplay of interests exercise considerable leverage over the division of labor in any health-care system, analysis plays a role as well. They distill from their analysis some quite clear-cut guidelines for matching tasks

to providers. The intensive accountability that characterizes private providers, for example, serves best for services that are readily contractible, easy to monitor, susceptible to competition and for which innovation is especially valuable. “Examples include elective surgery and most dental care, as well as the provision of drugs and many aspects of primary care.” Conversely, the extensive accountability of public (and, in some cases, non-profit) providers has a comparative advantages for services that are difficult to define in advance, offer benefits beyond those received by the patient, or have aspects of quality that are hard for patients to monitor (among other features.) Examples here include care for severe mental illness, blood banks, and long-term elder care.

Beyond the insightful observations about health care they offer, Eggleston and Zeckhauser earn the lead-off slot in this book for their elegant analytic structure, their liberating focus on comparative (rather than absolute) advantages for different delivery models, and (not the least) the accuracy and the significance of the simple sentence that ends their chapter: Although they may be derived from the health-care sector, “most of the principles set forth apply to a wide range of services.”

Peter Frumkin develops a similar theme of complexity and contingency in the proper matching of tasks to agents. His point of departure, though, is the observation that government not only selects from a roster of potential suppliers but often also powerfully shapes that roster. Frumkin’s focus is on human services, an arena in which government tends to be the dominant (and sometimes sole) source of demand. For a private firm this can be a happy position (though a tricky one to play to best advantage) as leverage over sellers leads to lower prices and other benefits. For a public sector purchaser with an extensive list of criteria for human services—including flexibility, cultural fit with client populations, reliability even when oversight is weak, and other factors beyond cost and readily defined quality measures—the right choice of providers can require thinking several steps ahead. A supplier (or set of suppliers) spurned today might not survive to be an option tomorrow; the chosen model is apt to prosper and expand.

This would be a minor matter if the right allocation of human services to public, for-profit, and nonprofit delivery was clear cut and well understood. Suppose we had a well-developed body of theory and evidence, along the lines of the Eggleston and Zeckhauser analysis of health care, offering guidelines for the proper assignment of every human service. Then the withering away of rejected models would be no loss, just healthy evolution within the organizational ecology. Frumkin suggests, however, that

the state of the art in this domain remains lamentably primitive, as “evaluation research on the comparative performance of agencies across sectors is slim and contradictory.” In many cases, he argues, we simply cannot say with much confidence which delivery model works best.

To complicate matters further, Frumkin contends, the for-profit players within the human services ecology are systematically more robust. Absent deliberate efforts to preserve the diversity of the system, he fears, nonprofits will be crowded out of many of their accustomed niches. Especially if the apparent advantages of for-profit suppliers prove illusory, a short-term focus on the part of the public purchaser risks degrading the organizational gene pool. Frumkin urges those who make decisions about the purchase of human services to maintain “an appreciation of the effects these decisions have on the long-term evolution of the ecology of service providers in the many fields of human services for which government funding represents a critical source of agency finance.”

In short, he argues, “preserving room for both nonprofit and for-profit service providers across a range of fields, at least for now, must be viewed as a managerial imperative, given the generally poor state of current knowledge.” There is a tacit subtext to this conclusion: Ignorance is expensive. The downside of an impoverished organizational ecology, and the substantial insurance premium implicit in sustaining a diversity of suppliers that may or may not turn out to be optimal, highlight the payoff to research and analysis.

The first two chapters illuminate the debate over whether and when government should opt for market-based alternatives. Steven Kelman next raises the salient but often neglected question of *how*. Delivering services directly, through the extensively accountable option of employing people and situating them in a formal government agency, imposes a fairly familiar set of public management worries. However, “though the decision to contract [for services] changes the nature of government’s worries,” Kelman warns, “it does not eliminate them.” The management of contracting relationships is a demanding and distinctive craft.

Especially for those agencies that already outsource much of their operations (including the U.S. Departments of Defense and Energy and the National Aeronautics and Space Administration), but also for any governing entity that embraces market-based demand strategies, “the ability to manage contracting must be considered a core competency.” Federal procurement reforms in the second half of the 1990s widened the range of discretion and inspired agencies to think anew about what to make and what

to buy and how to choose the best outside providers. However, “the third element of strategic contracting management, the administration of contracts once they have been signed, has been the neglected stepchild of these efforts.” Kelman’s chapter (and the larger effort from which it is drawn)¹² marks an attempt to give the neglected stepchild the attention it merits.

Kelman clears the ground by challenging the view (common among both academics and the general public) that government is peculiarly bad at managing contracts and systematically outwitted by nimbler, better-motivated private counterparts. Cost overruns in large defense projects are standard illustrations for the contention that mismanaging contracts is the norm. However, Kelman cites evidence that comparably large development projects in the private sector suffer to an equal or greater degree from cost escalation. Nor do financial data show richer returns for firms or units contracting with government, as should be the case if it were true that the public sector offers predictably easy pickings for shrewd private sellers.

Even if federal contract management is far better than the folktales suggest, according to Kelman, it is not as good as it needs to be. The implicit view that the real work of public management involves employees, not contracts, is at odds with reality in many agencies and invites a perverse underemphasis on the trade craft required to manage contracts well. Although contract management is often considered a mechanical matter to be handled by junior officials, “the most important responsibilities . . . are not just managerial in general: they are analogous to those of a senior executive, not a first-line supervisor or middle manager.” Kelman outlines a fine-grained, pragmatic agenda for upgrading the profession, organized around three kinds of reforms: “properly [defining] and [providing] training for the job, [splitting off] lower-level tasks from executive-type tasks, and [making] an investment in performance measurement as a discipline.”

From his privileged perspective as an architect of earlier rounds of federal procurement reform, Kelman argues that the changes required to render contract management an appropriately central part of strategic public management are at once necessary and feasible. He ends, though, with the cautionary note that this next stage of reform involves surmounting different kinds of hurdles. Whereas the 1990s reform campaigns “were in the first instance institutional design challenges,” reshaping the profession of contract administration, by contrast, involves “predominantly challenges of human resources management—of people and job design.” It thus requires grappling with larger issues concerning the quality, deployment, and motivation of federal personnel.

The next two chapters take up the “supply side” of market-based governance, examining unsettled questions about government’s role as a provider (rather than a purchaser) within the market system. Georges de Menil considers the balance between market and government in ensuring adequate retirement income. This is by no means a neglected topic—oceans of ink have been spilled on the subject in recent years, along with no small quantity of vitriol—but it remains far from settled. Although he does not expect to still the debate, de Menil calmly sorts out the arguments and sets them in historical and international context.

He starts by calibrating the stakes. If accountability, generically, is civilization’s underpinning, the duties owed to the aged are among the most salient specific forms: “The provision of old age security is, like the organization of exchange or the maintenance of law and order, one of society’s central functions. . . . A community in which the young were structurally incapable of providing for their old age, and the old were regularly abandoned by the collectivity, would be unlikely to survive for long.” Yet in principle, at least, there is an abundance of alternative formulas for old-age income security, with all-but-infinitely varying alloys of traditional governance and market-based means. In practice, a healthy fraction of those imaginable alternatives have been tried at some time and in some place.

The chapter begins with an overview of the history of old-age income practices in the United States and Western Europe, tracing the origins of what developed into the rival paradigms of individual insurance through the market versus collective provision through government. Next, de Menil provides a compressed but illuminating summary of the logic by which the two paradigms can be assessed. Finally, he surveys recent experience with altered blueprints for old-age income security in both developed and developing countries. He ends with cautious optimism about an emerging synthesis of market and governance, while underscoring the need for both deftly designed transactional architecture and difficult political choices for any community considering such an approach.

Information is a special kind of commodity. Whatever effort may be entailed in generating a piece of information, the incremental cost of disseminating it to an additional person—its marginal unit cost—tends to be low. One person’s possession of a bit of data, moreover, does not diminish its value for any other possessor (with exceptions that include competitive or strategic data). Indeed, information often grows in value as it is shared (think of technical standards, or product ratings). For these and other reasons, economists have generally looked more benignly on public provision

of information than on other cases of governmental supply. Information about the law is a special case of the special case, because its wide dissemination is not just desirable but essential to almost any definition of accountable governance. Unless those who are subject to the law are well informed about their obligations, Frederick Schauer and Virginia Wise suggest, “there is perhaps no law at all.” A naive observer, then, might predict a dominant role for formal government in the supply of legal information. Yet, at least with respect to the United States, that naive observer would guess wrong. Government turns out to be a secondary and shrinking player in the market for legal information. Schauer and Wise probe the reasons for this curious fact and assess its implications.

They trace the shifting mix over time of public and private supply. During a century or so of parallel provision, both supply channels for legal information flowed briskly. Official alternatives tended to be cheaper; private alternatives tended to be more artfully organized. The private advantage in value-added information services gradually widened, as the proprietary organizing scheme of the leading commercial purveyor became the de facto standard for citations and legal education. As the private channel grew dominant, the public channel of supply dried up for many types of data. Much legal information can no longer be obtained—either in a convenient form or at all—from government, and three foreign corporations dominate the U.S. market for legal data.

The government’s retreat from the supply of legal information could be a harmless curiosity, rather than a source of anxiety. Schauer and Wise suggest several reasons—some straightforward, and others quite subtle—for concern, however. The market power of a concentrated industry implies the risk of costs that are higher, or product offerings that are less finely tuned to users’ preferences, than the competitive market ideal. Beyond this generic defect of concentrated markets is the fact that “the bundling of legal information to make it available to users reflects the financial incentives and internal structures” of the private suppliers. The most widely used data on American court rulings comes in separate packages for each of seven geographic regions, in an accidental artifact of decisions made long ago by an early market leader. Evidence assembled by Schauer and Wise hints that this bundling affects how the law works and how it evolves. For example, because “when seen from California, Kansas and Nebraska are quite legally similar, there appears a substantial possibility that the bundling of opinions from Kansas but not from Nebraska courts within

the set of law books that most California lawyers and judges own may have played a significant role” in Californians’ disproportionate reference to Kansas precedent.

Similarly, legal publishers increasingly bundle legal information with other product lines offered by their conglomerate parents. Schauer and Wise find reason to believe that this has promoted the “substitution of nonlegal secondary information for legal secondary information, a substitution that has potentially profound implications for the nature of legal education, the nature of legal argument, the nature of legal practice, and the nature of law itself.”

The tilt toward market supply has occurred with remarkably little analysis or controversy. At one level, this shift can be seen as simply one more example of the emergence through evolution of the lowest-cost, best-performing supply model—the sifting and sorting that market economies do so well. However, if “legal information is best seen as constituting law rather than just describing it,” Schauer and Wise suggest, “a transformation that on its face may have looked technical and inconsequential” may be quietly reshaping something quite central to governance.

The third cluster of chapters explores experiments with market-based arrangements for orchestrating accountability outside government by altering the incentives that operate inside market institutions. Archon Fung starts the section with a provocative topic—the prospects for rendering commerce itself more extensively accountable through the creation of “social markets.” This term simply refers to market settings in which investors and consumers apply their social values to the choices they make. “To the extent that consumption and investment decisions depend not only on preferences about the price, quality, or features of products or about the risk and return characteristics of securities but also on preferences about the labor and environmental consequences of production processes and corporate policies, social values become important components of economic markets.” In such settings, “corporate officers must advance notions of social responsibility in order to make money for their shareholders.” The goals conventionally pursued by authoritative mandates and regulation may thus be advanced by utterly different means, in a marriage of intensive and extensive accountability.

Fung urges both openness to the potential value of such approaches and alertness to their characteristic risks and limits. To serve both ends, he starts by describing the ideal of social markets in a counterfactually transparent

and orderly world. He then gradually backs away from the ideal and toward the messy realities of our own world, gaining perspective (at the price of complexity) with each step. This method lets him distinguish accidental defects of social markets that can, in principle, be remedied from their fundamental drawbacks, including the generalization that “wealthy consumers will have more voice than poor ones.” Once his conceptual lens is ground, Fung applies it to some of the evidence on emerging social markets. These include a range of initiatives, both organized and diffuse, to promote “ethical consumerism.” They include as well the attempts of some corporations to portray themselves (on capital markets or consumer markets or both) as differentially attentive to particular social concerns. They include efforts to organize associations of firms pledging allegiance to explicit codes of conduct that serve as clear and coherent signals of their social practices. They include as well deliberate moves by policymakers to structure and catalyze social markets as adjuncts or alternatives to more conventional regulation.

Fung notes that social markets are still in their infancy, and he synthesizes from his chapter three criteria to guide their growth. Social markets offer a particularly promising blueprint for accountability when public sentiment is reasonably coherent; when firms are sufficiently vulnerable to diffuse public preferences; and where conventional alternatives—authoritative incentives, mandates, and regulation—are comparatively weak. Without suggesting that social markets will (or should) sweep away more traditional methods for engineering extensive accountability into the market realm, Fung predicts that they will remain an area of lively innovation in market-based governance.

It was only in the final decade or so of the twentieth century that a market-based approach to environmental protection made its break from the world of abstract theory to become a practical bipartisan policy initiative in the United States. Robert Stavins, an intellectual midwife of this movement, observes that “as more and more market-based environmental policy instruments have been proposed and implemented, the concept of harnessing market forces to protect the environment has evolved from political anathema to political correctness.” He marks the highlights of this transformation and extracts the main lessons.

Market-based approaches to environmental policy deploy a range of devices including tradable permits (which incorporate into firms’ production costs a price for harmful emissions) and pollution charges that use

fees (rather than fiats) to discourage environmental damage. When these and similar instruments “are well designed and implemented, they encourage firms or individuals to undertake pollution control efforts that are in their own interests and that collectively meet policy goals.” The traditional “command-and-control” approach, by contrast, overlays onto conventional market motives a separate structure of public accountability that is in tension with, rather than integrated into, firms’ economic incentives. Stavins distills from his long experience as an analyst and advocate some hard-won and quite specific lessons about the advantages of market-based alternatives (and how to recognize and reap those advantages) in particular environmental policy settings.

Stavins then broadens the frame to take in the “positive political economy” puzzle of why the breakthrough on market-based environmental policy approaches occurred in the late twentieth century (instead of earlier, or not at all). The defects of command-and-control regulation, after all—irrational uniformity, uneven and often random relationships between the costs and benefits of particular protective measures, rigidity, weak or even perverse incentives for firms to extend the technological frontier for clean production—had long been recognized. Why, before 1988, had these been seen by everyone except a few economists as an unavoidable and acceptable price to be paid for sound environmental stewardship? Why, by century’s end, had the notion of doing better through market-based approaches become a new orthodoxy (albeit still not the norm in practice)?

Stavins describes a stable though suboptimal equilibrium, lasting from the surge of new environmental laws in the 1970s to the end of the 1980s, in which “command-and-control instruments have dominated because all of the main parties involved—affected firms, environmental advocacy groups, organized labor, legislators, and bureaucrats—have had reasons to favor them.” What disrupted that equilibrium, he suggests, was not (as scholars might fondly dream) an improvement in prevailing levels of conceptual sophistication among practitioners. Stavins advances as a “refutable hypothesis” that a study of shifting views on market-based instruments among relevant congressional staffers over the past twenty years “would find increased support from Republicans and greatly increased support from Democrats but insufficient improvements in understanding to explain these changes.” Instead, he attributes the shift to rising regulatory costs, the embrace of market approaches by a few pioneering environmental advocates (inspired in part by initiatives that clearly cast market-based

tools as ways to reduce pollution), and the emergence of previously uncontrolled pollution challenges—including sulfur dioxide and chlorofluorocarbons—where there was no command-and-control status quo to overcome. He also describes the ideological equivalent of slow tectonic shifts, as markets generally rose in public favor. Finally, “a healthy dose of chance” placed a few open-minded incumbents into key policy positions.

Yet the environmental area, he suggests, does afford a heartening case in which analysis and evidence have won a round against inertia and orthodoxy. “There is clearly no policy panacea,” he concludes, in words that could be inserted into every chapter of this book. Rather, “the real challenge for bureaucrats, elected officials, and other participants in the environmental policy process comes in analyzing and then selecting the best instrument for each situation that arises.”

Cary Coglianese and David Lazer follow with a related inquiry into melding extensive accountability onto the market motivations of private actors. They offer an account of a class of innovations they term “management-based regulation.” This approach is generically distinct from conventional regulation in that it eschews the imposition of specific obligations and instead requires firms “to engage in the planning and decisionmaking required to identify both technologies and performance targets needed to achieve socially desired goals.” They identify the potential advantages of this approach: it situates “regulatory decisionmaking at the level at which the most information about processes and potential control methods is available.” If firms believe their own standards are more “reasonable and legitimate” than external mandates, they may be “less resistant to compliance.” Not least important, “by giving firms flexibility to create their own regulatory approaches, management-based approaches can promote innovation and social learning.”

Coglianese and Lazer dodge the sterile debate over whether this approach is superior or hazardous *in general* and structure an exploration of the conditions under which such a regulatory strategy makes sense. Their prudent starting point is “not always.” Performance-based regulation, which mandates some particular result, “dominates the alternatives” when it is easy to measure those results. Technology-based regulation, which mandates some particular means, is indicated when “the regulated sector is homogeneous” and it is possible to develop “a technological standard based on ‘best practices.’” The most promising domain for management-based regulation covers cases for which there is a “general understanding of how to achieve social objectives, but the appropriate response in par-

ticular situations depends on contextual factors.” Here there is no substitute for managers’ intimate understanding of their own operations and a high payoff from enlisting managers’ aid in drafting the terms of their broader accountability.

Eliciting candor and ensuring fidelity when the managerial imperatives of extensive and intensive accountability collide, of course, present serious challenges. Coglianese and Lazer move to a rigorous review of the conditions that must hold for management-based regulation to succeed in practice. They then illustrate their model by showing how those conditions have held tolerably well in an important and otherwise troublesome regulatory area: food safety. The dispersed and diverse food industry is ill suited to either technological or performance standards. Recognizing this, food safety experts in government and industry quietly improvised what came to be called the Hazards Analysis and Critical Control Points system. This system, which has been used for decades but became mandatory (in the United States) only in the 1990s, features “mandates that require firms to evaluate, monitor, and control potential dangers in the food-handling process.” Coglianese and Lazer document the respectable, though incomplete, accomplishments of this prototypical management-based regulatory approach.

They reach an appropriately nuanced conclusion: Management-based strategies “still require a governmental enforcement presence to ensure that firms conduct the necessary planning and implement their plans effectively.” Even so, these strategies appear particularly suited to a number of increasingly salient issues, including “worker fatigue, chemical accidents, ergonomic injuries, and contamination of food.” Coglianese and Lazer stress that even if “management-based regulation proves to be only an imperfect strategy, it may well be useful to remember that the alternatives . . . have imperfections of their own.” The emerging management-based model, in short, “increasingly competes in the regulatory toolbox with technology-based and performance-based” approaches. Regulating well is not easy; aligning extensive with intensive accountability is an endlessly diverse challenge; expanding the regulatory repertoire is generally good news.

The final set of chapters examines the upside and downside of market-based governance. Elaine Ciulla Kamarck leads off with an enthusiastic, though not indiscriminating, overview of transformations under way in the governance zeitgeist. She samples particularly telling instances of a global “revolt against bureaucracy” that dominated the final quarter of the

twentieth century. These include the repudiation of “big government” not just by the American Democrat Bill Clinton and the British Labourite Tony Blair but also, to take just some of the cases she cites, by former (and even current) Marxists in the developing world.

Kamarck distinguishes three subspecies of new-style government, each one a bit more distant than the last from the classic midcentury model. The first is “entrepreneurial government,” in which familiar structures remain in place but practices are radically altered. “Entrepreneurial governments go out of their way to hide the fact that they are government organizations, and for that reason they are the last, best hope of the traditional public sector.” Next is “networked government,” in which “the formal state is but one actor in an informal network of organizations.” The other nodes in the network can include for-profit firms, structured non-profit organizations, interest groups, governments at different levels or in different countries, trade associations, ad hoc clusters of civic concerns and energies, and a dizzying range of other entities. Formal government may have a privileged role in setting the agenda and providing funding for a particular mission (easing the transition from welfare to work, say), but it is not, in any familiar sense, in control of the network. The third variant, and the sharpest departure from the classic model, is “market government.” This model “operates with almost no government as we know it.” The function of formal authority is “to place costs on things that contribute—positively or negatively—to the public good,” then step back and let the market do the rest. Here (to use the terminology of this introduction) extensive accountability has no visible presence at all but operates solely through manipulating the terms of intensive accountability.

Kamarck offers a rich menu of examples of each model’s application in settings around the world. She sketches some principles to mark the most promising terrain for each of the three. She turns to the public-management literature to underscore the risks and limitations of such startlingly heterodox approaches to governance. Although Kamarck may be a Ph.D. political scientist, she is also a savvy and scarred veteran of real-world policymaking at the very highest levels. She has learned that a pungent sound bite can trump a penetrating study. So she urges her scholarly colleagues to continue their efforts to deepen our understanding of the downside of market-based governance. She puts them on notice, however, that (incomplete research notwithstanding) “the capacity of these new forms of government to answer public needs while continuing to shrink

the size of the state will make experimentation with them irresistible for politicians.”

In the following chapter, my contribution to this volume, I consider the implications of market-based reforms for the governmental workforce. I suggest that the application of criteria discussed elsewhere (in this book and in my previous work)¹³ are likely to yield a reasonably long list of collective functions that could be shifted out of formal government. What would this imply for public workers? Should employees’ interests have standing in the debate over market-based governance?

Plumbing a range of data sources and employing several different metrics, I show that, contrary to the perception of rampant outsourcing common among both critics and advocates, government employment has by no means withered away in the United States. Market-based approaches, so far, have only nibbled at the edges of the conventional model of public workers delivering public services. By the most comprehensive available metric, “at century’s end as at midcentury, roughly two-thirds of the government’s work was still being done by public employees.” There have clearly been instances of aggressive market-based reforms, but even in the aggregate they fall short, so far, of a revolution in governance. A fundamental shift in the means by which public missions are pursued, then, “is not a *fait accompli* to be accommodated” but rather “a choice to be weighed.”

The choice matters, I argue, because government jobs are distinctive. The research literature suggests that America’s public sector has resisted the broader economy’s tilt, during recent decades, toward relentless meritocracy. This means that though “public service may be financially unattractive to élites, it is quite the opposite for many workers who lack the high-level skills that the private economy increasingly rewards and demands.” So a major shift toward market-style public management and market-based supply would at once widen government’s access to top talent and squeeze the less-skilled workers sheltering in public jobs from an inhospitable economic climate.

I admit to “a quite uncomfortable degree of ambivalence” about this prospect. Income disparities may be corroding Americans’ sense of commonwealth; but the public payroll is an exceedingly clumsy weapon against economic inequality. Denying other citizens the advantages they might reap from market-based reforms, moreover, is hard to justify in the name of protecting the interests of government workers. I present a few

recommendations for softening the conflict but conclude that inequality must be confronted economy-wide rather than by fighting a rearguard campaign through public employment. “So long as labor policy remains the tacit subtext of the debate, . . . it will be hard to think clearly, or to talk honestly, about market-based government.”

Whereas I am at least implicitly sanguine—labor’s stakes aside—that some significant common missions can be better pursued through market means, Mark Moore’s misgivings are more fundamental. Governance and the market, he suggests, hinge on models of accountability that are more profoundly distinctive than is commonly recognized, and attempts to breed market traits into public management carry hidden hazards.

Moore starts with a challenge to the reigning enthusiasm for making “customer service” a watchword for improving governance. The idea of a customer is not merely an imperfect metaphor for the citizen’s relationship to government, it is a perniciously illusory one. Those positioned “at the tail end of the production process” in the public sector, analogous to the customer’s position in the private sector, seldom pay all costs of the services they receive; they have no legitimate monopoly on the criteria by which services are assessed; and they receive obligations and sanctions as well as benefits. Although there are cases in which citizens are, in essence, government’s customers and in which good customer service entails real public value, Moore argues that these cases are by no means typical, and the term is mischievously misleading.

Similarly, Moore rejects the idea that good governance can or should be guided by a single bottom line. His objections here go beyond the common observation that government’s goals are hard to measure; they are similar to (but deeper than) the notion of extensive accountability employed in this chapter. Financial measures are irredeemably flawed gauges of net value-added for government; nor is it logically (let alone practically) possible to define any other unidimensional metric. There is no alternative to basing both public management and public decisions on “multiple measures covering costs, processes, and outputs as well as outcomes.”

Finally, Moore takes up issues raised by outsourcing public tasks to private suppliers. Previous work on the topic stresses that sound privatization decisions require (among other things) that the work to be done can be clearly defined. In the public realm, however, as Moore observes, this is an exceedingly tall order. It has always been “difficult for a collective to reach agreement about the precise attributes of public value that it wants to see produced.” To suggest that privatization might boost performance, once

goals have been specified, is to shirk the real work, Moore contends. “The problem in government management continues to be the difficulty of organizing politics to give a clear mandate of what is to be produced.” Debates over means, he suggests, are both simpler than and inherently subordinate to this core challenge of defining public value.

The conversation about market-based governance (unlike the conversation about markets, *not* government) occurs chiefly among people who endorse a relatively ambitious definition of the public purpose. Their openness to market means is instrumental rather than fundamental—a tactic for improving the performance of public work and restoring citizens’ confidence that common goals can be pursued effectively. Robert Behn’s chapter both honors the appeal of this logic and highlights its hazards. “One of the implicit promises of market-based governance is that it will not only directly improve the performance of government but also, as a result, indirectly improve the public’s trust of government.” He sets about assessing what needs to occur for this sequence—market-based reforms improving performance, better performance increasing trust—to work out in practice.

First, he observes that there are at least four distinguishable grounds for distrust of government: corruption, abuse, flawed choices, and poor performance. Behn explores each of these and contends that they are separate indictments, not just different manifestations of an underlying disaffection. Market-based reforms, even at their best, have leverage against only part of citizens’ complaints.

Even if we were convinced that perceived performance shortfalls were the most important explanation for distrust of government, Behn warns, public perceptions of performance are loosely linked to actual performance. So market-based reforms could boost the effectiveness with which public work is done and still have only a delayed and diluted impact on perceived performance. Moreover, performance gains achieved through market means may be viewed not as a victory for government but as the practical admission of its weakness.

Yet though Behn urges us “to be a little less giddy about what improved performance can do for public trust,” he concludes by endorsing well-considered market-based reforms (along with any other promising strategies for boosting performance)—but with realistic expectations about the payoff in citizens’ esteem.

Behn’s themes provide the appropriate segue to what is as close to a concluding lesson as can be distilled from so diverse a set of perspectives on so sprawling a topic: It would be irresponsible to squander any opportunity

for using market mechanisms to expand the repertoire by which, and to improve the efficiency with which, the work of governance gets done. This admonition applies with special force to those committed to an expansive collective agenda, however wary they may be about market solutions. It would be equally irresponsible to ignore the risk that market-based governance can distort public missions or introduce its own brand of waste into public undertakings. *This* admonition applies with special force to those concerned about operational efficiency and the integrity of public choice, however inclined they may be to look with favor on market principles.

Analysts of public policy have a responsibility to help society economize, insofar as it can, on learning by trial and error. Experimenting with alternative architectures of accountability to find out which stand, which collapse, and which warp common work in unpredicted ways can be an effective means of gaining wisdom, but often it is an expensive and traumatic one. By assessing evidence from analogous efforts, extrapolating from past experience, and thinking through the likely trajectory of alternatives still untried, analysts can narrow the range of alternatives that must be tested out in real life, with the fates of real people at stake. This is a duty that the authors of the chapters assembled here clearly recognize and admirably fulfill.

Notes

1. The tax-lien sale plan engineered by Mayor Bret D. Schundler is described in David M. Halbfinger, "Schundler's Record in Running Jersey City," *New York Times*, October 19, 2001, p. A17.

2. Office of Management and Budget, *The President's Management Agenda* (Executive Office of the President, August 2001), p. 17.

3. This quotation appears (among other places) in the *Baseball Almanac*, online version (www.baseball-almanac.com/quotes/quoruth.shtml [October 15, 2001]).

4. John D. Donahue and Joseph S. Nye Jr., eds., *Governance amid Bigger, Better Markets* (Brookings, 2001).

5. Joseph S. Nye, Philip D. Zelikow, and David C. King, eds., *Why People Don't Trust Government* (Harvard University Press, 1997).

6. "Armeys's Axioms," from homepage of Representative Richard Armeys (R-Tex. 26th) (armey.house.gov/axioms.htm [November 14, 2001]).

7. Juliette Jowit, "How the Rail Privatisation Experience Went Wrong" *Financial Times*, October 7, 2001.

8. The *Post* results for September 2001, April 2000, and February 1999—as well as longer time series for comparable, though not identical, questions—are from the *Polling Report* website (www.pollingreport.com/institut.htm#Government [November 16, 2001]).

9. Matt. 25:14–30.

10. See David S. C. Chu and John P. White, “Ensuring Quality People in Defense,” in Ashton B. Carter and John P. White, eds., *Keeping the Edge: Managing Defense for the Future* (Cambridge: MIT Press, 2000).

11. Adolph A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* (New York: Macmillan, 1933).

12. Steven Kelman, “Remaking Federal Procurement,” Working Paper 3 (Cambridge, Mass.: Harvard University, John F. Kennedy School of Government, Visions of Governance for the Twenty-First Century Project, July 2001).

13. John D. Donahue, *The Privatization Decision: Public Ends, Private Means* (Basic Books, 1989).

