THE MARKET SURROGATE OBLIGATION OF PUBLIC SECTOR BOARDS

by

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Condensed from a longer unpublished manuscript co-authored with Ricarda Steeb.

The role of the governing board may vary considerably in practice, but in theory it is always that body which sets basic organizational values. Those values include the definition of the business to be engaged in and the return on resources to be achieved. Whether a given board decides, delegates or defaults, its accountability for core issues remains.

I find it convenient to divide organizations into market and nonmarket. This differentiation is roughly the same as profit-nonprofit if government is considered in the latter category; my implication is that the market status is of greater import than whether equity ownership exists and earnings are distributed. A board of an organization which competes in the marketplace ordinarily intends to create sufficient surplus value to enable a profitable return on equity. In order to make that return, the board’s organization must exchange enough of its product with consumers at a price sufficiently over its cost.

The effects of the market are profound. The characteristics of the marketplace phenomenon have been discussed both controversially and extensively since before the explosion of free market economics following publication of Wealth of Nations by Adam Smith in the mid-nineteenth century.

Boards which do not compete in the marketplace, however, make up an increasing share of our national economic activity. Non-profit organizations comprise a rapidly growing sector whose advancing size far outstrips our grasp of its nature, management and collective impact. Government, also a nonmarket enterprise, has experienced a striking growth.

DILEMMAS OF THE NONMARKET

There are a number of consequences which bear directly upon the basic job of the governing board when an organization has no market in which to compete. These conditions apply to mental health centers, school systems, housing authorities, county commissioners and the long list of non-market entities. They include the following:

1. The basic and critical link is usually broken between paying for and receiving a good or service. This fundamental exchange of value between purchaser and vendor is the core of commerce.

2. There is no automatic economic measurement of whether a product is worth the resources consumed in its production. Hence, the “value swap” is a circuitous one.

3. The meaning and usefulness of the concept of “bottom line” is sharply attenuated. There is characteristically no integrating or summarizing measure analogous to profit, market share or return on investment, though the utility of such a concept to measure and to promote managerial excellence is great.

4. Innovation, which is a creative recombination of means to achieve ends better, becomes less meaningful. In the absence of clear bottom lines to monitor, nonmarket agencies ask only that innovations be interesting and different.

THE VERBAL MARKET

In the absence of a market on which to base decisions, nonmarket entities employ a verbal process to decide about products, costs, distribution, quality and other characteristics of product and consumer. Boards or employees deliberate what would be “good” to engage in, what human needs are more important than others and what levels of quality are worth their cost. Congress, legislatures and agency boards all engage in this “rhetorical market.”

Such verbal processes in groups may appear to be more human, less mechanistic and more rational than the automatic market process. Yet they are open to some rather predictable pitfalls. Of those, focusing on means rather than ends may be the most destructive. Governmental and non-profit boards, for example, invariably dictate the means to be used by subordinates in producing some outcome value without having sufficiently defined the expected outcome value itself. “Quality services” of some kind are often emphasized when the ends toward which those service activities are ostensibly aimed are not adequately stated. Prescribing means is socially safer than ends in that means may rest for definition on what is acceptable among influential guilds or upon what is standard.

Resource allocation is oriented toward safe and generally agreed upon “good” activities. These usually support established professions and the methods in which they have strongly vested interest. This results in immersion in activities rather than in orientation toward results. Assurance of the link between purpose and performance is thereby unfulfilled. Nonmarket agencies can, in fact, fail miserably for years and never know it.

Yet much machinery is in place to carry out and monitor funded activities. Federal and state bureaucracies are virtual activities machines. They justify their
existence on busy performance of means rather than on results. Success comes to be defined as maintaining the size and complexity of the machinery thus set in motion.

THE MARKET SURROGATE OBLIGATION

Because these phenomena are made more likely due to lack of a market, nonmarket boards have an obligation to perform a market surrogate function. In not explicitly recognizing the insidious effects of the nonmarket condition, boards fail to give deliberate and studied attention to offsetting the difficulties.

This is a peculiar responsibility. The board of a corporation competing in the marketplace must adequately predict the actions of a market, but at no time need it act as market surrogate.

The closest that nonmarket boards come to fulfilling the market surrogate function is in making needs assessment studies. But such assessment of needs, though necessary, may delude the board into believing that it has addressed the market deficit. Even the most professional needs assessment can fall short by focusing on solutions rather than needs, failing to consider opportunity costs and being inappropriately objective.

Needs are often assessed in terms of the amounts of some "answer" which is deficient or missing. Mental health authorities study to determine how many psychiatric beds are needed; public schools speak of the number of teachers needed. We tend to define human needs in terms of the answers in which we have investment and in the language of today's and even yesterday's technology.

Further, the social service mentality rarely considers opportunity cost, those values which are given up in order to achieve the need-relief sought. Considering opportunity cost allows us to make the kind of comparison which a consumer would have to make, for we are choosing to expend resources for one need rather than spend for the relief of some competing need. This is, by its nature, an inescapable apples-and-oranges comparison. It is not enough that a need be addressed, but that its relief be brought about at the forfeiture of only lesser values. Needs assessment studies ignore this issue; the market surrogate role cannot.

Finally, a needs assessment often seeks to find some objective level of need. To construct a needs assessment as a quantification of identifiable characteristics is legitimate, but it is presumptuous to accept that this enumeration indicates what should be done. A market defines what people want at what cost.

Fulfilling the market surrogate obligation calls for a bottom line mentality on the part of the nonmarket board far beyond what is now the case. Boards will be called upon to develop mechanisms to enable increas-ingly refined judgments of what effect is worth foregoing what other effects. This is as if they were individual purchasers or, more to the point, as if they were responsibly exercising their roles as purchasing agents for the public.

At first glance it seems impossibly complex to determine the values of ten children learning to read, of a chronically disturbed person being able to live independently, of 20% more diversified employment base for a community. School boards, mental health trustees and economic development commissions make such choices routinely; legislatures choose across these dissimilar values. Yet in board and statehouse alike, the choices are ordinarily made by default. Critical public policy (public values) are determined by implicit rather than explicit means. There is no argument about whether we are omniscient enough to make such choices; we have no way to avoid them.

TRAPS ON THE WAY TO RESPONSIBILITY

If decisions akin, in their stark explicitness, to judgments of the market cannot be avoided, how is it that governing boards are able routinely to pretend that they can be? The answer is as old as human foibles and as current as the flawed process of the modern board. I have described elsewhere the problems and promises of conventional board process. With respect to the market surrogate obligation, boards' shortcomings in the normal course of things are to be expected. Speaking competently for a non-existent market is difficult no doubt, but difficulty alone is not the controlling factor.

We are often frightened by any process which exposes our values to the scrutiny of others. The absolute explicitness called for in fulfilling the market surrogate function renders indirectness and implicitness difficult to maintain. Allowing values to go unstated would cause few problems if we had an automatic way to sum our unverbalized choices in the way that the market does that for the private sector. But faced with a situation wherein a market mechanism is unavailable to us, we use whatever escapes we can to avoid explicit value deliberation.

Enunciating public value is a weighty proposition which few of us feel enfranchised or wise enough to carry out. Therefore, we will try to convince ourselves and others that we are not making such sweeping choices even though boards have no way to escape doing so. In protest, we will contend that there are no perfect or even acceptable measures of the public will. Therefore, we bring puristic, academic criticism to bear on every measure or tool which might be used. We do so without suggesting better ones and without recognizing that we are making implicit choices all the while.

The market surrogate obligation, in being concerned