

Contracting Out

What is Contracting and why is it Growing?

Contracting defined

The formal definition of a contract is simple: 'An agreement between two or more parties, especially one that is written and enforceable by law' (<http://Answers.com>, 2004). A contract specifies the good or service being procured, and typically includes information about price, schedule, and the definition and amount of the service or product being delivered. While the definition of a contract might be quite simple, as Phillip Cooper notes: 'great latitude is left to the contracting parties to an agreement to have the tools to fashion and implement it. Negotiations resulting in a meeting of minds are the dominant dynamic in most contracting' (2003: 13).

This chapter focuses on contracts between government and non-governmental entities and the role of the government contract manager. Government contracting has expanded substantially over the past three decades and has taken on ideological baggage, often associated with shrinking the size of government, lower pay, job losses, and outsourcing of jobs to other countries. At the same time, government has been a major purchaser of goods and services in the marketplace for hundreds of years, buying everything from weapons, uniforms, airplanes, and ships to paper, soap, light bulbs, and paper clips.

Public administration scholars pay particular attention to the relationship between government and its typically non-governmental contract partner. While the contractor is nongovernmental, the product or service they provide through their contract is generally perceived as public and the government is held accountable for outcomes. As Jeffrey L. Brudney and his colleagues (2005: 394) describe it:

Despite the apparent heterogeneity of the privatization concept and the various methods for achieving privatization, in the U.S. context especially, this term is usually taken to mean government 'contracting out' or 'outsourcing' with a for-profit firm, a non-profit organization, or another government to produce or deliver a service. Although the job of delivering services is contracted out, the services remain public, funded mainly by taxation, and decisions regarding their quantity, quality, distribution, and other characteristics are left to public decision makers (compare Boyne 1998: 475; Ferris 1986: 289) (Brudney et al., 2005).

Central to Brudney's definition is the notion of public control, funding and decision-making. The government is the principal and the contractor is simply the agent. Our definition of contracting leaves no ambiguity about the power relationship we see in government contracting. We understand that those who implement policy hold the power to define policy through administration, but that any exercise of this power by the contractor does not eliminate or diminish in any way government's responsibility for the actions of contractors.

The make or buy decision and managing organizations

There is nothing new about government carrying out its responsibilities through contracts. Don Kettl makes this point in recounting George Washington's complaints

about the shoddy uniforms supplied to his revolutionary troops by private contractors. At the same time, many observers believe that the nature and impact of government contracting has changed significantly since revolutionary times. Stephen Goldsmith and William D. Eggers discuss the evolution from simple contracting for goods and services, to contracting as a means of establishing and maintaining complex inter-organizational networks:

In service contract networks, governments use contractual arrangements as organizational tools. Contractor and subcontractor service agreements and relationships create an array of vertical and horizontal connections as opposed to simple one-to-one relationships. Such networks are prevalent in many areas of the public sector, including health, mental health, welfare, child welfare, transportation and defense (2004: 69).

In this view, contracting is a part of the organization's very culture and what Phillip Selznick termed the 'distinctive competence' of the network is indistinguishable from that of the organization. In fact, one key dimension of the value added by the organization is its ability to manage the network it has established. Indeed, Peter Drucker has predicted that by the middle of the twenty-first century most of the work in many organizations will be done by persons not employed by the organization — contractors (1999).

The make-or-buy decision helps define an organization's effort towards identity and distinctive competence. An organization may decide that to adequately focus on their core mission, they must contract out non-core functions. This non-core work still needs to get done but it is now done by workers from the contractor organization.

Organizations contract when a needed good or service cannot be provided by in-house staff. A related reason to contract is to access distinct competence that is available in the marketplace, such as cutting-edge technology, an environmental expert, legal or financial specialists. Contracting can be used to create competition and thereby reduce the cost and/or improve the quality of a desired good or service.

Contracting can be used to access a particular expertise in a geographic location where in-house specialists are not available. A temporary surge in work might dictate the use of contract staff rather than hiring permanent employees. The need to act quickly in an emergency might also dictate the use of contractors.

Government organizations may decide to contract for reasons other than management efficiency or effectiveness. In the aftermath of the taxpayer revolts that began in California in the 1970s, a strong anti-government movement developed in the United States that advocates reducing public employment and privatizing as much of the economy as possible. For example,

The 1970s witnessed an anti-bureaucratic mood that sought to limit the bureaucracy's power through various budgetary approaches, reorganizations, reforms, and spending limitations such as California's Proposition 13. Though not without efficacy and utility, overall, such approaches are inadequate to the task. They must be augmented by an effort to maximize the political representativeness of public bureaucracy (Krislov and Rosenbloom, 1981: vii).

In many cases, this 'contracting to downsize' is really an illusion as the displaced public workforce has been replaced with a contractor workforce, often located across the street or down the block; sometimes, it is the same worker paid more or less to do the same work he or she did for the government. Anti-government leaders will nevertheless trumpet their achievement of 'substantially reducing government headcount'.

Contracting can also be used to weaken the power of public employee unions and to achieve reductions in pension and benefit costs. Similarly, contracting is used to weaken or even eliminate civil service rules and protections. Taken together, all of these 'ideological' reasons to contract can be used to reduce cost and the obligation of government to public employees.

Government leaders also use contracting to build bridges to key constituencies and neighborhoods. For health and human services, it has been increasingly common to contract with local non-profit organizations to provide services previously provided by government social workers, child and elder care workers, and healthcare professionals. A related reason for these contracts may be to avoid direct government responsibility for difficult or failing services such as job training and placement, drug treatment, prison re-entry, homeless services, low-income housing, and even elementary and secondary education.

Why outsourcing is increasing

Government contracting has been growing for the past quarter of a century, coinciding with an international movement toward privatization ignited by Margaret Thatcher and Ronald Reagan. The supply of available contractors has increased dramatically over that time, aided by the rapid expansion of the Internet and related concepts of 'e-commerce' and 'e-government'. In the wake of this expansion of supplies and contract utilization, contract management must work to develop systems to ensure that contractors deliver the best possible goods and services at the lowest possible price.

We expect that the current trend toward greater outsourcing and increased organizational specialization in the private sector will influence government management for the foreseeable future. Perhaps even more important for government managers, effective management in an era of increased technical, economic, and social complexity requires additional contracting. Particularly in the current constrained fiscal environment, sophisticated public managers must master 'make-or-buy' decision-making to focus their organization on core competencies and simultaneously to more with less.

In government, contracting is a highly regulated activity. There are rules on advertising, the bidding process, and the steps that must be taken to review a bid. Once a contract is awarded, there are rules governing the ethics of interaction between government and contractor. Even as governments around the world expand their investments and purchasing in the market place to stimulate their economies, they must be mindful of the performance and ethical risks. For example, President Obama demanded unprecedented requirements of transparency and accountability in contracts funded by the American Recovery and Reinvestment Act of 2009 (US GAO, 2009). Three distinct report systems were put in place: one to the Vice President's Task Force; one to the agency letting the contract; and one to the Office of Management and Budget.

Despite these regulatory constraints, government must find a way to get contractor

personnel to meet high performance standards. Incentives must be provided to obtain desired behavior from contractor staff. As Goldsmith and Eggers (2004) point out, communication through both formal and informal channels is essential to the efficient and effective functioning of government service providers and their contract partners. Communication and informal contact, in particular, may be difficult in an environment designed to prevent corruption and the appearance of impropriety.

Contracting has been increasing all over the world. As Barbara Romzek and Jocelyn Johnston have observed, 'Governments at all levels have expanded the range of services they deliver through contracts — from traditional "make-or-buy" decisions for defense weaponry, highway construction and fleet purchases, to contracting for the ongoing provision of specialized social services' (2005: 436).

Adoption of the 'new public management', or NPM, varies across nations. For instance,

Traditional public administration persists in the Commission of the European Union (EU) and Germany. The aims and results of NPM differ. In the UK, NPM aimed to create the minimalist state. In Norway, it aimed to protect the state. The language of NPM obscures differences. Distinctiveness lies in the package not in the parts but there is no uniform, agreed upon package. Finally, the meaning of NPM has changed; for example, in Australia the early focus was corporate management but it gave way to a focus on contracting (Bevir, Rhodes and Weller, 2003).

Several factors may influence public sector modernization; they include "path dependency" (or "historical traditions, cultural norms and established practices"); political mobilization by advocacy coalitions of administrative and political elites; the institutionalization of such coalitions; and influential meta-organizations and institutions that produce knowledge' (Bevir, Rhodes and Weller, 2003). Reform in Western Europe is characterized by the following: 'continuous adjustment; responses to specific political crises; pragmatic structural change; reform as its own cause; and comprehensive programmes' (Bevir, Rhodes and Weller, 2003).

Australia and the Netherlands have contracted out typical government services such as welfare. These contracts are referred to as 'relational contracts' because more than just commercial considerations are at stake; they include commitments to more general values (Finn, 2008). More specifically,

The Australian Job Network (JN) was created in 1998 and, in a decade, made the transition from 'radical experiment' to established institution. Its design changed as policymakers adapted the model to secure greater efficiencies, to deal with unanticipated effects and, through successive 'welfare reforms', to redefine services to 'activate' more working age benefit claimants. The evidence suggests the JN delivers more job outcomes for half the cost of the previous system (Finn, 2008).

Performance in general has improved with contracting, but not without producing a myriad of complications. Contracting has improved participants' short-term job prospects minimally, by 5–10 percent. 'The cost-efficiency gains attributed to the Dutch and Australian models appear significant, but relatively little is known about the extent to which these gains have been offset by high transaction costs for the purchaser, providers and service users' (Finn, 2008). Furthermore,

Securing the delivery of government objectives through contracts is prone to the same implementation problems experienced in public sector delivery systems. Contracting out poses further challenges because it fragments programme responsibility among multiple contractors, changes the relationship between those who design policy and those who deliver front-line services, and blurs lines of responsibility and accountability (Finn, 2008).

Lobbying has also increased alongside of contracting: 'Providers have emerged as a distinct interest group and powerful lobbying force, with direct access to senior civil servants and ministers' (Finn, 2008). With this political backdrop, contracting is only set to increase in the near future.

Lower-cost technology of information, communication, and rapid, low-cost transportation make 'production location' more flexible

The expanded use of contracts is related to the dramatic expansion in the availability of extremely low-cost voice communication and information-sharing virtually anywhere in the world. Workers can share documents, financial officers can receive invoices and pay them electronically, and inspectors can transmit reports and video instantaneously from the site of the customer interface to the handheld of the CEO. For example, it is often said that Proctor and Gamble virtually runs the section of Wal-Mart stores where its products are sold. Multiple organizations can operate as one from disparate sites to serve customers.

In New York City, a Police Department operator answers a 911 call from a sick citizen, forwards the call with critical information to an FDNY (Fire Department of New York City) ambulance dispatcher who sends the nearest FDNY or private ambulance to bring the critically ill person to the nearest public or non-profit hospital. Billing and payment for the FDNY ambulance service is handled by FDNY civilian staff, an outside billing firm and/or city/state/federal Medicaid/Medicare public employees.

Similarly, ever larger air transports and cargo ships can carry goods from one side of the world to the other rapidly and at relatively low cost. Fresh Dover sole can be caught off the coast of England in the morning and served in a Manhattan restaurant that evening. It can make economic sense to ship water from Fiji to a New York City deli and sell it for profit at a price that is only slightly higher than Poland Spring water from Maine. Overnight shipping of documents, books, and other small, light items is almost taken for granted. Distance, time, and cost are less and less an obstacle to contracting as a tool to accomplish the work of an organization, be it public, private or non-profit.

The ideology of globalization and our global economy

In our view, it was large-scale, vertically-integrated bureaucratic hierarchies that enabled the economies of scale and mass production needed for the wealth-generating machine we called industrialization. For the first half of the twentieth century this model worked, and to some extent, it works today. However, as technology developed (satellite communications, the Internet, superhighways, containerized shipping on huge cargo ships, air freight, super and personal computers, cell phones, bar codes), a global economy developed which rewards organizational specialization and discourages vertical integration.

The make-or-buy calculus has changed. We now live in the post-industrial information age with much higher standards of efficiency, effectiveness, and customer service. Customers expect excellent goods and services promptly and at a good price. They are much less willing to accept slow, non-responsive organizations — as General Motors learned the hard way in 2009. New models of organizational efficiency are emerging, out of necessity and by design. For Margaret Thatcher, Ronald Reagan, and the anti-government advocates, the model was privatization — the smaller the government the better. For Osborne and the reinventers, the model was innovation — streamlined and more effective government (Osborne and Hutchinson, 2004). Today, we see increased emphasis on contracting out and a broader strategy of managing public services through networks. Contracting out and network management are not synonymous, but our view is that networks include both informal and contractual linkages. We consider the contractual links as equivalent to the steel frame of a bridge — the key relationships upon which the informal and non-contractual relationships are built.

Globalization and advancements in communication, transportation, and technology have created problems and demand that are larger than generally experienced only a few decades ago. Goldsmith and Eggers (2004) use the example of homeland security to illustrate that dealing with terrorism requires global scope and cooperation and simultaneously customized, local response capacity. This new network management ‘bears less resemblance to a traditional organization chart than it does to a more dynamic web of computer networks that can organize or reorganize, expand or contract, depending on the problem at hand’ (Goldsmith and Eggers, 2004: 8). The relationship between the various government and private organizations in efforts dealing with terrorism are not always defined entirely by contracts, but in some instances are in the interest of the private sector to perform. For example, a private firm's security force and its practices are a clear part of the network of organizations delivering homeland security services, even though they may have no contractual relationship with government. Information exchange between security forces can be critical, but is not provided in exchange for fees in a formal relationship, but in exchange for goodwill that might later result in reciprocity.

What management challenges does contracting present? Formal and legal relationships
Crafting RFPs and eliciting bids

Governments use a variety of methods to select contractors. The most common techniques are a sealed bid and a request for proposal (RFP). A sealed bid is used when the product or service is relatively easy to define, is widely available in the marketplace, and both the unit cost and total contract amount are modest (total purchases of less than \$100,000). Since quality is assumed to be standard, the sealed bid is awarded to the lowest bidder. The sealed bid must be received by a specific deadline. All bids are opened in public and recorded. The contract is awarded to the lowest bidder that also meets all the specifications of the bid.

Requests for proposals, or RFPs, are used for purchases of higher amounts (\$100,000 or more) and/or when the product or service is technical, approaches vary widely or the government is not exactly sure about the best approach. The RFP will set out what problem it seeks to solve or need it seeks to meet and then ask those interested in bidding to tell them what they think is the best approach, balancing price and level of performance. As government contracts out more services and requires complex

technological solutions, the RFP is being used ever more frequently.

To avoid charges of favoritism and to enable intelligent choices among what might be significantly different proposals, RFPs should include a predetermined scoring system, informing bidders how their proposals will be judged. The government agency must also assemble a team of knowledgeable staff to independently score the proposals and a predetermined methodology to choose among the bidders with the highest scores. RFP price quotes can be negotiated after submission but the government agency involved must take care to ensure that fairness is assured, in fact and in terms of appearance.

Negotiated or sole source contracting is generally discouraged in the public sector because the appearance of favoritism is so hard to avoid. Sole source contracting may be used when there is only one supplier of an essential commodity or service — a medical device, a weapons system, a medication or a special security system — or in an emergency circumstance such as a flood or terrorist attack where lives are at risk. A negotiated contract might also be used when a delay in acquiring the product or service might result in substantial cost over-runs for a larger construction project or weapons system.

To ensure the widest possible distribution of its notices of solicitation, governments may develop lists of bidders. Organizations interested in competing for government business fill out an enrollment application and are placed on a mailing or email list so that they automatically receive notification of solicitations for government contracts. In certain circumstances, where work is complicated, technical, and predictable, government agencies may develop pre-qualified lists of vendors. Pre-qualified lists might apply for construction projects, auditing, maintenance and repair, road work, and snow removal.

Governments may also make special provisions to ensure that small locally based businesses and businesses owned by minorities and women have access to public contracts. These provisions may include preference for subcontracts from larger contracts, exemption from bonding requirements, prompt payment guarantees, and technical assistance. Government wants to buy the highest quality at the lowest possible price but it may also want to ensure that the local citizens and businesses that provide its taxes and revenues have a reasonable chance to participate in the business opportunities provided by their government. Governments that are fully committed to a transparent and competitive contracting process will reach out to a broad range of stakeholders concerning the decision to contract and in assessing the efficacy of contracts after they are awarded.

Developing contract language that maintains management prerogatives

When a service is being contracted for the first time, it is difficult for the staff working on the RFP (or on the actual contract) to develop contract provisions that anticipate all the tasks involved in the work and all of the problems that may arise. Sometimes specifications in the RFP or the contract do not permit critical tasks to be performed. While contracts must provide a vendor with some predictability, there are a number of techniques that government can use to retain discretion over contract provisions and contractor work.

One very common technique is to use a task-order, mission contract. This large-scale,

multipurpose contract provides a general description of the contract's anticipated tasks, but does not release funding until a government client writes a specific task-order directing the firm to perform particular tasks. Another practice for dealing with this problem is to let a short-term 'trial' contract with explicit provisions for early and rapid renewal. Both of these techniques are useful as the organization learns more about the work being contracted out. As this learning occurs, the contract can get more specific. In the long run, it is best to translate these learning experiences into standard operating procedures and clearly delineated tasks, incentives, and expected outputs and outcomes.

Other techniques for improving an RFP or contract include a request for qualifications or request for information from prospective vendors. These requests to firms to either provide a demonstration of capability or evidence of qualifications can be used to narrow the field or develop the additional information needed in order to draft an appropriate RFP. Another strategy is to find one organization to work with and use a sole source procurement to pay that firm. Through this method the government can obtain some of the firm's time to learn more about how to define and measure the service being contracted. If this sole source technique is used, it may be necessary to prohibit this firm from competing on the final contract, in order to avoid conflicts of interest.

Managing performance

Effective contract management requires a range of management tools. Some of those tools relate to contract provisions that provide resources to government contract managers. What we mean by resources are contract clauses that provide managers with:

- the ability to define and shape the work of contractors;
- the flexibility to make mid-course corrections;
- the ability to obtain frequent and audited measures of contractor performance;
- methods for systematically providing performance-based incentives and disincentives — particularly financial bonuses and penalties.

We are strongly attracted to the use of incentive clauses in contracts. Incentives work best when they are rewards for the accomplishment of specific, verified performance measures. For example, when a firm that is installing subway tracks completes the work a month ahead of time, it is given a bonus for every day the project comes in ahead of schedule. In fact, an even better technique links a similar penalty clause to late completion. The point of an incentive is that it is only useful if it inspires the specific changes in behavior that improves organizational performance. If it doesn't motivate change or motivates the wrong change, it fails.

Managers should experiment with different forms of incentives, and attempt to determine the independent impact of the incentive on performance. One problem with bonuses is that if they are given too easily, they are soon seen as a type of base pay and people come to rely on and expect them. When that happens, their impact on performance is significantly reduced.

Designing and implementing performance measures

Performance measurement is critical to contract management — 'contractual

relationships with private and non-profit firms provide the surest way to punish poor performance: contract termination' (Cohen and Eimicke, 2000: 102). A properly designed performance management system can help a public manager decide whether it makes more sense to contract or to perform the task in-house. If contracting is the decision, then performance management can help make the best choice among competing contractors. An effective, real-time performance measurement system can allow contract managers and contractors to recalibrate resource allocations, assignments, and strategy. If the measures are accurate and focused on the outcomes that matter to those served, the metrics can be used to modify contractor behavior.

Performance contracts need not be extremely complicated but that does not mean they are easy to design or employ effectively. At a minimum, performance contracts must include objective performance standards, rewards for superior performance and penalties for failure to meet a minimum baseline (Osborne and Hutchinson, 2004: 180–1). In terms of rewards, contractors can share in savings achieved for the government, receive a portion of revenues increased, and/or be rewarded for high customer/citizen satisfaction or delivering the product or service more quickly than anticipated. Conversely, they can be punished for failing to meet contract minimum requirements.

We recognize that contractors will use their influence with elected officials to 'cut red tape' and minimize the 'interference of rule-driven bureaucrats'. Politically connected contractors will try to avoid complying with contract provisions they previously agreed to but now find 'onerous' and use friendly legislators and staff to apply pressure to government contract managers and monitors. And, when contract renewal time rolls around the contract manager is sure to receive many phone calls and emails from elected officials and 'interested citizens' expressing unbridled support for even the worst-performing contractor. Involving a broad range of stakeholders throughout the contract process is always a good idea and it becomes particularly valuable in these circumstances. The effective contract manager can draw on the unbiased feedback from a wide range of knowledgeable and involved stakeholders to resist political pressure to renew a poorly performing contractor.

The reality that 'better' may not always be 'cheaper' necessitates that the public contract manager choose the proper mix of metrics to use when soliciting and awarding government contracts, particularly in the field of human services. For-profit firms may appear cheaper, but non-profits may be better able and more willing to make sure they really help the hard to serve and those most in need. Unfortunately, studies comparing the performance of forprofits and non-profits in terms of quality and cost are limited and inconclusive (Frumkin, 2002: 14; Sanger, 2003).

Public program and contract managers should consider factors other than cost when setting criteria for contractor selection. Points should be awarded for documented past success in delivering quality outcomes, as measured by other governments, customers, and/or independent third parties. In fields where success has been difficult to achieve — foster care, substance abuse treatment, and prisoner reentry, for example — points could be awarded for innovative approaches that might lead to new best practices (Frumkin, 2002: 16). Government can also break up the workload into large and small assignments; divide the workload by geography and give preference to some community-based providers; reward experience in the field and in the community; and/or reward collaborations between for-profit and non-profit providers.

This challenge of ensuring contractor performance is relatively simple when purchasing

goods such as office supplies, computers or even food services. What makes government contracting so complex today is that human services such as child care, elder care, job training, education, and even security services — generally considered the core functions of the public sector — care now being contracted out to for-profit and non-profit companies. Finding the right contractor is complicated by potentially conflicting objectives for government contracting — cheaper may not be better or faster and better may not be either faster or cheaper.

Finding the right contractor begins with reaching consensus among a broad range of stakeholders on the objectives for the services to be contracted. Next, the effective contractor manager must find appropriate methods to measure contractor performance. Finally, the contractor manager must identify effective incentives and penalties to ensure that the contractor achieves the desired outcomes.

Ethics and Accountability

Contracting and democratic accountability

When we discuss contractor accountability, we need to ask the question: Accountable to what or who? We believe that the answer to that question is: 'Accountable to the system of democratic representation and its elected officials.' Accountability is not simply intended as a means of punishing representatives for taking wrong positions, but more importantly, it should encourage representatives to be responsive to the needs of those they represent. The difficulty with the accountability position is that this notion of providing stimulation for right behavior does not necessarily follow from the definition of accountability. Representation is an ongoing activity, not merely a set of mechanical or formal structures.

The accountability view of representation leaves a measure of power in the hands of the represented. According to this view, if the representative is willing to be elected to office only once, he (she) can do as he (she) pleases. Hence, the power relationship can be described as follows: in the short run, the representative is in the dominant position, but due to their ultimate veto, the represented have the last word and in the long run hold greater power. Clearly, the represented hold greater power in this view of representation than in the authorization view. Nonetheless, the public's leverage is periodic and latent rather than continuous and present.

The role of the unelected bureaucracy makes the issue of contractor accountability all the more difficult. As Carl Friedrich once observed, 'the core of modern government ... [is] a functioning bureaucracy' (1937: 44). Put another way, the major actors operating at the heart of the American political system are unelected officials. This has been extended to networks of public and private unelected officials in an increasingly complex set of market and non-market-based relationships (Olsen, 2005). The presence of unelected government and non-governmental players is a difficult notion to reconcile with a theory of governance that maintains that government ought to be democratic, or of and by the people. The problematic nature of citizen linkage to unelected officials is addressed in part through direct communication between the public and the bureaucracy. It is also addressed through the strong sense of responsibility and public ethics that is typical in the American public service. This internal norm in government is a deeply ingrained element of government's organizational culture. Perhaps some of these same communication techniques and a sense of public ethics can inform private contractors of public preferences and inspire

them to pay attention to them. However, contractor behavior should be even more constrained than the acts of unelected government officials, since whatever actions they take must be approved or at least known by government officials.

When Rudolph Giuliani was mayor of New York City, a contractor with the City's human resources administration placed a young girl into foster care who died at the hands of her guardian. Initially, the mayor attempted to assign blame to the contractor. While the contractor was at fault, the media and the public held the mayor accountable. He came to agree with this position and created a new agency exclusively focused on foster care. This agency reengineered the foster care contracting system with new reporting requirements, more effective management controls, and better procedures for quality control.

We believe that the overall probability of ensuring real accountability is lower when government contracts a function. When life and death issues are involved and higher levels of accountability are required, contracting should be avoided. Most of the time, such extreme accountability is not needed and the issue then becomes one of establishing a set of performance indicators and management processes adequate to ensuring appropriate contractor performance.

The danger of fraud and conflicts of interest

It is critical that government officials avoid both the reality and appearance of conflicts of interest. It is not enough to respond to an investigation or attack. Government officials must think through their past interactions and those of people they are close to, and anticipate potential conflicts of interest.

A number of techniques have been developed to reduce the possibility of conflicts of interest. Sealed, competitive bidding is one such technique. So, too, is the use of panels of officials to review proposals and select winning bids. Panels can include people from outside the agency to ensure greater independence and objectivity. Still, the best technique is vigilance and sensitivity on the part of government officials involved in contracting.

A common understanding of corruption in government is the use of a public position for private gain. Corruption and unethical behavior associated with contracting usually involves compromising the public interest for private benefit (Gray and Kaufmann, 1998: 1). The World Bank describes administrative corruption as 'the intentional imposition of distortions in the prescribed implementation of existing laws, rules and regulations to provide advantages to either state or non-state actors as a result of the illegal transfer or concentration of private gains to public officials' (2005: 2). A simple example is when a contractor pays a bribe to influence a person with the authority to award, renew, or change the terms of an existing contract. In such a circumstance, both parties may be acting illegally or at least unethically — offering and/or paying a bribe by one party and soliciting and/or accepting the bribe by the second party.

A related category of corruption is often characterized as the 'revolving door' where a contractor has the capacity to 'trade' career opportunities for the contracting agent or members of their families in return for assistance in winning the contract. Whether it just looks bad or is the result of an explicit quid pro quo, most organizations seek to monitor the behavior of its employees regarding the award of contracts and future employment of those employees. Many governments and non-profit organizations have explicit laws

or regulations limiting the right of former employees to work for an organization that received contracts during their public employment. A common limit lasts for one year after separation from the contracting organization (see, for example, Corporation for Public Broadcasting, 2004: 5).

In complicated contracting situations such as the outsourcing of a large information technology operation or the operation of a sewage treatment plant or waste treatment facility, the government may hire a third-party expert to advise them. It is not unusual for these third-party experts to have financial relationships with some of the bidders for the contract. These experts may even have a financial interest in the outcome of the transaction, directly or indirectly. These relationships may not be easily identified. Therefore, it is essential that the government invest in extensive due diligence to ensure that their hired advisors receive only payments for their analysis and advice, and demonstrate affirmatively that they have no other financial interest in the transaction (Sclar, 2000: 121).

Because government may be unsure of exactly how to fully specify what needs to be in the contract, they may leave aspects of the contract's requirements open or only generally defined. Contractors will often take advantage of the vagueness, requiring additional payments to do what is not explicitly required in the contract (Savas, 2005: 33). This failure to fully define what is required could be the result of genuine uncertainty, but it could also be due to incompetence or could be a deliberate act to enable a favored vendor to reap the benefits from the changes required after the contract is signed.

Political considerations can corrupt the contracting process in the public sector. The decision to contract rather than perform a service with in-house staff can be the result of political influence. Campaign contributors may convince an elected official to bid out services without any analysis justifying the decision (Clynch, 1999: 2). Career public servants may be pressured by political appointees to award contracts to those who have supported the current party or person in power. The connected contractor might even be very qualified and experienced. The problem is the distortion of an objective, merit-based selection process to meet other objectives.

Corruption can also occur among the contract seekers, with or without the knowledge of the contracting agency. Contractors cooperate to take turns or divide territories, submitting deliberately inflated bids for the contracts or districts that are not 'theirs' and winning with comfortably 'fat' bids in the areas 'given' to them. Large contractors and contractors associated with organized crime can intimidate legitimate, honest competitors out of the competition (Sclar, 2000: 48).

More broadly, there is corruption by incompetence. Many government agencies are contracting on a massive scale without necessarily instituting equally dramatic changes in their hiring and training practices. As Goldsmith and Eggers note, 'Managing a portfolio of provider networks is infinitely different than managing divisions of employees' (2004: 22). Governments that view contracting as a means of off-loading management headaches and that do not invest in staff and training for proper oversight can expect waste, complaints, and scandal.

Some rules that must apply to public employees in the contracting process cannot apply to their private sector partners. For example, the American Society for Public Administration's Code of Ethics suggests that public officials should not realize undue

personal gain in the performance of their official duties. In the private sector, a key motivating tool is additional compensation for behaviors creating additional profit for the firm. This creates a conflict of interest.

Corrupt and/or improper contract decisions can result because the officials making those decisions have not been trained in contract solicitation, evaluation, design or implementation. Many government employees assigned to the contracting process were not originally hired for that task and subsequently receive no training for a complicated and demanding assignment. Rigorous training of those assigned to contract management could help limit corruption and lead to better contracts and contract outcomes (Institute of Public Administration, 2005: 1–7).

Techniques for detecting and discouraging violations of public ethics

To determine the ethical standards for government contractors, we must first establish the rules that government officials dealing with contractors should follow. Laws and regulations covering compensation, gifts, bidding procedures, equal opportunity and discrimination, and disclosure must be reviewed and assessed to determine the potential applicability to contractors. Ethical standards, laws, and regulations should be part of the contracting process from the outset, should be part of the negotiation of contract terms, and should be reflected explicitly in the contract document and operating procedures.

Perhaps not surprisingly, Transparency International argues that transparency is an effective mechanism to prevent corruption (2005: 1–2). Contract solicitations, evaluations, and selections that are as open as possible to all potential bidders, to media observers, interested advocates, and the general public, are more likely to be fair, well-analyzed, and properly awarded. Transparency has its limits, however. Intelligent but corrupt officials and their contract partners may be able to keep their illicit behavior secret. The contract may be so technical that observers may not be interested or able to effectively monitor the process. Or, to ensure fairness or for security reasons, some processes cannot be completely transparent.

Whether it is gifts or bribes, annual financial disclosure filing requirements can be a check on the trading of contracts for personal financial gain. As part of that filing, federal income tax returns can be required. While the completely dishonest person will falsify all documents, the deterrent of multiple chances of discovery and multiple levels of penalties (tax fraud) may keep others from yielding to temptation.

Similarly, there are laws in many places seeking to limit the negative effects of the revolving door between public contracting offices and their contractors. To further discourage improper behavior, we could enact laws prohibiting members of the Senior Executive Service (and similarly situated high-level administrative policymakers at the state and local level) and political appointees from seeking employment with contractors benefiting from their policymaking or rule-making for at least a year or two upon leaving public service. We could also prohibit former government employees from working in a different division or subsidiary of the division of the company benefiting from their public contracting decision (POGO, 2004: 4).

Other methods of limiting the impact of conflicts of interest include recusals, waivers, divestiture, and trusts (US Office of Government Ethics, 2005: 5). Recusal requires a public official to withdraw from participation in a contracting decision where there might

be personal gain, or benefit to a family or close associate. Waivers can be used on a case-by-case basis to enable officials to participate in a decision where they may have an interest, but only where that interest is not substantial, very indirect, and is mitigated by its disclosure. Divestiture can enable an official to eliminate a potential conflict by selling the property that creates the potential conflict. Trusts can manage assets for public officials while they are in a decision-making position such that their actions have no relationship to gains or losses in their investment portfolio.

Stronger laws to protect or even to encourage civil servants aware of corrupt practices might also lead to a better contracting process. Those on the inside of the process are most likely to know about corruption in the contracting process, yet these potential whistleblowers are often subordinates of those engaging in the corrupt practices. And the superiors who they might be implicating are often politically connected to the chief executive and/or legislative leaders. There must be a secure process that encourages and enables those with concerns about corrupt practices to share what they know with enforcement officials without risking their job or creating a chilling environment for those trying to do their jobs honestly.

First, the contracting agency can educate bidders on the laws and regulations governing the contracting process and what constitutes ethical behavior. Agency personnel can also exhort and advocate the proposition that private contractors of the government should become guardians and protectors of the public trust. This moral conscience role can be accomplished more effectively if the private contractor is located in or close to the government agency they are serving. Effective public managers will learn to 'manage by wandering around' (Peters and Waterman, 1982) their own offices and those of their contractors, reinforcing the reality that these private firms are acting in the public service.

Secondly, in RFPs, the government agency can award points to contractors that have a track record of ethical behavior, have strong corporate codes of ethics, and can document a history of rewarding ethical behavior and punishing corrupt behavior on their own. The contract document itself should articulate ethical standards and behaviors and include enforcement mechanisms for violations. The contract could even require the contractor to report overtures for corrupt behavior coming from public employees.

Thirdly, the contract can specify incentives or bonus payments for meeting ethical standards and stiff penalties for violations. Contract renewals can be conditioned on the meeting of ethical requirements. Violations of certain provisions can even specify that the contractor is blacklisted from bidding on all future public contracts for a number of years, or even forever.

Finally, the public agency should independently monitor the behavior of the contractor to ensure ethical behavior. This can be done with agency employees or a third party, such as a private accounting firm, that can be hired to serve as a monitor. While potentially expensive, an outside monitor can help to preserve a positive working relationship between agency and contractor personnel and eliminate the possibility that agency personnel might try to deliberately sabotage the contractor. Inspectors General should also be established as a self-guided investigators of potentially corrupt practices.

Ultimately, it is the responsibility of the public manager to ensure that ethical standards are understood and observed. To do so, public managers will need to develop a set of

skills that are helpful in managing internal hierarchies but are essential to effective management of a network of outside contractors.

Public network managers must become expert consumers of information technology and performance management tools, so that they can effectively monitor the activities of off-site contractors and provide incentives for ethical behaviors and penalties for actions that do not meet government standards. Clearly, there must be performance measures for ethical behavior and those measures must be highlighted as critically important to the private contractors.

Unethical behavior by government officials, alone and in partnership with private contractors, has occurred since the founding of the United States and will no doubt be with us as long as we are a nation. The increase in government contracting increases the risk of unethical behavior. We believe the risk is worth the reward of better government services at a lower price. Government is already doing a better job of managing these networks of service providers and ensuring the ethical behavior of its own employees and those of its contractors. It remains one of the great challenges for public managers in the twenty-first century, but with proper training, attention, and application of the proper management tools, it is a challenge that we believe can be met.

Conclusions: Contract Management and Effective, Accountable Public Management

We do not believe that representative democracy is compromised by the presence of contractors working for unelected government officials. To the extent that contracted work enhances government's capacity and performance, it connects representatives to a more effective and efficient administrative system. In a formal sense, policy decisions flow from elected leaders to unelected government officials and from these public officials to private organizations under contract to the government. The reality, of course, is that contractors are in direct communication with elected leaders. Contractor behavior is influenced by contractor perceptions of the policy intent of elected leaders. Contractors lobby and make campaign contributions to influence those policies. The policy intent of these elected representatives is mediated and made operational by regulations, guidance, and contract provisions developed by unelected officials. All of these factors influence the behaviors that make the policy pronouncements of elected leaders real.

The increase in government contracting over the past several decades presents additional challenges to accountable, representative government. However, these challenges are part of a series of changes in modern times arising from new technology, globalization, and cultural shifts in the world. Contracting, properly managed, should not impair accountability and representative democracy. Poorly managed, contracting can pose significant threats.

Effective contract management requires skill at using all the tools of traditional and innovative management. Effective public managers understand human resource, financial, organizational, information, performance, strategic, political, and media management. They also acquire experience with quality management, benchmarking, reengineering, and team management.

The responsible contract manager must do more. In addition to deploying those tools in

problem-solving, today's responsible public manager must learn how to elicit contract bids that result in appropriate and well-priced services and goods. They must learn to monitor contractor performance, and write contracts that allow them to perform this monitoring function. Contract managers must learn how to develop informal networks that reach deep into contractor organizations, just as they have done within their own organizations.

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