A CCAF DISCUSSION PAPER

# TAKING CHANCES

## FINDING WAYS TO EMBRACE INNOVATION, RISK AND CONTROL IN PUBLIC SECTOR ORGANIZATIONS

A SET OF FIVE MANAGEMENT PRINCIPLES AND GUIDANCE FOR PUBLIC SECTOR MANAGERS, AUDITORS AND LEGISLATORS

CCAF-FCVI INC

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### A SET OF FIVE MANAGEMENT PRINCIPLES AND GUIDANCE FOR PUBLIC SECTOR MANAGERS, AUDITORS AND LEGISLATORS

*This is a discussion document, still in draft form. It is being developed as part of a three-year research project by the CCAF in close consultation with public sector managers, auditors and legislators across Canada.*

*CCAF looks forward to further discussion and refinement of the five principles and guidance in a series of meetings and focus groups to be held across Canada in 2009. The aim is to put this material to the test, so that it may be improved by the practical experience of a wide variety of public sector officials.*

*This document will be published by CCAF in final form in 2009 following these extensive consultations. CCAF also intends to develop and publish supporting tools for managers, auditors and legislators, beginning with a set of national and international case studies linked to the principles.*

*All advice is welcome and may be provided to Lee McCormack, CCAF Director of Research at lmccormack@ccaf-fcvi.com or at 613 241-6713 (ext 227).*

CCAF-FCVI INC

# Executive Summary

Changes in technology, in the complexity of work, and in citizens' expectations for better service put a premium on innovation as a way to improve the efficiency and effectiveness of operations. But public sector innovation (which relies on incentives, sound control and trust) can be difficult to promote in an environment that tends to shun risk, rather than embrace and manage it.

A public entity that fears risk is prone to creating new administrative rules, "just to be safe." But over time, administrative rules focusing on the prevention, detection and correction of possible problems can overlap without reference to whether the underlying causes of the problem are well understood, whether risks continue to exist, or whether the rules work at cross-purposes.

At a certain point – as compliance consumes increasing attention – sound management control can be compromised and sensible discretion and innovation can be inhibited.

Control, a core element of management, can be thought of as any action, procedure or process aimed at containing a risk to an acceptable level, or increasing the probability of a desired outcome. But control is not about using process as a replacement for common sense – it is about stewardship of resources, applying restrictive rules only where they are justified, and promoting innovation to improve the efficiency and effectiveness of operations. Public sector control restricts discretion in that it protects against unwanted events such as waste, non-compliance with authority or fraud. When it is well designed and sensibly applied, control sets the context in which employees can test innovative ideas and achieve their objectives.

**This document sets out five principles intended to support public sector managers, auditors and legislators in a common purpose: the application of sound management practices in the related areas of innovation, risk management and control. CCAF believes that common understandings and expectations can support more constructive and trust-based working relationships across public organizations. When managers, auditors and legislators share reasonable expectations for the management of difficult areas, friction is reduced, management practices and controls are improved and government entities are able to deliver better results for citizens.**

## Principle One: Management should ensure that innovation is led and encouraged, and that barriers to innovation are removed

*Organizations should sustain an environment where employees are encouraged to take initiative; where the basic skills of innovative practice are taught and supported; where legitimate mistakes are not sanctioned but learned from; where success is rewarded; and where blame is restricted to cases of incompetence, imprudence or malfeasance.*

Innovation is the creative generation and application of new ideas to achieve a significant improvement in a product, program, process, structure or policy. Innovation is about taking creative ideas and combining them with initiative and resourcefulness, to make them work. [1]

The combination of a lack of knowledge, incentives and skills can severely hinder the innovation process. It is rarely sufficient in the public sector to permit innovation – rather it must be persistently encouraged, resourced and pursued.

Creativity can only be translated into innovation when trust exists between the project manager and employees – and between the manager and senior governing authorities in the entity. The foundation for building trust is the application of sound management practice and accountability on all innovative projects. Still, this is not enough. Managers, staff and executive committees must also recognize that even when innovative projects are well managed, some will inevitably fail to achieve hoped-for results. Innovation therefore depends on finding the right balance or tolerance between risk-aversion and risk-taking, and ensuring that there is a common understanding of where that comfort zone is.

Barriers to innovation in the public sector can include:

- Delivery pressures and administrative burdens
- Short-term budgets, planning horizons and human resources
- Poor rewards and incentives
- Culture of risk aversion
- Poor skills in innovative project management
- Reluctance to close down failing programs or organizations.

These barriers can be overcome when values, incentives, leadership and other enablers are aligned in support of managed innovation. Some managers are more adept at introducing and supporting innovation than are others. Innovation champions are those who view their role broadly and have a good sense of the issues that affect their organization. They can convey belief in and enthusiasm about the proposed innovation, they have strategic and relational knowledge and they are able to enlist the support and involvement of stakeholders. Innovative managers use both internal and external people to scout for ideas and apply formal and informal selling channels. Finally they tend to see new ideas as opportunities and not as threats.

Each stage of the innovation cycle requires a different set of skills. As ideas are generated, managers need to understand the demands of citizens using a variety of applied science, modeling and "what if" scenario building. They should be able to learn by listening to their clients and partners. When projects move into the design and application stages, the required skills begin to include leadership and vision, building innovative networks, and expanding one's understanding of organizational culture, structure and dynamics. Project planning and risk management skills are also crucial. When innovation is being diffused, additional skills come to the fore – diplomacy and persuasion, communication and marketing (including social marketing), creating conditions for uptake, and project evaluation to identify and measure success.

It is inevitable that errors or unintended impacts will occur in innovative projects. When they do, organizations should be able to tolerate mistakes or adverse results, provided that the risk taken is shown to have been reasonable and the management of the risk was sound. Managers, auditors and elected officials alike should be prepared to accept that some well-controlled projects will fail – and when they do, the object is not to sanction the project manager but to ensure that learning occurs and is shared widely.

## Principle Two: Innovative projects must be well controlled and managed

*Creative ideas can come from anywhere in the organization but moving from the "raw idea" to the "implemented idea" stage does not happen by chance. Managers should be given the flexibility they need to test new ideas, provided that risks are considered in advance, and their projects are managed in a disciplined, accountable manner.*

Creative ideas cannot be translated into innovation unless there is trust between the project manager and employees, and between the manager and senior governing authorities. The foundation for this trust is sound management practice and accountability.

Bringing a creative idea to a practical result requires sound project management, something that does not happen by accident. There are several attributes of a properly controlled innovative project. Senior management must be made aware of the initiative at the front end and must support an adequately resourced project plan. An assessment of the risks must be made and the probability and possible consequences of failure understood. Remedial actions in the event of a failure must be considered and accepted by management at the outset of the project. Management must monitor progress. And senior management must offer sufficient authority to allow the taking of responsible chances – this may mean loosening rules to allow experimentation over the course of the project.

Underlying all this, participants must enter the project with the idea that there are no absolute successes or failures – the objective is to learn how to improve efficiency and effectiveness – to get better results for citizens. Unexpected results are inevitable and should be treated as a source of learning. Similarly, both successes and failures should be explained and defended by executive managers when they appear in front of accountability bodies.[2]

In the end, innovative managers and employees should be rewarded, whether the project was a "success" or not, provided that they played by these rules, controlled the project in a responsible way and communicated project learning throughout the organization.

## PRINCIPLE THREE: MANAGEMENT SHOULD INVEST IN A RISK-SMART CULTURE THAT CAN ACT ON OPPORTUNITY

*Organizations should develop the capacity to assess and act on risks and opportunities in order to better design their administrative rules, support innovation in the workplace, and achieve their objectives.*

A well-managed public sector organization should be able to identify uncertainties – both their potential likelihood and impact – and use this knowledge to support innovative behaviour and restrict administrative rules to those that are clearly necessary.

Risk management can allow an entity to constrain threats to acceptable levels, to reduce administrative rules to those that are necessary, and to take informed decisions on opportunities to innovate.

Public sector culture (the values, ethics, norms and training that underpin action) is risk averse. There are few obvious incentives to take risks and managers tend to associate risk taking with the possibility of something going wrong, of project failure or of financial loss. Cultural change begins with people and no entity can move from a risk-averse to a risk-smart culture without supporting its employees. Ideally, employees would have access to the training, tools, information and encouragement necessary to support change.

In a risk-smart organization, rule makers are able to move the balance from hard to soft controls because employees are competent – learning plans are resourced and implemented, key positions and activities have been identified, risks are understood and linked to rules, and sufficient back-up exists. In other words, the organization has strong resilience and capacity, and a control environment that makes sense in terms of risk.

## PRINCIPLE FOUR: MANAGEMENT SHOULD ELIMINATE UNNECESSARY ADMINISTRATIVE RULES AND CHALLENGE THE CREATION OF NEW ONES

*Administrative rules should be integrated, clear as to purpose and linked to risk. To support innovation and improved efficiency, public sector officials should review existing rules to modify those that no longer have a justifiable purpose, or whose burden is disproportionate to risk. To further limit red tape, proposed new rules should be challenged before going into place – they should be calibrated to risk, and promised benefits should clearly exceed expected costs.*

Whether a rule emanates from a central agency or originates within a ministry, management should communicate what the rule or control instrument aims to achieve, why it is in place, to whom it applies and what needs to be done by employees. Rules should be presented in an integrated manner that shows how the organization's controls fit together or interrelate.

Where administrative rules exist, they should be meaningful – that is, their purpose should be understood and undeniable. Meaningful rules are those that support democratic, professional, ethical, and people values and the underlying aims of fairness, propriety and sound stewardship of public funds.

Any control instrument creates many related activities, few of which are ever identified, or costed, by those who impose them. Control activities for any one instrument may include observing, comparing, approving, reporting, coordinating, checking, analyzing, authorizing, reconciling, supervising, reviewing, segregating and following up.

When control instruments proliferate, the ratio of activities to instruments (many activities for each instrument) can lead to an exponential increase in administrative workload and cost. The sheer volume of control activities can become a major impediment to innovative practice.

A reduction in hard controls should never become an absolute objective. In judging where best to aim on the checking-trusting spectrum, managers should carefully consider the overall ethical behaviour and capacity in the organization. Where management capacity is strong and ethics are reinforced, operational risk is generally low – and management can safely reduce control activities. Where capacity is weak, safe opportunities to strip away controls are diminished.

Tailored rules give operational discretion to well managed entities, but this authority must be warranted. Tailored rules imply the issuance of principle-based administrative policies that allow levels of local discretion to vary, based on management capacity and risk.

Organizations wishing to weed out and tailor their existing rules should focus on areas of greatest return. Care should be taken to ensure that the costs associated with any review process are reasonable and containable, that those involved in the work do not have this responsibility added to their existing workload, and that early successes in reducing administrative burdens are well communicated to all staff.

Best opportunities are likely to be found in rules that have a significant impact on many, or all, units in the organization. Middle managers and employees have an intuitive sense of where these opportunities lie, and they are often prepared to share their views. Senior management should seek their input.

New administrative rules should only be introduced where they have been considered by a body able to assess overall potential impacts. New administrative rules only make sense when calibrated to an identified and ongoing risk. If a clear relationship between risk and a proposed control measure cannot be demonstrated, it is likely that the rule should not be put into place.

It is counterproductive to implement new rules without identifying the potential costs. Compliance costs include the administrative and paperwork requirements associated with meeting a rule plus other matters such as equipment purchases, training, and the development and implementation of new information technology and reporting systems. To obtain a true picture of the potential costs and benefits of a proposed rule, managers should consult stakeholders, particularly those people most likely to be impacted by the new control.

## Principle Five: Management and staff must respect the rules that exist

*Managers and employees should respect the organization's control framework and follow its rules – and there should be well-understood consequences if this does not occur.*

The solution to broken rules is not introducing new ones – it is making sure that the existing rules are well designed, understood and respected.

In a well-managed public sector organization the consequences of non-compliance are clear and proportionate with risk and context. Managers ensure that violations of core policies, procedures and codes of conduct are documented and investigated, and that prompt remedial action is taken.

Respect for the control framework is the only way to ensure sound stewardship of resources, the single most important determinant of public confidence and trust.

**CCAF intends to test these five principles and their associated guidance in jurisdictions across Canada over the course of 2009 and plans to issue a number of tools aimed at helping managers and auditors to apply the principles, in a practical way, in their daily work.**

# Introduction

Public institutions are critical to Canada's well being and must be managed in a sound and professional manner.

Citizens expect public entities to respond competently to social and economic problems. But effective policy and program responses are difficult when the vertical authorities of public organizations (each entity has its own domain) conflict with a need to work seamlessly across jurisdictions. Although some entities can deliver cost-effective services through storefronts, self-serve kiosks and the Internet – and routinely operate across boundaries – many cannot. Compounding this, the reach of new technologies and access to information laws mean that some citizens now expect to be more engaged in the design, delivery and improvement of policies and programs that affect their lives. This is a new frontier.

**These factors refocus traditional public management and put a premium on innovation as a way to improve efficiency and effectiveness.** But innovation (which relies on incentives, sensible project control and trust) can be difficult to promote in an environment that tends to shun risk, rather than embrace and manage it. Few managers are prepared to take risks when the failure to always achieve expected results is viewed as a black mark and the rewards for successful innovation are often not apparent.

**Through this document, CCAF hopes to encourage a consensus among managers, auditors and legislators on ways to improve public management in three related areas:**

- Encouraging the **innovation** necessary to improve the efficiency and effectiveness of operations,
- Improving the capacity to manage **risk** – building the trust required to confidently reduce red tape and support the launching of innovative projects, and
- Ensuring sound **control** – limiting administrative rules to those that make sense while focusing employees less on process, and more on the achievement of results.

This document sets out five principles intended to help managers, auditors and legislators agree on reasonable expectations respecting innovation, risk and control. **CCAF believes that common understanding in these areas can support more constructive and trust-based working relationships.** When managers, auditors and legislators agree on reasonable expectations in difficult areas, friction is reduced, management practices and controls are improved and government is able to deliver better results for citizens.

## Underlying Idea #1: Managers have choices on control

The decision of whether to encourage innovation and deal with internal red tape comes down to how management wants to effect control.

**Control focuses on management actions that support people in the achievement of objectives** – actions associated with effectiveness and efficiency of operations, resource stewardship, reliability of information used for internal management and external reporting, and compliance with applicable laws and regulations.[3]

Control is a core element of management and provides reasonable comfort that six basic conditions are in place:

- The delivery of programs and services is **efficient and effective**,
- **Reliable financial and non-financial performance information** is used to support operations and accountability – sound performance assessment and reporting[4],
- **Laws, regulations and delegated authorities in the ministry are respected**,
- Organizational behaviour reinforces **public service values and ethics**,
- **Assets are protected** from unauthorized acquisition, use or disposition – there is adequate prevention or detection of fraud, theft or other malfeasance, and
- **Essential resources (human, physical, information and intellectual) are sustained** – they are maintained, renewed or replaced when necessary.[5]

**Control should always be linked to risk and can be thought of as any action, procedure or process aimed at containing a risk to an acceptable level, or increasing the probability of a desired outcome.**[6] When a public sector organization explores its risks, it should consider the most cost-effective approach to control. **It is a core management responsibility to calibrate control instruments to realistic assessments of risk.**

Control depends on capacity – on knowledge, financial resources, capital assets, and motivated employees. Well-controlled organizations exhibit certain characteristics:

- People focus on objectives,
- People demonstrate sound judgment and stewardship – and manage the risk of inappropriate actions,
- People are able to innovate in light of known risks,
- People have reliable financial and non-financial information to guide decisions and account for performance, and
- The organization earns the confidence of legislators and the general public.[7]

Public sector control is both restricting and enabling. It restricts discretion in that it protects against unwanted events such as waste, lapses of probity, or non-compliance with authority. But **control is enabling because it supports the achievement of objectives and sets the boundaries within which employees can take informed decisions.**[8] When it is well designed and sensibly applied, **control provides the context within which employees can test innovative ideas and improve operations for the benefit of citizens.**

Ultimately, for any public sector organization, control is not an option. The issue is how best to effect it.

## Underlying Idea #2: More rules do not equal better control

Occasionally basic norms of public sector fairness, propriety or stewardship are violated. When this occurs, the resulting issues may be played out in ministry boardrooms, in the legislature, in the media, in the courts – or in some cases, in all of these. Failure to adequately manage public resources – whether through incompetence or fraud – impacts managers, executive committees, auditors and elected officials. And it damages public trust.

**Yet a common tendency, when the dust settles, is for executives to reinforce their administrative rules in order to demonstrate that the problem has been addressed and will never happen again.**[9]

Over time, administrative rules focusing on the prevention, detection and correction of potential problems can overlap without reference to whether the underlying causes of the problem are well understood, whether identified risks continue to exist, or whether the rules work at cross-purposes. Like an unkempt garden, administrative rules can grow in sheer volume to the point where managers and staff are overwhelmed.

At a certain point – as compliance consumes increasing attention – sound management control (which focuses on stewardship, efficient operation and the achievement of objectives) can be compromised.

**In common language, when the reasons behind administrative constraint are unclear, when constraints overlap and lose their connection to underlying risk, when the volume of rules becomes daunting, when they divert attention from the achievement of objectives to the management of process, or when they are seen to inhibit sensible discretion and innovative practice, the organization is caught in a web of rules.**

Organizations struck with this malady tend to be risk averse, unwilling to try new ideas, and unable to improve efficiency, effectiveness and economy in their operations. When innovation is impeded by too many rules, citizens lose by receiving less value for their tax dollars than they deserve.

## UNDERLYING IDEA #3: THIS IS PRACTICAL GUIDANCE, NOT STANDARDS

Some public sector organizations may find that their self-assessed management capacity falls short of the practices implied by these five CCAF principles. This is natural and understandable. Three thoughts are relevant in this context:

- **First, these CCAF principles represent recommended practice, but they are not management standards or audit criteria.** Senior managers and auditors will need to discuss these principles and reach a consensus on what is reasonable and acceptable in each organizational case. Although the principles should help managers and auditors to reach that consensus, they are no substitute for the discussions that will still need to take place.
- **Second, the principles describe performance at a high level – that of the best-managed public sector organizations.** There is little point in setting recommended practices at the level of average performance or mediocrity. At the same time, public sector managers and auditors should recognize that movement toward these principles requires change in the culture of the organization. Cultural change occurs gradually and requires sustained communication, training and other reinforcement. Deciding to move toward these principles means recognizing that there are costs to bear and no quick fixes.
- **Third, existing management capacity and the overall environment of risk will determine how far, and how fast, managers will want to move toward these principles.** Implementation should be based on what is practical, given the investments involved. Managers will want to ask whether the investment makes sense given existing capacity and the risks associated with the current state. It is important that proposals to implement the CCAF principles be put to the tests of (1) practicality and (2) clear net benefit associated with moving forward.

There is no perfect approach to encouraging innovation, reducing administrative rules and maintaining control in public sector organizations. **The best-case scenario is that public sector managers and auditors will discuss these CCAF principles, move toward consensus, and adapt them to the specific needs of the organization at hand.** Dialogue, aimed at a gradual implementation of management improvement, may be the greatest benefit of the principles themselves. Consensus among managers and auditors will take time to build, but dialogue is much better in the long run than an attempt to implement these principles rapidly, without taking the time to discuss costs and practicalities.

## APPLICATION OF THE PRINCIPLES

The five interrelated principles can be applied in any public sector organization, whether a large ministry, a smaller organization, or a central agency. Although the principles are written to serve the needs of Canadian federal and provincial governments, Canadian municipal authorities or para public entities (or even international jurisdictions) may well find them applicable – even though some of the organizational forms discussed (e.g., central agencies) will be different.

Elected members of federal and provincial legislatures also share an interest in these principles. Legislators play an important role by passing the laws that mandate public sector organizations, by approving their budgets, and by holding the executive branch to account for performance – both in what was achieved and how it was done. These principles can help legislators to ask informed questions on whether a public sector organization is well managed from the standpoint of innovation, risk management and control.

# Five Management Principles for Balancing Innovation, Risk and Control in Summary Form[10]

**Principle One:** **Management should ensure that innovation is led and encouraged, and that barriers to innovation are removed**

*Organizations should sustain an environment where employees are encouraged to take initiative; where the basic skills of innovative practice are taught and supported; where legitimate mistakes are not sanctioned but learned from; where success is rewarded; and where blame is restricted to cases of incompetence, imprudence or malfeasance.*

**Principle Two:** **Innovative projects must be well controlled and managed**

*Creative ideas can come from anywhere in the organization but moving from the "raw idea" to the "implemented idea" stage does not happen by chance. Managers should be given the flexibility they need to test new ideas, provided that risks are considered in advance, and their projects are managed in a disciplined, accountable manner.*

**Principle Three:** **Management should invest in a risk-smart culture that can act on opportunity**

*Organizations should develop the capacity to assess and act on risks and opportunities in order to better design their administrative rules, support innovation in the workplace, and achieve their objectives.*

**Principle Four:** **Management should eliminate unnecessary administrative rules and challenge the creation of new ones**

*Administrative rules should be integrated, clear as to purpose and linked to risk. To support innovation and improved efficiency, public sector officials should review existing rules to modify those that no longer have a justifiable purpose, or whose burden is disproportionate to risk. To further limit red tape, proposed new rules should be challenged before going into place – they should be calibrated to risk, and promised benefits should clearly exceed expected costs.*

**Principle Five:** **Management and staff must respect the rules that exist**

*Managers and employees should respect the organization's control framework and follow its rules – and there should be well-understood consequences if this does not occur.*

# The Five Principles
## with Detailed Discussion and Analysis

### Principle One: Management should ensure that innovation is led and encouraged, and that barriers to innovation are removed

*Organizations should sustain an environment where employees are encouraged to take initiative; where the basic skills of innovative practice are taught and supported; where legitimate mistakes are not sanctioned but learned from; where success is rewarded; and where blame is restricted to cases of incompetence, imprudence or malfeasance.*

### Discussion, Analysis and Guidance

#### *Overview*

Whether creative ideas occur through structured thinking or serendipity, they are assets to the organization. But innovation goes beyond "creativity" (which is commonly defined as the generation of a new and promising idea) to include the project design and management follow-through required to capture the benefit of the idea, and implement a new way of doing things. Creativity is about the idea. Innovation is about the idea and the implementation.[11]

In the private sector, an organization may launch ten initiatives aimed at achieving an objective with the expectation that several will fail. If the objective is achieved, it may not matter much if all ten initiatives were adequate – or whether three worked well, two retained some promise, while five were abandoned.

The private sector view that even well managed initiatives may fail is largely foreign to the public sector where auditors and managers tend to place an equal focus on each initiative as well as on the overall objective. An environment where the rewards system is based on avoiding unexpected results is an environment that discourages innovation and encourages the setting of easy to reach goals.[12] Innovation in the public sector is often seen as an optional extra, or a burden, rather than as a core activity – and the perceived costs of failure appear to outweigh the rewards of success.[13]

**Promoting innovation depends on cultural change, sustained by the leadership of senior executives.** Cultural change depends on consistent messaging, reinforcing incentives, persistence, and the ultimate development of trust. Senior management should reinforce the message that project managers are accountable for the sound control of their projects – but they will always be backed up when well-managed projects fail to deliver expected results.

Leadership and trust should be reinforced from all angles. The idea of treating "innovation" as essential to more efficient and effective service delivery is not always featured in values and ethics codes, and the management of innovation is rarely taught in public sector management schools. The combination of a lack of knowledge, incentives and skills can severely hinder the innovation process.[14] In effect, there are significant barriers to innovation and it is rarely sufficient for managers to permit innovation – rather it must be actively encouraged, resourced, and persistently supported by senior leaders.

#### *Innovation means substantial change, not "fine-tuning"*

**Innovation is the creative generation and application of new ideas that achieve a significant improvement in a product, program, process, structure or policy. Innovation is about taking creative ideas and combining them with initiative, to make them work.**[15]

Public sector innovation may focus on the design and implementation of groundbreaking ideas respecting strategy/policy, service/product and program design, program delivery, administrative process, and system interaction (e.g., new ways of interacting with other entities and knowledge bases).[16]Although some argue that small, incremental change is innovative in nature – others suggest that it falls into the category of process improvement or reengineering and is largely the result of fine-tuning, rather than innovative practice.[17] The principles proposed in this document focus more on how to encourage and manage the more radical or transformative change necessary to improve productivity in a major way. That is, for the purposes of these CCAF principles, **innovation involves the implementation of substantially new ideas: it is ground breaking, it seizes unique opportunities and it leads to fundamental improvements.**[18]

### *Barriers to Innovation Are Many*

Barriers to innovation in the public sector can arise within the organization, within the broader government environment or in the broader societal environment.[19] **Current research suggests that by far the largest number of barriers occur <u>within</u> public sector organizations themselves**. This may reflect the fact that innovative projects change existing operating procedures, power structures, work dynamics and occupational patterns.[20] Change can be uncomfortable.

There are a number of specific barriers to innovation in the public sector:

- **Delivery pressures and administrative burdens**: Managers and professionals rarely make sufficient time to think about innovation. Rather, a large proportion of time is spent responding to the day-to-day pressures, delivering services and reporting to senior management, central agencies and others.
- **Short-term budgets, people, and planning horizons**: The inability to think beyond day-to-day pressures may be reinforced by budget and planning horizons that emphasize annual efficiency gains over those of a more long-term, sustainable nature. The former can be achieved by a one-time cost cut. But sustainable savings require innovation. And when senior managers change regularly, it is difficult to maintain the management attention that is required.
- **Poor rewards and incentives**: The phenomenon of higher penalties for failed innovations than rewards for successful ones is consistent across public sector jurisdictions. Performance appraisal systems do not sufficiently recognize or value innovation. And innovation as a management practice is rarely taught in public sector management schools.
- **Culture of risk aversion**: Many managers see little upside in taking risk. While many programs may only function at an "acceptable" (as opposed to high efficiency) level, they normally receive less critical attention from the media, Parliament, auditors and Public Accounts Committees than do programs or projects where a perceived failure has occurred. Public servants recognize that there are career downsides associated with perceived failure.
- **Poor skills in innovative project management**: Managers need to know how to structure and manage innovative projects and manage risks. These factors represent teachable knowledge and skills, but public sector organizations do not always insist on them.
- **Reluctance to close down failing programs or organizations**: Although private sector companies must innovate in order to survive, it is rare that public sector organizations cease to exist because they were not innovative. The private and public sector imperatives are different.[21]

### *INCENTIVES AND ENABLERS CAN HELP TO COUNTERACT THE BARRIERS*

Research has shown that barriers can be overcome when values, incentives, leadership and other enablers are aligned in support of managed innovation:[22]

**AN INNOVATIVE CULTURE REQUIRES LEADERSHIP AND SUPPORT FROM THE TOP:** This means aligning organizational priorities to guide innovation, recognizing innovators, granting the latitude for experimentation, reducing unnecessary administrative burden, and providing protection from blame when well managed projects do not pan out as originally expected. **It also means that managers who start innovative projects see them through to a point where they are stable and sustainable.**

**INCREASE THE REWARDS FOR INNOVATIVE INDIVIDUALS AND TEAMS:** Rewards may be financial, recognition, authority, or career-progression based. Recognition is highly valued in the public sector and teams may identify the delegation of additional authority as an important vote of confidence and motivator. It is important that efforts are appreciated and positively communicated.

**RESOURCES:** Because inadequate resources are a frequent problem, managers should ensure that their innovative projects have both the prior knowledge of management and the necessary resource support. To address the resource issue, central agencies and ministries might consider the creation of innovation reserves to support promising ideas that are backed up by a sound project plan.

**ENSURE DIVERSITY:** Innovation requires an ability to see things differently. Differences in the backgrounds and perspectives of an organization's employees may help to foster innovation.

**LEARNING:** Innovative organizations are able to learn through benchmarking and professional networks. They also treat innovation as a teachable set of skills and practices, and they link management development and training plans to those skills and practices.

**INNOVATION IS EVERYONE'S RESPONSIBILITY:** Organizations should encourage and draw on ideas at all levels. Attempting to isolate innovative practice in "skunk works" units tends not to work in the public sector. Innovation should be valued and seen as a responsibility of all employees.

**SCOPE FOR EXPERIMENTATION:** Creating safe places to test ideas such as **pilot projects and task force teams** is an effective way to experiment. A key factor is trust. Well-managed failures should be defended, provided that learning takes place, and the organization "fails forward."

**MANAGED INNOVATION REQUIRES MONITORING AND EVALUATION:** The aim is to promote real-time learning so that the main lessons drawn from a particular innovation are fed back to inform policy and management practice quickly.

**EMPOWERING FRONT LINE STAFF:** Evidence shows that front line staff and middle managers are the most frequent public sector innovators. Yet evidence also indicates that these employees may exhibit the greatest resistance to change, thus hindering innovation. There is a need to engage middle managers and front line staff – the culture bearers in the organization – and avoid the assumption that innovation can only come from headquarters.

**INVOLVEMENT OF THOSE LIKELY TO BE IMPACTED:** It is important to ensure that the **views of end-users** are taken into account when developing and implementing an innovation. Careful attention to user requirements at an early stage can identify and correct obvious problems, and facilitate the acceptance and diffusion of the new approach.

## *ENCOURAGING CHAMPIONS, WHILE BUILDING SKILLS, AND TRUST*

Some managers are more adept at introducing and supporting innovation than are others.[23] Innovation champions are those who view their role broadly and have a sense of the issues that affect their organization. Champions convey belief and enthusiasm about the proposed innovation, they have strategic knowledge and are able to enlist the support and involvement of stakeholders. Champions use both internal and external people to scout for ideas and apply formal and informal selling channels. Finally they tend to see new ideas as opportunities and not as threats.

It is important to distinguish between innovation champions and units. Evidence suggests that setting up separate units or "skunk works" is not conducive to greater and more diffused innovation. Skunk works units may signal that innovation is a specialist activity, distinct from the tasks and responsibilities of employees.[24] **When innovation is seen as a specialist function, it is unlikely to grow as a broad-based management practice.** Organizations wishing to promote innovation should pay attention to identifying and encouraging many potential innovation champions.

Beyond this, managers should recognize that **each stage of the innovation cycle requires a different set of skills.**[25] As **ideas are generated**, managers must understand citizens' demands using a variety of applied science, modeling and "what if" scenario building.[26] They should learn by listening to their clients and partners. When projects move into the **design and application stages**, key skills begin to include leadership and vision, building innovative networks, and understanding of organizational culture, structure and dynamics. Project planning and risk management skills are also crucial at this stage. When **innovation is being diffused**, new skills come to the fore – diplomacy and persuasion, communication and social marketing, creating conditions for uptake, and project evaluation to identify and measure success.

**The final essential condition is trust** – a cultural value that is difficult to develop but easy to lose. Innovation can only occur when an implicit bargain is put in place. That bargain consists of three elements:

- That innovators will **manage their projects in a sound, professional and prudent manner**,
- That the executive managers, to whom they report, will provide **reasonable relief from normal administrative constraints** provided that a credible risk assessment has been conducted, and
- That all parties (managers, governing bodies, auditors and elected officials) buy into and support an enlightened form of **public accountability.**

It is inevitable that errors or unintended impacts will occur in innovative projects. When they do, organizations should be able to tolerate mistakes or adverse results, provided that any risk taken can be shown to have been reasonable and the management of the risk to have been sound.[27]

This places a burden on all participants. **Managers, auditors and elected officials alike should be prepared to accept that some well-controlled projects will fail – and when they do, the object is not to sanction the project manager but to ensure that learning occurs and is shared widely.**

When media become active – or when legislative committees call for swift retribution – auditors, comptrollers, managers and elected officials should be prepared to account for what was done, for what worked (and didn't), for what was learned, and for what actions will be taken. But there should be no contrition for a well-managed innovative project that yielded few, or unexpected, results. On the contrary, senior managers, auditors and responsible elected officials should be prepared to explain and defend, if necessary, the work that was done.

## PRINCIPLE TWO: INNOVATIVE PROJECTS MUST BE WELL CONTROLLED AND MANAGED

*Creative ideas can come from anywhere in the organization but moving from the "raw idea" to the "implemented idea" stage does not happen by chance. Managers should be given the flexibility they need to test new ideas, provided that risks are considered in advance, and their projects are managed in a disciplined, accountable manner.*

## DISCUSSION, ANALYSIS AND GUIDANCE

### *OVERVIEW*

Some may think that innovation occurs best where there is little structure – where employees can test ideas without the restraint of rules or management discipline. It cannot work that way in public sector entities for two reasons. First, unfocused energy rarely results in practical innovation and second, taxpayers' dollars are at play. Unaccountable use of public resources may lead to misuse of funds or worse.

There are at least four necessary conditions for innovation to flourish in a public sector environment – opportunity, motivation, management skill and trust. It often happens that although opportunity may be present, there is a lack motivation (and of basic knowledge and skills) in how to manage risk and structure innovative projects.

### *SIX ATTRIBUTES OF WELL-MANAGED INNOVATION*

Bringing a creative idea to a practical result requires sound project management. Creativity cannot be translated into innovation unless there is a workable management structure that supports trust between the project manager and employees – and between the manager and senior governing authorities. Project managers must earn this trust. In return for being given reasonable administrative authority, their obligation is to ensure sound project management practice and accountability.[28] **There are six attributes or underlying conditions of a properly controlled innovative project:**

**Prior Knowledge:** Senior management must be made aware of the initiative at the front end and must support an adequately resourced project plan.

**Risk Assessment:** An assessment of the risks must be made and the probability and possible consequences of failure understood.

**Risk Mitigation and Acceptance:** Remedial actions in the event of a failure must be considered and accepted by management at the outset of the project.

**Monitoring:** Management must monitor progress.

**Earned Authority:** Senior management must be prepared to offer sufficient authority to innovative managers – this may well mean loosening rules to facilitate experimentation over the course of the project.

**Mature Expectations:** All participants must enter the project with the idea that:

- There are no absolute successes or failures,
- The objective is learn how to improve the efficiency and effectiveness of the organization,
- Unexpected results are inevitable and will be a source of learning, and
- Successes and failures will be explained and defended by executive managers in front of accountability bodies.[29]

**In the end, innovative managers and employees should be rewarded whether the project was a "success" or not, provided that they played by these rules, controlled the project responsibly and communicated project learning throughout the organization.**

## ACCOUNTABILITY AND ITS LINK TO INNOVATION

Accountability is a relationship based on obligations to demonstrate, review, and take responsibility for performance, both the results achieved in light of agreed expectations and the means used.[30]

**Successful innovative projects require a respect for accountability and a focus in three areas: starting the project on the right foot, adjusting to stay on course, and fairly reporting on what was achieved (and how it was done)**. None of these supporting conditions requires extensive bureaucratic process, but managers should pay attention to them throughout the project lifecycle.

Starting on the right foot means that **clear roles and responsibilities** are established at the beginning of an innovative project. Where responsibilities are unclear, the issues should be sorted out before the work is started. Performance expectations and operating constraints should also be understood and agreed on at the start.

Rules or other operating constraints should reflect expected risks and the capacity of the project team to manage the initiative in a responsible manner. **The presumption should be that demonstrated capacity to control the project should allow for a reduction in operating constraint.** Hard controls can and should vary for innovative projects and "cookie cutter" approaches should be challenged. **Operating constraints for teams managing innovative projects should be restricted to those reasonably required to control the project in a sound manner.**

Management should understand the risk profile and mitigation strategy for the project and should be satisfied that both are within acceptable tolerances. Performance expectations should reflect capacity (authorities, skills, and resources) and the risk profile of the project. Finally, management should recognize at the outset that innovative projects have uncertain outcomes, and some will inevitably fail to achieve expected results, even when they are well controlled. This is normal and should not be viewed as a project failure.

Staying the course is important and depends on project monitoring, adjustment and learning. This means that feedback on progress should be provided, lessons should be learned and corrections should be made. More fundamentally, **staying the course depends on the stability of leadership**, of teams and of philosophy. Successful innovation cannot occur when leaders regularly change jobs in mid-stream or shy away from clearing obstacles that impede progress.

Closing the loop with senior management is important. Simple, balanced and timely information should be available to demonstrate what has been achieved, how it was done, and what was learned. This reporting should never become bureaucratic or burdensome – an emphasis should be placed on simplicity. **Success should be rewarded. And when well-controlled but risky projects fail to meet their intended results, management should exercise care to learn from the experience and avoid the laying on of blame. Rather, management should visibly defend the project.**

Managed innovation is the only way that an organization can test ways to better conduct its operations, learn, and build the trust that will pay benefits over time. In a well-controlled public sector entity, innovation is encouraged and undertaken not as an adjunct to good management but as a fundamental and reinforcing element of it.

## Principle Three: Management should invest in a risk-smart culture that can act on opportunity

*Organizations should develop the capacity to assess and act on risks and opportunities in order to better design their administrative rules, support innovation in the workplace, and achieve their objectives.*

## Discussion, Analysis and Guidance

### *Overview* [31]

Organizations exist for a purpose. Successful private sector companies aim to earn profit and generate value for shareholders. Public sector organizations aim to develop policies, deliver services to citizens, and support the achievement of broad societal benefits. Regardless of their objectives, both public and private sector entities face uncertainty. A well-managed public sector organization should be able to identify uncertainties – both their potential likelihood and impact – and use this knowledge to support innovative projects, improve results for citizens and eliminate unnecessary administrative rules.[32]

Risk is synonymous with uncertainty of outcome. Although **risk often conjures negative images of peril, it also applies to all uncertainty, both negative and positive.** Events or activities that have potentially negative consequences threaten the achievement of objectives. At the same time, when an organization regularly avoids reasonable risk, it becomes rigid in its outlook and trades off opportunities to improve the efficiency and effectiveness of its operations. There is a positive side to taking risk.

**Improving value for money requires that public sector entities embrace this positive (or opportunity) side of risk.** Although there is no real way to avoid uncertainty, there are ways to understand its dimensions and act on innovative opportunities that arise. But to do this, managers must cease to equate risk with negative consequences and begin to understand the opportunity side.

### *Typical Risks in Public Sector Organizations*

No public sector organization can move safely from a "checking" to a "trusting" control environment without first ensuring that sound risk management practices are in place. Risk management can allow an entity to constrain threats to acceptable levels, to reduce administrative rules to those that are necessary, and to take informed decisions on opportunities to innovate.[33] When an organization understands risk, it can gradually move its control environment to one less dependent on hard controls. Typical risks for a public sector entity include:

- Poor **stewardship** or failure to guard against malpractice or waste;
- Anything that damages **reputation**, or undermines public confidence;
- Failure to **comply** with regulations – compromising health, safety or the environment;
- Anything that poses a **threat to the delivery of services**;
- High **opportunity costs** – failure to seize opportunities to **innovate**; and
- Failure to link rules to risk, to the point where a **web of rules** develops and the efficient achievement of objectives is compromised.[34]

Public sector entities should implement cost-effective approaches to assess and address the impact of uncertainty. Employees engaged in this work should be backed by skill development opportunities, and by the encouragement necessary to apply those lessons in their daily job.[35]

There is no one right way to manage risk in a public sector entity. Managers should be prepared to learn what works in comparable organizations and adapt those lessons to their own environment. **Central or co-ordinating agencies also have an important role in setting risk management frameworks for broad application, and in providing training and experience sharing opportunities for ministry staff.**

At a conceptual level, risk management involves identifying, assessing and addressing risks – and reviewing, reporting, learning and taking informed action based on that analysis. Central agencies and management committees in ministries should ensure that their approaches to risk management cover these main elements, and that risk management is integrated into the daily management practices of the organization.[36]

### *Working together to promote a risk-smart culture*

**Public sector culture (the values, ethics and norms that underpin action) is risk averse.** With few incentives to take risks, managers often link risk taking with the possibility of something going wrong or of project failure. Conversely, in successful private sector entities, risk taking is considered essential to improved service or product delivery – the core of a company's competitive advantage.[37] **Private sector entities are often prepared to take informed chances.**

Bringing about cultural change requires **persistent attention**:

- Senior management should lead on risk management – the benefits should be clearly communicated to staff;
- Risk management should be embedded in the management cycle – planning, doing, adjusting, checking, learning and reporting; and
- Administrative rules should be linked to (and be proportional to) risk.[38]

**In assessing corporate cultures, ministries and central agencies should ask several questions:**

- Is risk management seen as everyone's business or as a specialist function?
- Do learning plans include risk management skills?
- Is risk management embedded in the ministry's management processes?
- Is the management of risk linked to the achievement of objectives and to the management of innovative projects?
- Do managers link the rules they are responsible for and the risks that those rules aim to mitigate, and are the two in reasonable balance?[39]

**Cultural change begins with people and no entity can move from a risk averse to a risk-smart culture without equipping its employees.** Ideally, employees should have access to the training, tools, information and encouragement necessary to support change. Practically, there are limits to the investments that a public sector entity can make – a reality that calls for a corporate training and development plan defining risk management, among others, as a useful investment that is aligned to corporate needs.

**Risk smart organizations regularly monitor their external environment for changes that suggest threat or opportunity.** Organizations should commit to a risk management process (tied to innovative project and entity-wide planning) to permit a considered response to residual risk exposure.[40]

**Public sector organizations should ensure that all significant risks, once identified, are assigned to an owner who has the responsibility for managing and monitoring.** Similarly, a well-managed organization should know the owners of its main administrative rules – each owner should know whether the costs of the rule are proportional to risk. Although the risk and rule owners do not need to be the same person, they should regularly talk.

**In a risk-smart organization, rule makers are able to move the balance from hard to soft controls** because employees are competent – learning plans are resourced and implemented, key positions and activities have been identified, risks are understood and linked to rules, and there is relative organizational stability. In other words, the organization has strong resilience and capacity, and a control environment that makes sense in terms of risk.[41]

## Principle Four: Management should eliminate unnecessary administrative rules and challenge the creation of new ones

*Administrative rules should be integrated, clear as to purpose and linked to risk. To support innovation and improved efficiency, public sector officials should review existing rules to modify those that no longer have a justifiable purpose, or whose burden is disproportionate to risk. To further limit red tape, proposed new rules should be challenged before going into place – they should be calibrated to risk, and promised benefits should clearly exceed expected costs.*

## Discussion, Analysis and Guidance

### *Overview*

**Control is exercised through the actions of people.** Employees should be aware of the rules that constrain their actions and managers should clearly communicate their expectations for ethical behaviour. Staff should have sufficient information and training to make decisions that reflect their legal authorities and other administrative requirements.[42]

**There is a tendency in public sector organizations to layer administrative requirements in a seemingly random way, to the point where sheer volume becomes a concern.** At least some of these requirements are driven by short-term imperatives that have ceased to be appropriate with the passage of time, with changes in technology, or with improvements in organizational capacity.

**The creation of randomly layered rules reflects an aversion to the management of risk, and diverts attention from the achievement of results to matters of process.** Layered rules can create confusion between process and objectives, they decrease productivity, and they often irritate employees.[43]

Administrative rules should never proliferate to the point where they become unduly burdensome, or negatively impact on operational efficiency and the achievement of objectives.[44] Accordingly, central agency and ministry officials should review the most burdensome elements of the existing rules base – and should challenge proposals for new rules.[45]

Rules that pass the test are **clear, understandable and accessible** to all employees; they address areas of concern in an administratively **efficient** manner and are **proportionate to risk** (no overkill); they **do not conflict**; they are **tailored** (giving credit to well-managed organizations); they have **benefits that exceed their costs,** and they are **respected.**[46]

A prerequisite for effective rule reduction is the building of management capacity. Where capacity is strong, the risk of control failures is diminished and the need for detailed rules is lessened. Similarly, the more that managers reinforce public sector values and ethics, the less their organizations will depend on hard control instruments.[47] When these two factors (management capacity and values) are reinforced, the entity becomes more resilient. Building this resilience requires sustained leadership, but it is the foundation for the effective challenge of burdensome rules.

### *Rules should be linked to values, and reinforced by management*

It is difficult to follow rules that are unclear as to purpose, poorly presented, or unconnected. Regardless of whether the rule comes from a central agency, or from within a ministry, management should communicate what the rule aims to achieve, why it is in place, to whom it applies and what needs to be done by employees. **Wherever it would enhance understanding, rules should be presented in an integrated manner, showing how they fit together.**

The most meaningful rules are those that support democratic, professional, ethical, and people values and the underlying principles of fairness, propriety and sound stewardship of public funds.[48] **Management has a responsibility to communicate the values that underpin ethical behaviour in the entity and to demonstrate them to employees.** Reinforced through ongoing communication, training and the organization's policy framework, sound public service values are essential to prevent conflict of interest, to provide guidance for proper behaviour, to identify improper behaviour promptly, to remove temptation for unethical behaviour, and to provide discipline, where appropriate.[49]

Managers should demonstrate that the organization's values will not be compromised. Second, they should reinforce these values through communication with staff in meetings, in one-to-one discussions, or in dealing with day-to-day activities. Third, management should consider developing a **values and ethics code**, or equivalent, while ensuring that employees periodically acknowledge compliance with it. Such a code should be simple, intuitive and defendable – and it should show examples of behaviours that are acceptable and others that are not.[50]

### *Many Administrative Costs Are Hidden*

Administrative rules serve valid purposes including the prevention of fraud, the overall stewardship of resources or the recovery from undesirable events.[51] However, the implementation of any significant rule normally establishes many related **control activities**, few of which are ever identified or assessed as to cost. Control activities for any one rule may include observing, comparing, approving, reporting, coordinating, checking, analyzing, authorizing, reconciling, supervising, reviewing, segregating and following up. **Every activity imposes a repetitive, mostly hidden cost.** [52]

Public sector entities must also control the personal information of citizens whether related to tax records, employment history, the cross-indexing of Ministry records, or other private matters. Many additional activities apply to public sector information systems, including logical and physical access restrictions, back up and recovery, job scheduling and completion checks, system edits and software selection and testing.[53]

Given these many activities, it is not surprising that public sector managers – whose personal authorities are limited by legislation and detailed instruments of delegation – may become overwhelmed. **The sheer volume of control activities can become a major impediment to innovation.** This is particularly so when new control instruments are implemented without due regard to the burdens imposed by those that already exist.

### *Finding the Balance Between Hard and Soft Controls*

Concern with the "web of rules" focuses on finding the right balance between hard and soft control instruments – or what some call the balance between checking and trusting. At the "hard" controls side of the spectrum are the firm rules, uniformity of processes, centralization, oversight and systems intended to ensure that employees are responsible in their actions and accountable for what they did, how they did it and what they achieved. On the "soft side" are found devolution of authority, staff and organizational capacity development, permissive action based on public sector values, and a reduction in rules and obligatory processes.

In most public service jurisdictions the balance between hard and soft controls has continually shifted between checking and trusting over a period of years.[54] An ideal balance is something occasionally termed as "loose-tight." **In the loose-tight model a few critical "hard" rules are set and tightly monitored. But within that framework, employees have substantial freedom to act and innovate – provided that they understand the risk environment and apply sound management practices and public service values in their work.**

### *Reviewing existing rules: weeding out, and tailoring rules to capacity*

Moving from a control environment that is dominated by "checking" to one that is more trust-based requires central agencies and ministries to ensure that the existing base of administrative rules reflects the current risk environment. Rule makers should therefore be prepared to:

- First, **eliminate (or "weed out")** those rules that no longer have a continuing rationale or are unduly burdensome, given the risks they aim to address, and
- Second, **"tailor" the remaining rules to specific cases**, taking into account the management capacity of the entity and perceived risk.

A reduction in rules should never become an absolute objective. In judging where best to aim on the checking-trusting spectrum, public sector managers should carefully consider the overall management capacity in the organization. Where management capacity is strong, operational risk is generally low – and management can safely reduce administrative constraints. Where capacity is weak, safe opportunities to strip away rules are diminished.

### *Tailored rules give more operational discretion, but this must be earned*

In general, demonstrated management capacity (including the ability to manage risk) should translate into fewer rules and less invasive control at the operational level. **Tailored rules imply the issuance of principle-based administrative policies that allow levels of local discretion to vary, based on management capacity and risk.**[55]

For example, it may be justifiable for central agencies to set enterprise-wide procurement policies requiring Cabinet approval of high value purchases. But it may also make sense to design a tailored rule allowing some ministries additional latitude to act, provided that they demonstrate sound management capacity. This might allow well-managed entities to purchase at higher dollar-value thresholds without central agency approval, or it could allow exemptions from other generally applied restrictions.[56]

In a similar vein, when central agencies require common ministry standards for the performance of oversight functions (e.g., enterprise-wide rules for evaluation or internal audit) it is unlikely that the smallest agencies will have, or can build, the capacity required to meet those standards. In such cases, **central agencies may need to tailor the rules for small agencies in order to allow a different or more appropriate set of rules.** Otherwise central agencies should accept that additional resources will be necessary when small agencies are unable to meet the stipulated level of performance.

### *Focusing where the benefits are greatest*

Rule reductions designed to make public sector processes more efficient may involve the Pareto rule, which implies that **20% of the rules are responsible for 80% of workload**. Organizations wishing to weed out and tailor their rules should make a distinction between high and low benefit areas and focus on areas of greatest return.

Some burdensome rules originate with central bodies (legislatures or central agencies), but many do not. **Because many rules originate locally, central agencies and ministries alike should be prepared to eliminate any rule, activity or process** where an assessment of management capacity (and of the overall risk environment) suggests that the cost of applying the rule outweighs the benefits.

Systematic, annual review of management capacity in ministries is one way to build a time line of strengths and weaknesses across the government. Although the costs associated with government-wide review are significant, there is little doubt that a credible understanding of operational capacity – both its strengths and weaknesses – is a prerequisite for the weeding and tailoring of burdensome rules.[57]

### *THE NEED FOR STRUCTURED REVIEW*

De-layering the existing base of rules represents transformational change – something that requires leadership and a review process well supported by central agency and ministry executive committees

Even a well-designed process may be met with ambivalence by staff, who could view it as additional workload bearing limited chance of success. A poorly designed review process can add as much administrative burden as it eliminates, especially in its early stages. **Care should be taken to ensure that the costs associated with any review process are reasonable and containable**, that those involved in the work do not have this responsibility added to their existing workload, and that early successes in reducing administrative burdens are well communicated to all staff.

To deal with potential problems, it may be appropriate for entities to support a limited number of **task forces or study groups** involving officials from both central agencies and ministries.[58] In the absence of practical experience, **pilot projects** aimed at de-layering rules in designated areas can be an effective way to learn which project management approaches work best.

Public sector organizations may want to consider **six possible tests**:

1. Does this rule have a sound **rationale** – does it address a real risk, or is it imposed more to entrench a process? Is the rule clear and does it make sense?
2. Is the rule demonstrably **efficient** – does it impose a reasonable administrative burden relative to the risk it aims to mitigate, and do the benefits of following the rule outweigh the costs? Does it overlap or conflict with a rule already in place?
3. Is the rule **justified** – was it discussed with stakeholders who accept that there is a risk or capacity issue that needs to be addressed?
4. Can the rule be **tailored** for application to avoid a one-size-fits-all approach? Can some organizations be exempt from the requirement if they demonstrate sound management capacity in the area?
5. Are there reasonable **alternative instruments** (say voluntary measures or information strategies) that would be sufficient to minimize risk and meet the control objectives?
6. Might there be **unintended impacts** – can the rule be targeted to address a problem without spilling over or creating distortions in unintended areas?[59]

**Organizations should resist the temptation to review the existing base of rules on an optimistically tight schedule.** Recognizing the Pareto rule, central agencies and ministries should consult stakeholders to identify those control activities and rules that pose the greatest irritant – and start there. Opportunities are likely to be found in rules that have a significant impact on many, or all, units in the organization – or when detailed rules exist in low risk areas where management capacity is strong. Middle managers and employees have an intuitive sense of where these opportunities lie and senior management should seek their input.

In the end, an authoritative body must reach a decision. Getting there means that study teams or task forces engaged in reducing rules should be treated as priority projects, and participating employees should be rewarded for their corporate effort. All things considered, an organization that is prepared to weed and tailor its ongoing base of rules is an organization better equipped to move toward the loose-tight ideal, focusing less on process and more on its objectives.

### *CHALLENGING NEWLY PROPOSED RULES: BENEFITS SHOULD EXCEED COSTS*

Just as the existing base should be reviewed, newly proposed rules should be challenged to meet certain basic conditions.[60] They should:

- **Effectively address the identified concern or risk**,
- Be the **most efficient option**,
- Provide **benefits that exceed their costs**, and
- Be **approved by an authoritative body** that is able to assess impacts and require the integration of new rules with those that already exist.

New administrative rules only make sense when calibrated to an ongoing risk. If a clear relationship between risk and a proposed new rule cannot be demonstrated, it is unlikely that the rule should be put into place. Restricting new rules to those that are necessary requires a **five-step assessment process** commonly understood by most students of policy formulation.

- **Define the risk** or issue of concern,
- **Identify viable options** for achieving the desired control objective,
- **Assess the impact** (costs and benefits) of the proposed rule and consult with potentially impacted stakeholders,
- **Develop a strategy to implement** the rule if it passes this challenge, and
- Ensure that a knowledgeable, legitimate and accountable authority reviews the analysis and **approves the new rule**.[61]

Newly proposed rules should be put to two basic tests: 1) is there a sound **rationale** – does the proposed rule make sense and 2) are the **likely costs** affordable and reasonable?[62]

It is counterproductive to implement new rules without first assessing the **potential costs**. Compliance costs include the administrative and paperwork requirements associated with meeting a rule plus other matters such as equipment purchases, training, and the development and implementation of new information technology and reporting systems. Because these costs can be both substantial and hidden, it is important that they be explicitly brought to light in the analysis leading to a new rule.[63]

Reasoned assessment of proposed new rules, while desirable, cannot always be done. When a rule must be put into place on an urgent basis, entities should consider tagging the rule with a **sunset clause** – requiring the necessary analysis to be done within a reasonable time period, or the rule sunsets.

### *EXTERNAL ADVICE AND COSTS*

Whether reviewing the existing base or challenging the implementation of a new rule, consideration should be given to including **outside or independent advice**.[64] When judiciously used, outside advisors or internal auditors can help to bring knowledge from other jurisdictions (including the private sector) identify other potentially viable options, and assess whether the conclusions reached by the study group are reasonable.

If rule makers want a true picture of the potential costs and benefits of a proposed rule, they should consult stakeholders – those likely to be impacted directly. Stakeholder consultation can help to identify:

- Obstacles to successful implementation,
- The extent of required changes to systems and business processes,
- Additional administrative burden and costs involved,
- Implications for other aspects of the entity's administration, and
- Alternative options that might not have been considered adequately during the design and analysis stage.

Outside advisors should have full access to the analysis that is underway. They should be given a reasonable opportunity to respond to draft material and be provided with subsequent feedback regarding how their views were addressed.[65] At the same time, managers should be aware that external advisors can be costly and will add time to the review process. As with any investment, managers will need to balance the benefits with the costs.

**Assessing administrative rules against a set of criteria will cost money.** To do it, senior officials must first agree that the short-term costs of structured review and challenge are worth the ongoing administrative efficiencies. In that sense, challenging proposed rules is analogous to a person thinking about quitting smoking. It takes a substantial commitment to make the initial effort but the returns are significant and ongoing.

When administrative rules are aligned with values, they are more likely to be understood and respected. Similarly, when functional management capacity is strong, the risk of control failures is diminished and organizations have an opportunity to reduce their hard controls. **Building management capacity and aligning rules with values and ethics requires continual reinforcement.** This is a key challenge for managers wishing to reduce red tape and promote innovation in public sector organizations.

## PRINCIPLE FIVE: MANAGEMENT AND STAFF MUST RESPECT THE RULES THAT EXIST

*Managers and employees should respect the organization's control framework and follow its rules – and there should be well-understood consequences if this does not occur*

## DISCUSSION, ANALYSIS AND GUIDANCE

### OVERVIEW

**The solution to broken rules is not introducing new ones – it is making sure that the existing rules are well designed, understood and respected.**[66]

A focus on results and innovation is not a license for ignoring basic principles; for illegal, unethical, or otherwise improper behaviour; or for incompetence.[67] Accordingly, there is a role for the assignment of blame and sanctions on individuals when actions have violated basic norms of fairness, propriety, or good stewardship.

### THE IMPORTANCE OF COMPLIANCE

**In a well-managed public sector organization the consequences of non-compliance are clear and proportionate with risk and context.** Managing compliance is an area of shared responsibility where central agencies and ministries (the external and internal rule setters) have an obligation to ensure that rules are clear and coherent – as per principle one – and public servants have an obligation to understand those rules and abide by them.[68]

In a rule-compliant environment managers ensure that violations of core policies, procedures and codes of conduct are documented and investigated, and that prompt remedial action is taken. Buttressing this, managers should ensure that formal channels of communication exist for people to report suspected improprieties. In a well-controlled public sector organization, anonymity of reporting is permitted and employees actually use the communication channel.[69]

### IMPACT, INTENT AND THE CONSEQUENCES OF NON-COMPLIANCE

Where important rules are disregarded or malfeasance occurs, **consequences should be fair**, **timely and balanced.** Senior officials should ensure that the severity of consequences is reasonable given the harm caused by noncompliance.

In considering the possible mix of consequences, officials should balance various considerations:

**Impact.** This includes consideration of the seriousness of actual or potential harm. Factors at play include the impact on resources, on the workforce, or on the reputation of the government. Other factors might include the impact on assets (including loss, waste or misallocation of funds), or whether there was personal gain.

**History.** Factors to be considered include previous cases and seriousness of non-compliance, including whether the incident was isolated to one individual or organizational unit, or reflective of a broader systemic problem.

**Intent.** Was the behaviour culpable or non-culpable? Consideration should be given as to whether there has been a deliberate contravention of legal or policy requirements.

**Other circumstances.** Consideration should be given as to whether the public good and the interest of taxpayers were ultimately served or harmed.[70]

Just as the rules and the behavioural expectations of employees and managers should be clear, the consequences for non-compliance should also be understood.

For control failures at an **organizational level** consequences may range from suasion (collaborative effort to improve control systems), through formal consent (a commitment to develop capacity in order to avoid future problems), to counteraction (imposed redress measures or conditions placed on funding) and finally, in extreme cases, to incapacitation (removal of senior officials or constrained organizational authorities).

A similar set of graduated consequences may also apply to **individuals**. Least severe consequences at the level of suasion might include the requirement for training, an oral reprimand or observations in a performance appraisal. Moderately severe ones could include reassignment or changes in delegated authority. And more severe consequences might range from counteraction (suspension, demotion or financial penalty) to incapacitation (termination of employment or of legal proceedings).[71]

**The quid pro quo for organizations that challenge and restrict their rules to those that are clear, integrated and meaningful is that those rules must be respected and followed.**

# CONCLUSION

The ultimate goal of any public sector organization is the improved wellbeing of citizens. Senior officials should encourage well-controlled innovation as a way to improve efficiency and effectiveness. Because middle managers and front line employees are important culture bearers, encouraging their innovative endeavors is critical. Innovation is not a specialist or a headquarters function. It is everyone's business.

Managers should ensure that control instruments are calibrated to risk and to organizational capacity. Where risks are low and capacity is strong, there should be a bias toward soft controls, rather than toward hard rules and obligatory processes. Managers should assess the risks and costs of any new rules they propose. The basic rules of a public entity should be understandable, proportionate to risk, and acceptable from a cost standpoint. And those rules must be respected.

Where a web of rules has developed, officials in central agencies and ministries should weed out and tailor those ones that no longer make sense. In looking for opportunities managers should consult with stakeholders, focus on the 20% of rules that may cause 80% of the irritation, and avoid trying to review too much, too fast.

Some innovative projects will fail. This is normal. **Avoiding unwarranted blame is the mark of sound leadership and the building of trust.** A well-led organization visibly rewards learning and focuses on blame only if incompetence, imprudence, or malfeasance occurs. Accountability requires that people accept responsibility for their mistakes. But excessive emphasis on laying blame is counterproductive.[72]

Public sector organizations are facing recruitment, employee retention and capacity challenges as an increasingly well educated and mobile workforce enters Canada's post-industrial economy. Young people who have employment options are unlikely to opt for a working environment that suffocates creativity and innovation and fails to engender trust.

# Endnotes

1 G. Dinsdale, M. Moore & A. Gaudes, *Organizing for Deliberate Innovation: A Toolkit for Teams,* CCMD Roundtable on the Innovative Public Service, chaired by Ruth Dantzer (2002), p. 13. The definition was slightly changed by CCAF to emphasize the idea of "initiative."

2 Adapted from the Office of the Auditor General of Canada, *2002 Report of the Auditor General*, Chapter 9: Modernizing Accountability in the Public Service (December 2002), p. 2. An accountability body could be a committee (eg. a legislative Public Accounts Committee) or an individual, say the deputy head of the Ministry.

3 This is a mix of two private-sector-oriented definitions – COSO, p. 1, Executive Summary as printed on COSO home page; CoCo, paragraph 6. Explicit mention of resource stewardship was included by CCAF. Some would argue that the definition of control should also include strategic planning, as that management function is critical to setting an organization on the right path with agreed-on expected results. The definition of control adopted by CCAF leaves out <u>planning</u>, along with other traditional management functions (<u>organizing</u> and <u>directing</u>, see the literature of Peter Drucker), on the grounds that control is but one function of management, not all of it. The underlying thought is that control is one of four functions of management – the others being planning, organizing and directing. Some argue for a fifth management function (<u>accountability/reporting</u>) but CCAF includes this in the definition of control.

4 It is worthwhile noting that the information used for public performance reporting should be a small subset of the sum of performance information used to control operations. As the CCAF and the Public Sector Accounting Board of Canada indicate in their seminal documents on performance reporting (Principles of Public Performance Reporting and Statement of Recommended Practices II, respectively) public performance reports should focus on a "few, critical" issues. This argues for a tight selection of measures to be provided in public performance reports. Although public performance reports should generally emphasize the "outcomes or results" spectrum of measures, operational control must focus on the full spectrum – with measurement of efficiency, economy and effectiveness. And there must be only one set of books – the measures used in public performance reports must be entirely consistent with those used for internal control.

5 This view of "control" is similar in form to the COSO definition but with the addition by CCAF of several important concepts: non-financial performance information; use of information to support operations, reporting and accountability; authorities; values and ethics; and renewal of resources to ensure sustainability.

6 UK National Audit Office (NAO), *Supporting Innovation: Managing Risk in Government Departments – Report by the Comptroller and Auditor General* (2000). This definition is found in the document glossary.

7 Canadian Institute of Chartered Accountants (CICA), *Guidance on Control (CoCo)*, Control and Governance Series – Number 1 (November 1995), Introduction, paragraph 2.

8 Office of the Auditor General of Canada, *1992 Report of the Auditor General of Canada – Chapter 4: Change and Control in the Federal Government* (1992), paragraph 4.13.

9 In a public sector organization there is a hierarchy of administrative constraint that begins with legislation (largely within the authority of the parliament or legislature) and cascades through subordinate legislation (regulations), policies, executive orders, guidelines and processes. Changes to regulations and to these other non-legislative constraints are largely within the authority of the executive branch – central agencies and ministries.

The executive branch of government cannot change legislation on its own behalf but it has vast discretion on how to go about administering the authorities provided to it in legislation and delegated (through formal instruments of delegation) to civil servants throughout the government.

**In this document CCAF uses the interchangeable terms <u>"rules" or "administrative rules"</u> to encompass those constraints put in place by central agencies and ministries to administer the executive branch operations of government – in other words, the regulations, policies, executive orders, guidelines, procedures, processes and other instruments that the government uses to manage itself. Similarly the focus of this document is on what might be called, <u>internal red tape</u> – the administrative web or rules that can grow up over time as governments manage their own operations – it does not deal with external rules imposed on others.**

It is beyond doubt that governments can and do create regulatory burdens on citizens and businesses, but those instruments are outside the scope of this document.

[10] Five <u>draft</u> principles are proposed as a <u>starting point</u> for discussion across Canada. Material has been taken from a variety of footnoted sources, in some cases in a form close to that of the original. This is acceptable in a draft document that will be widely discussed and will change substantially. These principles do not try to cover every issue associated with risk, innovation and control. Rather they focus on these concepts as they relate to administrative management – particularly the maintenance of sound control combined with the reduction of unproductive rules.

The principles are aimed at public sector organizations – that is, to government entities (and to managers, auditors, legislators and other interested persons) at the federal, provincial and territorial levels in Canada. The principles should be viewed as integrated. A government wanting to make room for innovation should pay attention to all of the draft principles, not just a small subset of them.

[11] It is important to note that innovation does not always involve achieving the same mandate in a more efficient and effective manner (doing the same thing but in a more operationally efficient manner). Innovation can often involve alternative service delivery or public/private partnerships where a government organization gets out of the business of direct program delivery altogether. In these cases, the entity has become innovative by literally changing its mandate – and delivering the service on a contractual rather than a direct-service-delivery basis.

[12] Public Policy Forum, *Innovation and Risk-Taking: An Industry Canada Perspective*, Background document for a Roundtable Discussion to be held on behalf of the Office of the Auditor General (October 6, 1998).

[13] See both Mulgan and Albury as quoted in IDEA Knowledge, *Innovation in Public Services: Literature Review* (September 2005), p. 2; and Public Policy Forum, *Innovation and Risk-Taking*, *op. cit*.

[14] Mulgan and Albury (2003) as quoted in IDEA Knowledge, *Innovation in Public Services*, op. cit., p. 24; and as supplemented by CCAF analysis. Note that in any public sector organization, innovation is likely to move through four main stages:

**Creativity** and generating possibilities (how ideas are stimulated and supported).
**Incubating and prototyping** (the mechanisms that are used to develop ideas and manage associated risks).
**Replicating and scaling** up (the promotion of effective and timely diffusion of successful innovation).
**Analyzing and learning** (evaluation of what works with a view to promoting continuous learning and improvement in public services.

(See D. Albury & G. Mulgan, *Innovation in the Public Sector* [UK Cabinet Strategy Unit, October 2003], p. 10. Although critical, learning tends to be the most often neglected element in the innovation process.)

[15] Dinsdale, *op. cit.,* p. 13. The definition was slightly changed by CCAF to emphasize the idea of "initiative."

[16] IDEA Knowledge, *op. cit.*, pp. 6 and 9. In each of these areas, the magnitude or impact of innovative projects can range widely:

**Incremental** innovations represent minor changes to existing services or processes. These do not attract headlines and rarely change how organizations are structured. However, they can add up over time to make continuous improvements in operational efficiency, program effectiveness and overall value-for-money.

**Radica**l innovations are less frequent and involve either the development of new services or the introduction of fundamentally new ways of doing things in terms of organizational processes or service delivery. They can bring about a significant improvement in performance for the innovating organization and alter the expectations of service users.

**Transformative/Systemic** innovations give rise to new workforce structures and new types of organization. They transform entire sectors and dramatically change relationships between organizations. Transformative innovations are rare and take decades to have their full effect, requiring fundamental changes in organizational, social and cultural arrangements.

(See Mulgan and Albury, *Innovation in the Public Sector*, *op. cit., and* as quoted in *Innovation in Public Services Literature Review*, *op. cit.*, p.6.

[17] Dinsdale, *op. cit.,* p. 14.

[18] *Ibid*., p. 16.

[19] Barriers to innovation tend to fall into three main classes:

Those that arise **within** the organization. These can include hostile or skeptical attitudes; turf fights; difficulty in coordinating organizations; logistical problems; difficulty in maintaining the enthusiasm of staff; difficulty in introducing new technology; union opposition; middle management resistance; and general opposition to entrepreneurial action.

Obstacles that arise **in the government environment** – resource, legislative or regulatory constraints, or the opposition of elected officials.

Barriers that exist in the **external** environment, for example public doubts about the effectiveness of programs; difficulty in reaching the program's target group; opposition by those affected in the private sector (including entities that would experience increased competition) and general public opposition or skepticism.

(See Sandford Borins, *The Challenge of Innovating in Government* (PricewaterhouseCoopers Endowment for The Business of Government – Innovation, Abramson & Littman ed. 2001), pp. 59105. This is as it is quoted in *Innovating in Public Services: Literature Review, op. cit.,* pp. 2526.)

Becoming entrepreneurial represents a major **cultural shift,** something that can only be achieved through a persistent breaking down of barriers and a realignment of incentives. Cultural change is difficult to effect but if persistent signals are sent from leaders in central agencies to ministries (and from managers to staff) – and predictable rewards, sanctions and incentives are offered – it can occur.

[20] *Ibid*. As quoted in Innovating in *Public Services: Literature Review*, *op. cit*., pp. 25-26.

[21] Albury, *Innovation in the Public Sector*, *op. cit*. As quoted in *Innovation in Public Services; Literature Review*, *op. cit.,* pp. 2425.

[22] These factors are based on a number of sources quoted in *Innovation in Public Services; Literature Search*, *op. cit*., pp. 20-23 including Osbourne and Plastrik's (2000) field book for government re-inventors, Light's (1998) work on innovative non-profits and small public sector organizations and Borins (2001). CCAF views are also added.

[23] (J.M. Howell, C.M. Shea & C.A. Higgins, "Champions of Product Innovations: Defining, Developing and Validating a Measure of Champion Behavior" in *Journal of Business Venturing*, vol. 20, no. 5, pp. 641-661.) as quoted in *Innovation in Public Services: Literature Search*, op. cit., p. 22.

[24] (*Ibid*.) as quoted in *Innovation in Public Services: Literature Search*, *op. cit*., p. 22.

[25] (Tom Ling, *Innovation: Lessons from the Private Sector,* A 'think piece' in support of the Invest to Save Study [November 2002].) as quoted in *Innovation in Public Services: Literature Search*, *op. cit*., p. 22.

[26] This is essentially a program evaluator's needs assessment tool kit.

[27] Office of the Auditor General of Canada, *2002 Report of the Auditor General of Canada – Chapter 9: Modernizing Accountability in the Public Service* (December 2002), p. 2.

[28] Trust also depends on recognizing that even when innovative projects are well managed, and subject to modern notions of accountability, some will inevitably fail to deliver hoped-for results. The key to encouraging innovation is to find the right balance or tolerance zone between risk-aversion and risk-taking, and ensuring that there is a common understanding of where that zone is. See also Public Policy Forum, *Innovation and Risk-Taking*, *op. cit*. This idea is discussed in more detail under principle one.

[29] Adapted from the Office of the Auditor General of Canada, *2002 Report*, Chapter 9, *op. cit*., p. 2. An accountability body could be a committee (eg. a legislative Public Accounts Committee) or an individual, say the deputy head of the Ministry.

[30] *Ibid*., p. 1. Until recently, the concept of accountability was seen as a simple relationship – managers were to be given the responsibility and resources to do a job and then held to account for what was achieved. More

modern notions of accountability require managers to account not only for what was achieved, but also for how it was done. Modern notions of control require this latter definition of accountability.

[31] Readers should note that the following discussion refers to the discipline of risk management as it relates to the reduction of administrative rules and the encouragement of innovation to improve efficiency and effectiveness. It is a focused discussion and does not, for example, cover the broad idea of enterprise-wide risk – something that encompasses all forms of risk management activity, for all kinds of purposes, across an entire organization. **While CCAF might have distinguished types of risks more linked to the calibration of administrative rules – for example, strategic vs. operational – a choice was made to use the simple generic terms, "risk" and "risk management" in this document. Readers of this document while it is in its discussion stage may wish to comment on this.**

[32] A well-managed public sector entity should be guided by a sound understanding of the risks it aims to mitigate and the administrative costs associated with any new rules. Administrative rules that constrain efficient management and innovation should not go into place unless they are proportional to, risk. Rules already in place – and whose burden is disproportionate to the risks they address – should be reviewed, modified or eliminated (principle four). In either case, the proper design and adjustment of rules requires first, a capacity to measure and manage risk.

[33] Her Majesty's Treasury (UK), *The Orange Book: Management of Risk – Principles and Concepts* (Her Majesty's Stationary Office, October 2004), p. 7.

[34] Uncertainties in the operating environment are a daily reality. Many risks are unique to the organization and result from differences in objectives; the size, complexity, reach and public visibility of the organization; the amount of money spent; the differing nature and expectations of clients; the sensitivity and value of financial or citizen-related data; and the requirements for system reliability, availability and performance. The risks noted in the main text are adapted from the UK NAO, *Supporting Innovation*, *op. cit.*, p. 1. The link between rules and risk was added by CCAF.

[35] UK NAO, *Supporting Innovation*, *op. cit.,* p. 2.

[36] One useful public sector model may be sourced from the *UK HM Treasury's Orange Book*, *op. cit.* This model is summarized below because it encompasses most of the common features found in many risk management models.

**Step 1: Identify Risks**

Initial risk identification occurs when an organization is beginning to incorporate risk management into its work, and continuous risk identification occurs when the entity has bought into the approach and begun to identify risks on a routine basis.

**Step 2: Assess Threats and Opportunities**

In step 2, managers categorize risks and create a risk profile. They then assess those risks to judge likelihood of occurrence and potential impact. As organizations establish risk tolerances and overall risk appetite, managers should take two perspectives. When considering threats, they should judge the level of exposure considered acceptable should that risk be realized; when considering opportunities to innovate and improve performance (positive risks), they should assess how much they are willing to risk to obtain the possible benefits.

**Step 3: Address the Risks**

Public sector managers may decide to address uncertainty in any of four ways:

*Tolerate* – This may be the only reasonable course if the proposed activity is necessary or the costs of taking action are prohibitive.

*Treat* – Managers can treat or mitigate the risk, while continuing the activity. This makes sense when the administrative costs of treatment are reasonable. The "residual risk" after treatment should be acceptable, justifiable, and within the risk appetite.

*Transfer* – This often applies to financial matters where a risk might be transferred to another party. Financial risk is often transferred in the private sector through conventional insurance, though this option is not always available to public sector managers.

*Terminate* – Where risks jeopardize the reputation or even the existence of the entity, managers may conclude that the underlying activities are unacceptable.

**Step 4: Monitoring, Reporting, Communicating and Learning**

Managers should regularly monitor the environment in order to keep the risk profile current, relevant and applicable. They should be prepared to eliminate administrative rules that are costly and disproportionate to risk, and no longer make sense (see principle four).

Managers should play a leadership role and support communication to disseminate best practices from one unit to another. In particular, they should communicate the "opportunity side" of uncertainty and encourage employees to take reasonable risks in support of innovative projects that can improve productivity (see principle three).

[37] UK NAO, *Supporting Innovation*, *op. cit.,* p. 2.

[38] *Ibid*., p. 69. Supplemented by CCAF analysis.

[39] *Ibid*., Annex 1, supplemented by a review of the Government of Canada's Management Accountability Framework, and by CCAF analysis.

[40] Office of the Comptroller General of Canada. *Core Management Controls (Draft)*, (November 2007), section on risk management. When it comes to external monitoring, public sector organizations might include the scanning of economic, regulatory and commercial factors, as well as the measurement of client satisfaction. Internally, managers should monitor factors such as employee demographics, labour relations, and financial and operational results.

[41] *Ibid*., Section on people management.

[42] Treasury Board of Canada Secretariat, *Framework for Management Compliance (Draft)* [February 5, 2008], Clause 7.1.3.

[43] Australian Public Service Commission, *Reducing Red Tape in the Australian Public Service – Management Advisory Report No. 7* (2007), p. 2.

[44] Office of the Auditor General of Canada, *2002 Report*, Chapter 9, *op. cit.*, paragraph 9.68. In order to innovate, take reasonable risks, and learn from mistakes, managers need a degree of discretion and flexibility to act. Too many rules and procedures can impede innovation and lead to inefficiency, ineffectiveness, and frustration.

[45] Treasury Board of Canada Secretariat, *Untangling the "Web of Rules": Towards a New Management Regime*, Presentation by Wayne G. Wouters to the Advisory Committee on the Public Service (January 2008), Annex A "The Smart Rules Charter".

[46] When a rule is respected, the underlying determinants are that it has clear accountabilities regarding who is required to do what, it is easily monitored and there are consequences for non-compliance. See principle five for a fuller discussion.

[47] Office of the Auditor General of Canada, *2002 Report,* Chapter 9, *op. cit.*, p. 8.

[48] Four basic sets of values are at play here:

**Respect for democracy** recognizes that authority rests with elected officials who are accountable to legislatures and to citizens. A well-performing public sector organization emphasizes respect for democracy. It manages delegated authority in a professional manner and provides ministers, legislators and Canadians with timely and accurate information on the results of its work.

**Professional values** require employees to provide high-quality, impartial policy advice while committing to the design, delivery and continuous improvement of programs and services. Professional values emphasize stewardship, duty of office and care, and protection of assets. They also emphasize innovation aimed at improving the cost-effectiveness of processes, programs and services, provided that this occurs in a managed way, with due regard to risks and the need for sound management control.

**Ethical values** (integrity, trust and honesty) are the cornerstone of sound control. They require public servants to support the common good at all times. They recognize the need for openness, transparency and accountability in what is done and how it is done.

**People values** include courage, decency, responsibility and humanity. In a healthy workplace they demonstrate themselves in respect, civility, fairness and caring. Values-driven organizations support learning and are led through participation, openness, communication and a respect for diversity.

See "Sheila Fraser, Efficacy and Adaptability of Government: The Post-Gomery Reality – A Panel Discussion: Accountability or Suffocation?, Speech to Queen's School of Policy Studies (April 28, 2006)". See also Results for Canadians and the John Tait Report on Values and Ethics. It is notable that innovation (mentioned here under "professional values") does not always make its way into values and ethics codes.

49 *Ibid*.

50 Office of the Comptroller General of Canada, *Core*, *op. cit.,* pp. 15-16.

51 There are likely five main purposes to hard controls:

**Directive** – providing high level, obligatory direction from legislatures, governance bodies, standards organizations, central agencies and other authoritative groups. These can range from the strategic (legislation setting out organizational mandate) to the operational (government-wide administrative policies).

**Preventive** – activities or processes designed to prevent or reduce the impact of errors or malfeasance. An example is the segregation of incompatible duties (where a person is not able to both commit and conceal). Another is a simple inventory of assets.

**Detective** – activities or processes designed to detect errors or malfeasance, for example internal audit or a periodic inventory count.

**Corrective** – activities or processes that correct errors or malice in a timely manner.

**Recovery** – activities or processes designed to recover from errors, malice or other undesirable events; for example, disaster recovery or business continuation plans.

(See the University of Victoria Internal Audit Website – Activities Section.)

52 When control instruments are allowed to proliferate, this ratio of activities to instruments (many activities for each instrument) can lead to an exponential increase in administrative workload, cost and burden.

53 CICA, *Guidance on Control*, *op. cit.*, paragraphs 98-99.

54 Geneviève Lépine, *The Web of Rules: A Study of the Relationship Between Regulation of Public Servants and Past Public Service Reform Initiatives* (Public Policy Forum) September 2007); & Sandra Nutley, "Public Manager 2010: A Recognizable Future?" in *Public Money & Management* (January-March 2000), p. 6-8.

55 Risk in this case means both operational risk and risk associated with possible changes in the outside environment.

56 Although the idea of tailored rules can apply to both internal administrative matters and to external activities – for example, to the rules that apply to organizations in receipt of government grants and contributions – the management principles in this document are meant to deal with the "internal" web of rules only. At the federal level, an excellent report on external administrative burdens associated with G&C programming was produced by a blue ribbon panel. (See *From Red Tape to Clear Results*, Government of Canada, 2007.)

57 When central agencies and senior ministry officials are considering tailored rules, they should ask whether the demonstration of sound public service values and existing management capacity are sufficient to mitigate risk. At the highest general level, central agencies and public sector executive committees might start by asking ten main questions:

Have we put in place the conditions for effective **strategic direction** and delivery of results?

Have we taken unequivocal steps to reinforce the importance of public sector **values and ethics** (democratic, professional, ethical and people values)?

Have we secured the **right people and work environment** to assure success?

Is our **resource stewardship** (relative to assets, money and people) integrated and effective, and are its underlying principles clear to all staff?

Have we defined the context and practices for **managing and integrating risk** into corporate decision-making?

Is information on program **results** gathered and used to make decisions, and is performance reporting balanced, defensible, and easy to understand?

Have we secured the **policy development capacity** required to serve our Minister and support government-wide priorities effectively?

Are **clearly assigned responsibilities and authorities** for results consistent with resources and capabilities?

Are partnerships skilfully managed, policies and programs developed from the 'outside in', and **services** citizen-centred?

Do we encourage **innovation,** promote organizational **learning** and anticipate and adapt to change?

These questions come from work done in January 2003 by the Federal Office of the Comptroller General as a precursor to the development of the Management Accountability Framework.

58 If the study group is within a ministry, some combination of headquarters and regional staff, including operational employees and functional specialists, may be appropriate.

59 These tests were developed from initial work done by the Federal Treasury Board Secretariat in early 2008. Test 2 on cost estimation requires an administrative rules costing model. Examples exist in Canada and in other OECD countries including the Netherlands and Australia. Tests 3 and 4 were added based on CCAF analysis, and some reference to Reducing Red Tape in the APS (p. 11) has been made. The responses to these tests depend to a considerable extent on existing risks and the internal management capacity of the organization. Where risks are mitigated and management capacity is adequate, control may be exercised less through formal rules and processes (hard controls) and more through the ongoing monitoring of performance.

60 Australian Public Service Commission, *op. cit.*

61 *Ibid.,* pp. 5 and 9.

62 In assessing rationale, managers might ask whether:

the core issue of concern – the risk – is defined at the outset and the proposed rule is proportionate to that risk at hand;

the reasons behind the proposed rule are clear, and the rule is clear about what it requires from staff; and

alternatives such as the use of moral suasion, education in values and ethics, or the building of management capacity have been considered and found to be insufficient.

63 Examples of administrative rule costing models and review processes exist in several public sector jurisdictions and managers should benchmark their approaches against leading international practices to draw on lessons learned.

The Australian Business Cost Calculator User Guide (Department of Finance and Deregulation, October 2006, p. 6) sets out a detailed categorization of costs that is summarized below. Compliance costs fall into several categories and can impact stakeholders in ways that are not always considered by rule makers. For example:

**Notification**: Reporting transactions to a ministerial or central agency authority before or after the event – for example on expenses made or people hired.

**Education**: Maintaining awareness of legislation and regulations, and the costs of keeping abreast of changes. Education costs occur even when an area is deregulated, as employees must get used to the new environment.

**Permission**: Seeking permission inside or outside the organization to undertake an activity, for example spending from a controlled budgetary allotment, or purchasing a capital good, or hiring a new employee. Considerable delay and cost can incur in the processes and procedures associated with permission.

**Purchases**: Costs of all materials and equipment purchased in order to comply with the rule.

**Records**: Keeping all transactional documents up to date and accessible.

**Enforcement**: Inspections, audits and evaluations as well as the costs of remedial action.

**Publication**: Costs associated with reporting compliance, for example in reports from a ministry to the legislature in respect of a given piece of legislation.

**Procedural**: Costs of doing non-administrative (non-paperwork) tasks, for example in hiring new people to implement or enforce the rule or in conducting normal management monitoring to ensure that the rule is being followed.

This electronic cost calculator is used in Australia to estimate the compliance costs of both internal and external rules and regulations. It was adapted from the Standard Cost Model, first developed in the Netherlands and later adopted by the OECD as a recommended practice. This standard cost model could be easily adapted to the requirements of other public sector jurisdictions and could be presented in hard copy or in electronic form. (See OECD, Cutting Red Tape: Comparing Administrative Burdens Across Countries – OECD 2007 and Administrative Simplification in the Netherlands – OECD 2007.)

Of course, any standard cost model can only deal with those factors that are quantifiable. It would be useful to recognize that less tangible costs should also be taken into account when they are material – for example, the appearance of an implicit sanction, leading to a negative impact on staff morale (advice of Michael Joyce, Queen's University July 18, 08).

[64] Australian Public Service Commission, *op. cit.,* p. 15.

[65] *Ibid.,* p. 13.

[66] Sheila Fraser, *Efficacy and Adaptability of Government*, *op. cit*.

To add to the ideas underlying this speech, compliance means that the rules are known, understood and followed. Managers should clearly communicate to employees both the need to maintain a robust environment of internal control, and the consequences of not doing so. Organizations might consider reinforcing this with an independent oversight function (e.g., an ombudsman) to manage cases concerning ethical questions.

[67] Office of the Auditor General of Canada, *2002 Report*, Chapter 9, *op. cit.*, paragraph 9.49.

[68] Treasury Board of Canada Secretariat, *Framework*, *op. cit.*, paragraph 3.2.

[69] Office of the Comptroller General of Canada, *Core*, *op. cit*.

[70] Treasury Board of Canada Secretariat*, Framework*, *op. cit.*, paragraph 9.2.

[71] *Ibid*., Annexes C and D.

[72] *Ibid.,* paragraph 9.67.

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