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Institutional Risk of Russian Public Sector Organizations Management

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Abstract

The Government of the Russian Federation has been overhauling a public sector of economy since 2010. One of the transformation's goals is a gradual reduction of public spending on the public-sector organizations, and simultaneous increase in efficiency of their economic activity and in the quality of rendered public services. After the federal law on the legal status of public (municipal) institutions improvement came into force, the operating mechanisms and internal institutional links of public sector organizations have been changed, including full participation of public sector organizations in market relations. For instance, budgetary funds are allocated on contractual basis in form of government tasks. However, the significant improvements have not been achieved. Experts have a common ground in reasons of organizational fails. Among them are poor quality of planning, goal setting, and incorrect setting of development indicators' target values.

Keywords: Institutional risks, public sector organizations, institutional environment, target indicators, institutional traps.

Introduction

The indicative management involves planned changes in management objects through sequential implementation of actions aimed at target indicators values achievement. Target indicators are the management system key elements specifying the managerial impact modes and directions, and, consequently, the required resources. A proper target indicator's value determines, in large measure, the effectiveness of all planned actions.

Only the last alternative (the initially inaccurate value), caused by low qualification of employees', imperfect information, inadequacy of calculation tools, and other objective factors, is acceptable in the neoclassical economics. The mistake will be identified and corrected, and the action plans and indicators values adjustment will get back the controlled object on required vector of development. Even if, however, the economic operator, which made a mistake, does not identify and eliminate it, the market mechanisms will drive the operator to do it, for example, through competition, because if competitors use more exact target (planned) indicators they will get a market advantage [1-6]. The neoclassicists believe that homo economicus (consumer, entrepreneur, and enterprise) is always aimed at income maximization and cost minimization. So, initially inaccurate target indicators description in the system is irrational, and, consequently, is impossible, but institutional economics research suggests otherwise. The economic subjects, affected predictably irrational motivation, may and often have made mistakes in setting target indicators values [7]. In this case, it should go along with Russian philosopher A. Zinoviev, who pointed out that "… only naive people can believe the market is let run its own course, left to itself, and some mythic "invisible hand".

Economics research in market risk and institutions dysfunction leads the academic community to realization the existing of various social and economic actors, other than traditional risks caused by environmental uncertainty, such as institutional risks [8]. With the papers of D. North [9], R. Coase [10], R. Merton [11], A. Auzan [12], V. Tambovtsev [13], V. Polterovich [14], O. Sukharev [15] and others, the notion of "institutional risk" was introduced in economics, research of institutional risks' causes, factors, and socio-economic environment exposures to risk began.

In general, the institutional risk is a probability of non-conforming event caused by economic subjects' opportunist behavior, institutional environment imperfection, and institutions' irrationality [16].

Purpose of Research

The purpose of research is to consider and to visualize institutional risks' influence on public sector organizations' current activities aimed on controlled object's planned changes using target indicators.

Methodology

The research is based on principles of dialectical logic, systematic and institutional approach to analyzing the economic phenomena and processes; on analysis and generalization of indicative management theoretical and empirical findings throughout the world. The substantiated, and widely used scientific approaches, such as selection, distribution, comparison, generalization, problem and hypothetical knowledge, forecasting, graphical description, were used to get a new scientific knowledge.

Findings

1. Institutional traps. Institutional traps in public sector had arisen from direct government involvement, as it is impossible to provide citizens with public goods through market-based instruments. Institutional traps receive adequate attention in academic literature. This research is focused on traps directly related to defining the goals of public sector organizations' activities and values of target indicators selection.

Management entities of public sector are: 1) the Government of the Russian Federation (GRF) defines general social policy; 2) State Institutions (SI), are the government agents responsible for organization of social policy implementation and its tasks fulfillment; 3) Public sector organizations are the direct executors that provide citizens with public services.

Fig. 1 (authors' original figure) illustrates scheme of management entities' balanced effect on public sector: public sector organizations deliver services at optimal price (P^{optim}) which provides full cost recovery from resources of all level budgets; the amount and range of services available to citizens (Q^{max}) in public sector organizations supported with financing are established by the Government of the Russian Federation; state institutions control that the range of services available to citizens in these organizations may not be lower than the minimum range (Q^{min}). In practice, the distortions exist. On the one hand, the Government of the Russian Federation seeks to minimize the value of state obligations and social guarantees by putting the financial burden of social services provision on public sector organizations. Nominally citizens may claim a wide range of services (Fig. 1b, point Q^{max}). But owing to difficulties caused by reducing the price to prime cost (P^{min}), the public-sector organizations limit availability of their services or start charging their customers. On the other hand, public sector organizations are uninterested in providing the wide range of services. On the contrary, these organizations seeking for maximum state financial support (Fig 1b, point P^{max}) tend to limit the range of provided services (Fig. 1b, point Q^{min}) to the minimum. A failure to provide this minimum range will lead to adverse impacts.

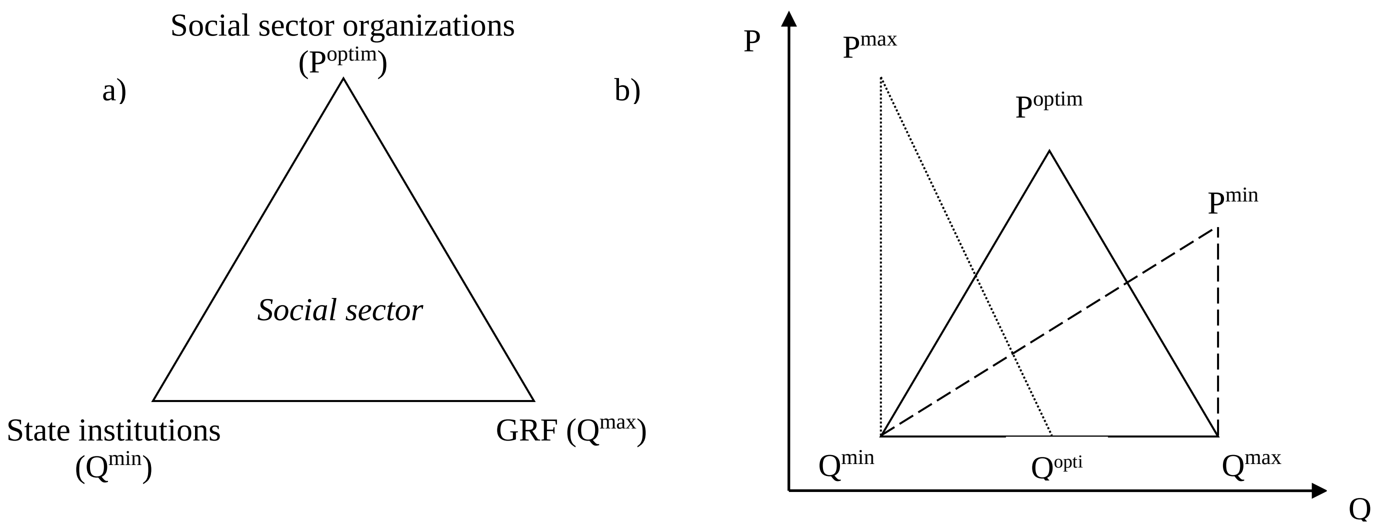

Figure 1. Impact of management entities on public sector

The described contradiction defines public sector bias towards the GRF or public-sector organizations. However, the state institutions do not participate in public sector development, but only maintain the minimum range of social services actually rendered.

It can be inferred that none of the management entities pursue the sustainable development of public sector, as the objectives of their activities are opposed to target indicators values. Fails of ongoing social reforms are largely caused by it; as, in the preparation of transformation, the goal setting is based on traditional approaches to management, which implies a rational behavior of economic entities interested in single final outcome. The Accounts Chamber of the Russian Federation notes that "many of state programs goals completely lack specificity, vague, and are not sufficiently aligned with objectives of state programs. The typical situation would be where the goal achievement is not provided by any objective, or where the objective is not aimed at any goal achievement, are typical" [17].

Unbalanced interests of public sector's actors determine the institutional traps emergence. In authors' opinion, these institutional traps have a direct effect on the performance of public sector organizations' management functions (planning, organizing, motivating, controlling):

1) Goal setting based on subjective vision of controlled object ideal state. State institution, entitled to set goals for public sector organizations, is guided by own vision of controlled object development in future. But the necessity of current situation analysis and translation of external environment overall uncertainty into risks to organize effective management (planning function of management) is neglected.

2) Different stakeholders' interests' collision in determining approaches to measurement of goals accomplishment. Having intuitive notion of abovementioned institutional traps, at the goal-setting stage the management entities of different levels are trying to state the goal in such a way as to have an opportunity to prolong the term for its execution or to call for additional financing (planning function of management).

3) Imprecise planning of resource requirements for goal accomplishment. Lack of any significant for management entities punishment for failure to accomplish goals, leads to superficial analysis of resource requirements that does not take unexpected and hidden costs into account, or to sequestration of spending during the execution phase (planning and motivation functions of management).

4) The intention of shifting responsibility for stated goal achievement on subordinated management level without agreement on time frame, content, resources, and other items related to goal achievement (motivation function of management).

5) Politicization of public sector development goals. Due to the lack of real public control, the state institutions can set knowingly unachievable or populist goals without exact execution term, and use these goals for political purposes.

In consideration of the foregoing, it can be assumed that if target indicators values setting were influenced by institutional traps (ITr), there is a high probability, that current operations of public sector organizations would be exposed to the standard institutional risks. These risks are represented in regional public-sector system by specific institutional norms (traps) or actors affecting the planned activities', aimed at target values achievement, delivery time and/or cost of implementation.

Under the Federal Law of the Russian Federation of June 28, 2014, No. 172-FZ "About strategic planning in the Russian Federation" the achievement of national policy strategic goals and objectives, including public sector, is implemented through state programs. 44 national programs are categorized under five blocks. In 2015 twelve state programs in the “New Quality of Life” block were implemented, target values of 700 indicators were defined. Only 421 of indicators’ target values were achieved (60.1% of the total amount), 147 were not achieved (21% of the total amount), and for 132 indicators (18,9% of the total amount) no data was presented.

Table 1

Volume of financing for the state program of the Russian Federation in 2015 (in thousands of Russian Roubles)

No.	Block name	Planned volume of financing	Volume of assimilated funds	Execution, %
1	“New Quality of Life”	3 527 724 657.20	3 492 212 958.00	99.0
2	« Innovative Development and Modernization of the Economy »	2 315 641 511.90	2 241 660 425.70	96.8
3	«Balanced Regional Development»	717 591 632.30	714 068 977.10	99.5
4	«Efficient state»	1 298 843 394.80	1 264 804 866.80	97.4
	Total	7 859 801 196.20	7 712 747 227.60	98.1

Despite the target indicators’ partial performance, the funds allocated for these programs were used to almost full extent (Tab. 1) [18].

2. Institutional uncertainty. Initially, uncertainty is a philosophical category, as it concerns the sphere of knowledge, the transition from unknown to explored field. The future cannot always be described as the result of some objective laws or trends proposed by researchers. According to Heisenberg’s uncertainty principle not only the future is undefined, but even present cannot be measured, so uncertainty is a “fundamental, required property of our world” [19].

Uncertainty is a lack of predetermined outcomes and limits. Uncertainty of the future means that the future is infinite and has no alternative. In this regard, turning uncertainty into certainty is impossible. Any algorithms claiming to describe the future, can effectively solve certain problems in a short-term horizon, but they cannot be regarded as something universal and given once and forever [20].

Institutions are able only to protect from uncertainty, but not to eliminate it. Specifying an action plan, building up the matrix of repeated procedures, institutions construct validity, which, according to Hannah Arendt, stays in the context of reality with all its uncertainty. This description leads to the conclusion that institutions are the rules, possible situations, when there is no need for future determination, but for keeping the present and for standing reproduction of achieved, until it's efficient [21,22].

Based on D. Moskovkin's research [19, 23] the institutional uncertainty can be described as a situation where interested actors do not reach a compromise on the procedures and rules, and the rules are constantly changing and sporadic. As a result, the institutional uncertainty has an indirect effect on the selection of target indicators' values. This enables to preserve the current state of affairs. Despite the strategic targets of public sector development are set at federal level, the regional actors tend to fix values of general management indicators on current values. For instance, the actual values of considerable number of indicators in the "New Quality of Life" block in 2015 exceed their planned values. Also, some plans of sate programs' implementation for 2014 -2016 were mechanically corrected in the second half of 2015, to adjust the dates of planned milestones to actual reported dates.

3. Institutional irrationality

Is a performance of certain actions aimed on performance, but not on the achievement of defined results. In authors' opinion in public sector these actions translated into peculiarities of public sector organizations as objects of management. The following are examples of these peculiarities. 1) Diversification of provided services. Wide range of social services, which are necessary for costumers, requires a system that ensures a proper functioning of public sector organizations of different types at the macro level, and the variety of social services provision, in accordance with public sector organization's specialization, at micro level. 2) Social service delivery process standardization and algorithmization. The process of social service delivery is considered as a set of specific actions related to costumer's problem determination and solution. Lack of standardization and algorithmization often leads to mutually exclusive results of actual services rendered to public, and services recorded in primary sources and report forms. 3) The complexity of the internal social processes coordination. The social services extension is related to increasingly greater number of participants' involvement. As any single employee, that provides particular services, does not see the use fullness of his job, so the duration of service provision increases and efficiency of resource utilization monitoring decreases. 4) Commercialization and customer orientation requires the simultaneous subordination and respect constitutional rights to life, to protection of health, to medical care, to a decent life, and to free development. 5) The complexity of performance measurement, and the differences in perception of the achieved results (quality and quantity of services) between management, employees and consumers.

In general, the three elements of institutional risks combination leads to deviation of achieved results from goals in time and scope at the state level in the Russian Federation (at meso level of management). In terms of institutional economics data deviation can be graphically represented (Fig. 2). Where:

I1 - target indicator's value defined on institution environment basis to avoid the impact of its negative issues at planning stage.

I_2 – target indicator's value, defined on institutional uncertainty basis

Type "AT" institutional trap – is a set of actors' (institutions') opportunistic actions negatively affecting the delivery time of stated goals.

Type "T" institutional trap – is a set of inefficient stable norms negatively affecting the stated goals delivery time.

Type "AE" institutional trap – is set of actors' (institutions') opportunistic actions negatively affecting the efficiency of cost for achieving goals.

Type "E" institutional trap – is a set of inefficient stable norms negatively affecting the efficiency of cost for achieving goals.

R_p – management entity's planned state, achieved through implementation of activities, which are meeting the delivery time and cost efficiency requirements (generally, established at level above).

R_T – the actual result, characterized by substantial deviation of time frames and cost inefficiency, caused by type "AT" and (or) "T" institutional trap's indirect negative influence.

R_N – the actual result characterized by general deviation of time frames and cost efficiency, caused by irrational factors in public sector organizations' activity.

R_E – the actual result characterized by low level of cost efficiency and deviation of time frames, caused by type "AE" and (or) "E" institutional trap's indirect negative influence.

E scale – is a conditional socioeconomic efficiency of activities, including organizational processes complexity, resource costs, etc.

T scale –is amount of time for goals achievement.

Fig. 2 illustrates that the target indicator (indicators) value established under the influence of institutional uncertainty (I2) achievement is largely guaranteed, as the requirements for the applicable measures' complexity are low. It determines the falling of current organizational and management activities into institutional traps' field of action. In this case the actual results achieved (R_T, R_N, or R_E) differs from the planned one, defined, for example, at the federal level.

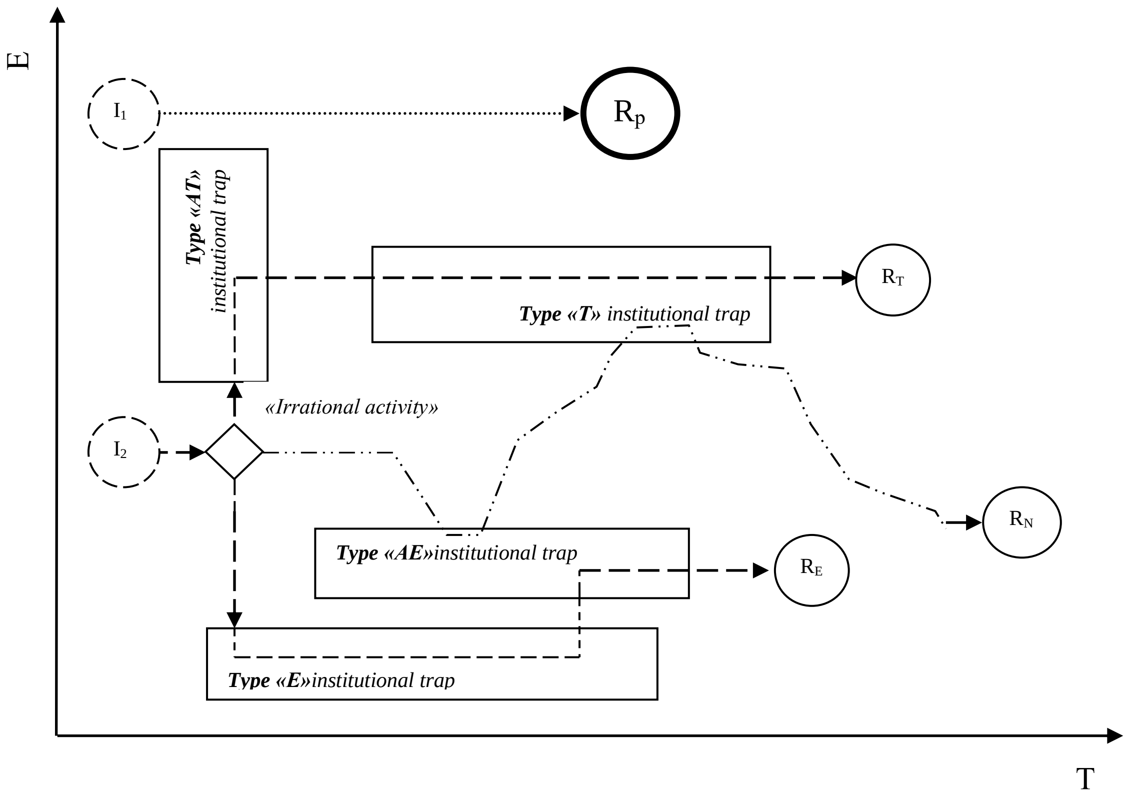

Figure 2. Visualization of public sector organizations' performance deviation caused by institutional traps' and inefficient functioning at meso level

Conclusion.

As it seen, the lack of state regulation of public sector's institutional environment causes the formation of institutional traps variety and appearance of institutional actors that hamper a positive development. Besides, public sector organizations perpetual reformation resulted emerging of their irrational regulatory functions. In conjunction with economic liberty extension of these organizations, it stipulates an institutional uncertainty. In this paper, institutional risks of management in public sector were analyzed from the perspective of institutional traps, institutional uncertainty and non-rational institution functioning. In terms of Russia's economic downturn a search for a new approach to preliminary (forecast) assessment of measures’ aimed at goals achieving (except conventional rate of return method that takes into consideration various opportunist motives of particular economic subjects) is important today.

Results

In summary, it can be assumed that institutional environment of public sector organizations has a significant and various impact on their ability to set the correct goals and the achieve them. In this case the impact is likely negative, as firstly, the two of three public sector parties (public authorities and public-sector organizations) are not interested in radical changes of established institutional norms that define the production and provision of social services. Secondly, social services consumers (the third party) are passive. Despite the palpable discontent in rendered services’ range and quality, the consumers are not active in attempting to improve the situation and do not express the discontent openly. Under such circumstances, the only political will and project management implementation are not enough. The perpetual and mature transformation of public sector’s institutional environment is required. The transformation should be primarily based on management paradigm shift. The indicative management, that specifies peculiarities of working with institutional environment, can emerge as a new paradigm.

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