



GOVERNMENT OUTCOMES LAB

Strengthening public organisations: contracting out and cross-sector partnerships

Dr Mara Airoidi
11th July 2022



@golaboxford



golab.ox.ac.uk



Engaging with external organisations to deliver complex products or services is challenging.

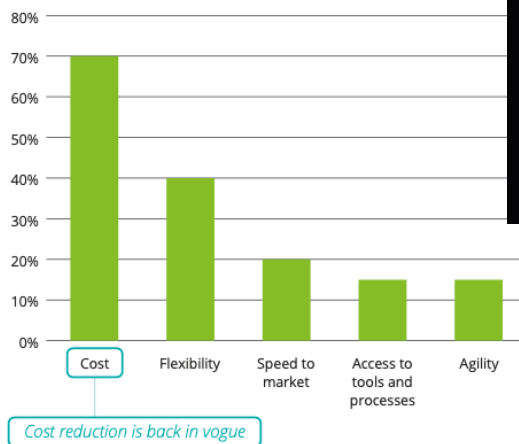
Your experience with, for instance, outsourcing:

- why did you outsource?
- examples of challenges you experienced

Reasons to outsource



Outsourcing objectives



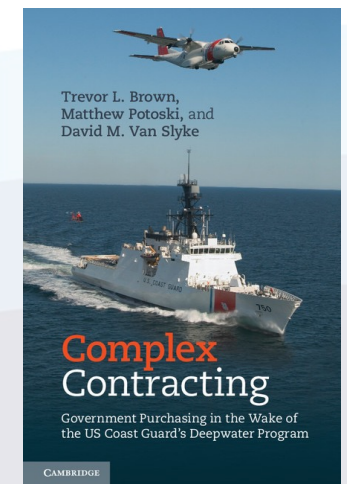
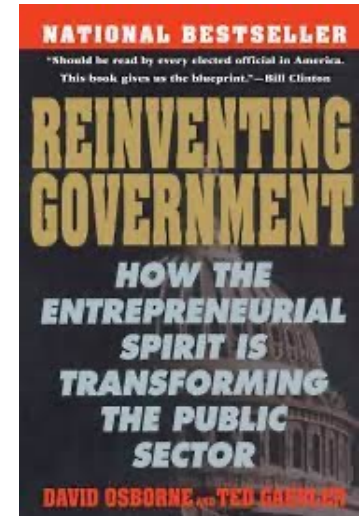
Source: Deloitte Global Outsourcing Survey 2020

“What drives the clients’ decisions is cost reduction. If there is no positive cost case, it will not happen. It is always about cost.”

Partner, Law firm, EMEA

Why do governments outsource?

- Promote efficiency
- Respond to citizen concerns and preferences
- Save or control costs
- Enhance effectiveness
- Improve transparency or ‘accountability’
- Political imperative for ‘smaller government’



When outsourcing hits the headlines



**GOVERNMENT
OUTCOMES
LAB**

THE SUNDAY TIMES

IT 'disaster' could cost taxpayer billions

Abandoned NHS IT system has cost £10bn so far

Bill for abortive plan, described as 'the biggest IT failure ever seen', was originally estimated to be £6.4bn

Queensland Health's \$1.2 billion payroll debacle described as 'great failure in public administration', but Premier vows 'action'

Queensland Health payroll fail: Government ordered to pay IBM costs

Is outsourcing the cause of RBS debacle?

Robert Peston
Economics editor

Conceptual framework: “transaction cost economics”

		Information asymmetry	
		Absent	Present
Opportunism	Absent	Bliss	‘General clause’ contracting
	Present	Comprehensive contracting	Serious contractual difficulties

Adapted from Williamson, 1985

Insight 1. Careful vetting of counterpart(s)

Exercise: *to outsource or
not to outsource?*



Contracting approaches

Walking the contractual tightrope: a transaction cost economics perspective on social impact bonds

Clare FitzGerald , Eleanor Carter , Ruth Dixon  and Mara Airoidi 

University of Oxford, Blavatnik School of Government, Government Outcomes Lab, Oxford, UK

		Information asymmetry	
		Absent	Present
Opportunism	Absent	Bliss	‘General clause’ contracting
	Present	Comprehensive contracting	Serious contractual difficulties

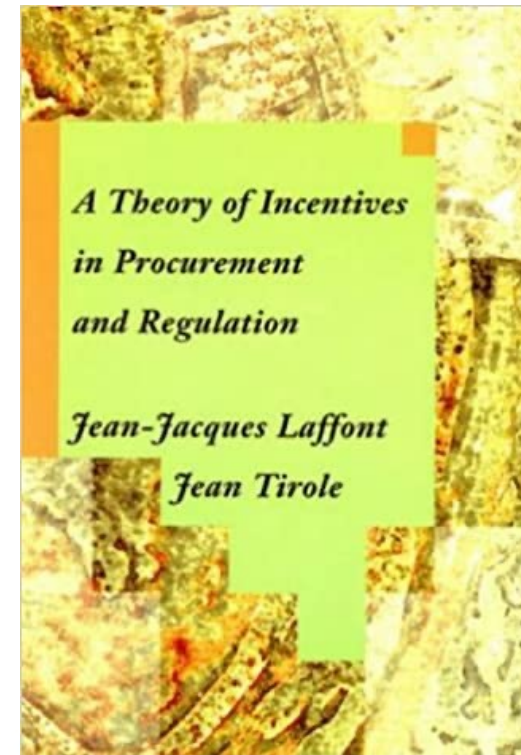


Adapted from Williamson, 1985

Insight 2. Clarity on WHAT and WHY you outsource

Incentive mechanisms?

- Open auctions
- very detailed contracts
- KPIs
- Bonuses
- Penalties



Laffont & Tirole, 1993

Incentive mechanisms?

- Open auctions
- very detailed contracts
- KPIs
- Bonuses
- Penalties

Renforcer l'efficacité de la commande publique

Les notes du conseil d'analyse économique, n° 22, avril 2015

CARTELS

**AGGRESSIVE
BIDDING**

**WINNER'S
COURSE**

CORRUPTION

SHADING

ADAPTATIONS

RENEGOTIATIONS

Renegotiations are frequent

Selected studies on the frequency of renegotiations in PPPs

Geographical area	Sector	% of renegotiated contracts	References
Latin and Caribbean America	All sectors	68%	(Guasch 2004)
	Electricity	41%	
	Transport	78%	
	Water	92%	
United States	Highways	40%	(Engel, Fisher and Galetovic 2011)
France	Highways	50%	(Athias and Saussier 2007)
	Car Parks	73%	Beuve et al. (2013)
United Kingdom	All sectors	55%	NAO (2001)

And may be expensive

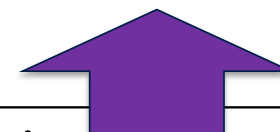
Eg highway construction contracts in California (Bajari-Houghton-Tadelis 2012, based on 800+ contracts):
- adaptation costs = 8-15% of winning bid

Estace & Saussier 2014

Insight 3. anticipate active management of the contract over its lifetime (the contract will change)

Contracting approaches

		Information asymmetry	
		Absent	Present
Opportunism	Absent	Bliss	'General clause' contracting
	Present	Comprehensive contracting	Serious contractual difficulties



Adapted from Williamson, 1985



NEGOTIATIONS

A New Approach to Contracts

by David Frydlinger, Oliver Hart, and Kate Vitasek

FROM THE SEPTEMBER–OCTOBER 2019 ISSUE

“...a *formal relational contract* that specifies **mutual goals** and establishes **governance structures** to keep the parties’ expectations and interests aligned over the long term. Designed from the outset to foster trust and collaboration, this legally enforceable contract is especially useful for highly complex relationships in which it is impossible to predict every what-if scenario.”

CONTRACTING IN THE NEW ECONOMY

Using Relational Contracts to Boost
Trust and Collaboration in Strategic
Business Relationships



With a Foreword by Oliver Hart,
Winner of the Nobel Prize in Economic Sciences



	Transactional Contract	Formal Relational Contract
Focus	The commercial transaction	The relationship
Relationship	Arm's-length relationship	Partnership
Social norms	Disconnect from social norms	Explicitly includes social norms as contractual obligations
Risk management	Use of power and creation of enforceable contractual obligations	Risk avoidance by creation of continuous alignment of interests
Planning	Aims for complete planning, i.e., contract should cover all future events	Creates a fair and balanced flexible framework

There are limited public-private examples of formal-relational contracting practice. What can/should we introduce to public contracting?

Fig. 7.2 Comparison across five dimensions

Insight 4. build on the relationships and keep alignment

Key highlights & your experience

1. careful vetting of counterpart(s)
2. clarity on WHAT and WHY you outsource
3. anticipate active management of the contract over its lifetime (the contract will change)
4. build on the relationships and keep alignment

		Information asymmetry	
		Absent	Present
Opportunism	Absent	Bliss	'General clause' contracting
	Present	Comprehensive contracting	Serious contractual difficulties

Adapted from Williamson, 1985

Consider the transaction costs *over the lifetime* of the contract/relationship [but also the associated “transaction benefits”!]