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MANAGING THROUGH CONTRACTS (A CASE STUDY MUNICIPALITY OF ELBASAN, ALBANIA)

ZARZĄDZANIE PRZEZ KONTRAKTY – STUDIUM DZIAŁALNOŚCI ZARZĄDCZEJ MIASTA ELBASAN W ALBANI

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Streszczenie. Głównym celem niniejszej pracy jest pomóc lokalnym władzom w Albanii przeanalizować kwestię wydajności zarządczej w odniesieniu do zawieranych przez nie umów na świadczenie usług publicznych. Autorzy koncentrują uwagę na funkcjonowaniu urzędu miasta Elbasan w Albanii i analizują sposób sporządzania umów i ich wpływ na świadczenie usług. W tym celu wykorzystano model opracowany przez Mari Sako, która badała kwestię zawierania umów pomiędzy przedsiębiorstwami w Wielkiej Brytanii i Japonii. Model ten analizuje stosunki umowne pod kątem zestawu aspektów, proponując zastosowanie dwóch archetypów: Obligational Contractual Relationship (Zobowiązujący Stosunek Umowny) oraz Adversarial Contractual Relationship (Podstępny Stosunek Umowny). W tej pracy proponowane przez Mari Sako aspekty analizy wykorzystano do porównania umów sektora publicznego. Pod uwagę wzięto zarówno naturę umowy, jak i naturę specyfikacji, jej zawartość i autora. Analiza pozwoliła na wyciągnięcie dwóch wniosków, które być może pomogą lokalnym władzom określić zalety i uniknąć błędów wynikających z zawierania umów danego rodzaju na świadczenie usług publicznych.

Key words: Adversarial Contractual Relationship, Contractualism, Different Contractual Forms in different sectors, Local authorities in Albania, New “Institutional Economics”, Obligational Contractual Relationship, Quality and Efficiency.

Słowa kluczowe: Adversarial Contractual Relationship – ACR (Podstępne Stosunki Umowne), jakość i wydajność, kontraktualizm, nowa ‘ekonomia instytucjonalna’, Obligational Contractual Relationship – OCR – (Zobowiązujące Stosunki Umowne), różne formy umów dla różnych sektorów, władze lokalne w Albanii.

INTRODUCTION

Many of the services provided by the public sector are delivered through contracts, which can be either internal or external with private and voluntary organisations. People have to learn how to write contracts and specifications for services as well as how to make sure that services are delivered according to the terms of those contracts.

We will look in the Municipality of Elbasan, Albania to see how contracts have developed and how they affect the delivery of services. Firstly, we find that there are different sorts of contracts in different areas within the public sector, these differences include; the contract period, whether or not they are left after a competitive bidding process, how detailed the specifications are, and how punitive the default clauses are.

We then try to explain why these differences occur. Explanations include the structure of the market in which contracts are made, managers' ideas about what sort of contract is likely to yield both efficiency and quality, and the political attitudes of those making the contracting policy. The fact that there are wide variations implies that managers have a degree of discretion. We then look at how that discretion is being exercised. For this we use the framework developed by Sako (1992) who looked at business-to-business contracting in the United Kingdom and Japan. She analyses contractual relationships according to a series of dimensions and proposes two archetypes, an Obligational Contractual Relationship and an Adversarial Contractual Relationship. Her dimensions are used to compare public sector contracts. As well as the nature of the contract, we also consider the nature of the specification, what it contains and who writes it.

Extensive literature examines the role of trust as a key joint venture management issue (Gulati 1995, Parkhe 1998, Currall, Inkpen 2002). The issue of joint venture control is the focus of one of the largest collections of empirical studies in the area of joint venture. In recent years, learning and knowledge management have also become a key alliance research issue as discussed in Inkpen's (2002) literature review. This idea is consistent with the view of others, who have argued that trust should not be viewed as a static construct. I have taken (Inkpen, Currall 2002) into account in that a co-evolutionary approach is useful for studying trust.

Different forms in different sectors

Different areas within the public sector have adopted different sorts of contracts. In the case of local authorities, which are compelled to use competitive tendering, the contract forms have, by necessity, reflected the competition process: sealed bids are invited; there can be little chance of establishing a relationship with the supplier before the bidding process. Apart from checking credentials and references, everything required must be specified at the contract stage; the authority must protect its interests with strong penalty clauses and default procedures. At the same time, contracts are for relatively long periods (one to five year for most services) and therefore a relationship with the suppliers has to be developed over the contract period.

In the Municipality of Elbasan, contracts were initially for one year between the purchasers and providers, but there were long-term relationships for both sides. Despite the short-term nature of the contracts, penalty clauses and destructive default procedures were not commonly used in the early days of contracting. There was, however, great recourse to details about the processes carried out under contract as the purchasers side did not trust the providers. There were not normally competitions for large blocks of work. There was tendering for most services, but generally providers did not have to bid for the bulk of their work against another provider. This lack of bidding would imply the need to establish trust,

although the details in the contracts and specifications suggest that this has not necessarily been the case. It is not clear why this was so, but it may simply have been the result of people being put in adverse positions.

There are some doubts about whether what were termed contracts within the public authorities, were really a contractual relationship at all in the commercial sense of the term. It has long been known that internal contracts are not legally enforceable, because there is only one legal entity (Harden 1992). Allen (1995) pointed out that there were several fundamental differences between a contract and the contractual arrangements within the public sector, where there was no choice, but to enter into a contract (purchasers and providers were compelled to trade with each other), terms were imposed by a higher authority in the event of a failure to agree, and disputes were resolved by internal administrative procedures rather than legal recourse or the terms of arrangement. She argued that the public sector contractual arrangements were in practice a series of administrative procedures, rather than a set of contracts; because of degree of control exercised.

She also argued that there was potential value in using internal contracts to improve performance, but that improvements would have to be made to the process. These improvements included the administrative resolution of disputes should be clarified, and the consequences of trust 'failure' needed to be spelled out so that they would know how their actions might influence in the best way.

In local authorities, different procedures were adopted in different sectors of the Municipalities. Negotiations, rather than a strict sealed bid approach, preceded the outsourcing of computer contracts, implying the development of a close relationship between the departments and the computer suppliers. Major agreements between the social assistance department, tax departments and the TEC (IT services firm) in Elbasan Municipality started as a very detailed and punitive contract but grew into more trusting arrangements as the year progressed.

Influences on the type of contract

There are a variety of influences on the type of contractual relationship, which people adopt internally within the public sector and externally between it and private and voluntary sectors, including legal requirements, the structure of the market, managers' approach to quality and efficiency, as well as political and administrative rules under which the contracting is done.

Law and regulations

A major determinant of the nature of transactions and contracts is of course the rules established by the government. According to the Albanian legal framework, there are laws,

such as ('Tendering law' 2008), which applies the public authorities to promote competition and therefore mitigate the development of long-term and less competitive relationships.

In the public services, there are those who believe that contracting is a matter for the law and lawyers. This view is especially held by lawyers, who are involved in drafting the contracts and therefore think that they should also be involved in determining the relationships between parties. They apply the same principles to contracting with civil engineering companies, cleaning companies and a local branch of a charity. While the purchasing side of local authorities needs to be protected, the law is not the only answer. As a standard textbook on the law of contracts states:

Writers of the contract textbook tend to talk as if in real life agreements are effectively controlled by the law as stated in their books. A moment's reflections will show that this is not so. There is a wide range of transactions where the sums at stake are so small that litigation between the contracted parties is exceptionally unlikely..... in substantial areas of business, contractual disputes were resolved by references to norms which were significantly different from the theoretical legal position. The most important single reason for this seems to be that, in many business situations, the contract is not a discrete transactions but part of a continuing relationship between the parties and that insistence on certain legal rights would be disruptive of that relationship..... In other areas of business, strict insistence on legal rights is common (Specification... 2008).

It would seem, then, that the law and legal obligations are not the whole explanation for contract forms or a sufficient guide as to how to contract, except in cases where there are specific legal requirements which cannot be avoided.

Quality and efficiency

More recent work on contracting has suggested that there are other factors beside these structural market determinants which can influence the way in which organisations make transactions with each other. For example, Sako found that even where there is a large number of potential suppliers, purchasers may wish to develop a longer-term relationship with a small number of them. They do this because of the potential for improved quality and a more economical long-term series of transactions.

Politics

The third influence is politics. There is a reasonably close relationship between companies supplying public services and local authorities. For example, the process of developing competitive tendering in local government was created by advisers drawn from the companies which wished to compete for the local authority work. As well as advisers, working parties were established to allow companies to say how they would like the process to be or-

ganised. On the other hand, there were local authority members, especially representatives from the left politic parties, who did not want to contract out to the private sector functions which had been previously done by directly employed labour. These included left party-controlled authorities, but there were also right party authorities whose members resented being told how to run their affairs by the Department of the Environment. In a survey in the Elbasan Municipality, April 2009, contractors complained that some councils deliberately organised the contracting process in such a way as to frustrate competition. Even among those who had won Elbasan local authority contracts, 25% were fairly and 11% very dissatisfied with the process (Elbasani Information Newspaper p. 4). The reasons for this dissatisfaction were that the councils did not want private contractors, the documents were too complicated and the procedures too difficult. On the other hand, in central government, work had been awarded frequently to private contractors without a bid from the current employees.

‘New Institutional Economics’

Once economists started to realise that the real world exhibited few of the features of the theoretical world of perfect knowledge and perfectly rational choices in a perfectly competitive market, the problem arose: how to explain market behavior when these conditions do not apply. The problem is important in the context of government contracting, since only rarely do conditions of perfect competition arise in the field of the government procurement: in relatively low level purchases, such as stationary or vehicles, there may be a highly competitive market with many competing alternative suppliers, in which it is possible for governments to gather sufficient information and have the capacity to make well-informed, optimal decisions.

In procurements that typically absorb large amounts of public funds, such conditions do not apply. Markets for the supply of such things as big computer systems are characterised by a small number of suppliers and complicated products and services, about which the buyer will have less knowledge than the supplier. Local governments are often faced with a small number of service suppliers, especially in expensive services such as secure accommodation for orphans. It is likely that governments will not find it possible to collect, absorb and analyse sufficient information to make the optimal choice, even if there is a compulsory tendering system in operation.

The arrangement between a local authority and a contractor is subject to the same pressures as any other contractual arrangement: each side wants the best outcome for themselves and will use whatever advantage they can to achieve this. Both sides will try to minimise the risk attached to themselves from entering the contract. The contract will reflect the balance of knowledge and power between the parties and the nature of the relationship between the two.

There is a body of economics concerned with the contractual relationship between parties in the real world (as opposed to the theoretical world of perfect information and large numbers of willing buyers and sellers beloved of economic theory).

This branch of economics is sometimes called 'The New Institutional Economics', although by now it is no longer new. The underlying questions of this branch of economics are:

- Why do firms sometimes choose to buy their inputs in the market place and at other times decide to make the inputs themselves?
- When is it best to organise production through the market and when is it best to organise it through a hierarchy of employees?

More broadly,

- Why do organisations exist, and what determines the boundary between one organisation and the next?

These questions were first asked by (Coase 1937, Williamson 1975) developed Coase's work further to look systematically at the problems posed by the fact that markets are not perfect. In a book published in 1975 he looked at the question: when it is better to purchase goods and services in the market and when is it better to produce them yourself, using your own employees?

This is essentially the question for government: when should they write a contract with an independent body for the supply of services and when should they provide them using their employees? Under conditions of 'bounded rationality' not all information is known, or it is impossible to take all of the information into account in the decision process. The conditions in the market that Williamson considered were:

- **Complexity:** the transaction is so complex that it is not possible to consider all the options.
- **Uncertainty:** not all possible futures can be predicted, so it is not possible to write a contract that takes them all into account.
- **Language:** It is not possible to specify everything in language that both parties to contract can agree on.
- **Small numbers:** where there are very few suppliers, those in the market can engage in opportunistic behaviors to the disadvantage of the purchasers.
- **Information 'impactedness':** where one side to the transaction has more information, especially about costs, than the other.
- **First-mover advantages:** by which winners of a contract gain information that puts future competitors at a disadvantage and reduces the impact of competition in all future transactions.
- **Atmosphere:** the moral stance that parties to the transaction take, which may not be perfectly economically self-seeking.

Williamson usefully draws these elements into a framework, which he calls the 'organisational failures framework', which is illustrated in the Figure 1 (Ibid... p. 40).

Human Factors Enviromental Factors

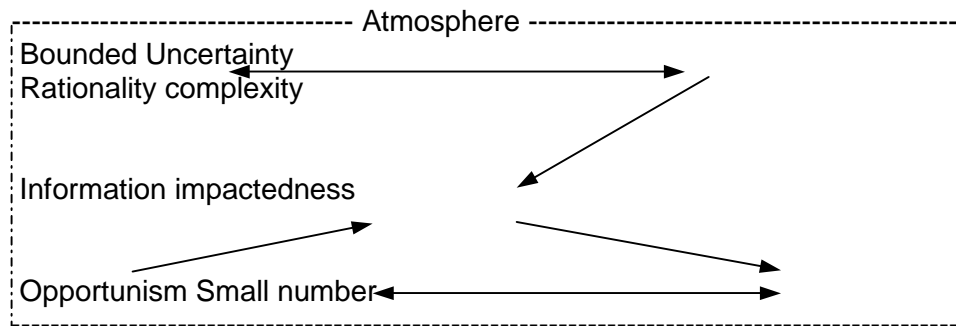


Fig. 1. The organisational failures framework
Source: own.

We can use this frame work to study the way contracting has developed between local authorities and companies.

In most markets, people involved in transactions are not normally able to make completely optimal decisions : they do not have perfect knowledge; they do not have the capacity to process all the available information for every transaction.

Even if they had the information and capacity, there remains the problem in any transaction of trying to ensure that the person from whom one party is purchasing delivers what is expected, and is motivated and enabled to do so in all the possible circumstances that might subsequently arise.

Solutions to 'bounded rationality'

A contract that covers all possible events or contingences is called a 'complete contract', which would be written in such a way that both parties know exactly what the consequences of every possible event would be. In practice, such contracts are very rare and can be written only for very simple transaction. Complicated transactions make the cost of writing complete contracts too high under the conditions of bounded rationality.

The existence of bounded rationality results in the possibility of '*opportunistic behavior*' through which one party of the transaction tries to take advantage of the other. One way that one side can gain an advantage is by knowing more than the other side, or by keeping secret '*private information*'. The fact that information is not perfectly shared (known as '*information asymmetry*') leads to '*adverse selection*' and '*moral hazard*', both forms of self-interested misbehavior made possible by imperfect knowledge.

The problem for local authorities is : how should the procurement process be organised when complete contracts are not feasible?

It is especially difficult in the case of services, as opposed to products, in that the characteristics of the service are technically difficult to design. It is also the case that, in many public services, the specification of the full range of possible contingencies is impossible to write in advance.

Milgrom, Roberts (1992) describe one set of solutions to the problem of bounded rationality in the world of real contracts that can never be complete. These solutions are:

- relational contracts, through which long-term relationships are developed;
- implicit contracts, where shared objectives make explicit contracts unnecessary;
- developing commitment;
- ex-post renegotiation;
- dealing with specific assets, which the contractor has bought solely for the purpose of fulfilling the contract;
 - the 'hold-up' problem, whereby the buyer is completely dependent on a single contractor;
 - private information and pre-contractual opportunism, whereby the contractor cheats the purchaser;
 - measurement costs;
 - adverse selection, where contractors only choose contracts, or part of contracts, that can make big profits, leaving aside the rest;
 - signaling, screening and self-selection.

The question for local authorities can now be reformulated: 'How can local authorities ensure that contracting with private sector avoids the dangers identified in the New Institutional Economics literature'?

The first way suggested by Milgrom and Roberts was the establishment of 'relational contracts', by which they mean a relationship between the buyer and the seller that does not rely entirely on the contract for the supply of a particular good or service at a particular time but involves the establishment of expectations on both sides that a longer-term relationship will develop in which the two sides behave in mutually beneficial ways. Later in this paper we will look in more detail at how such relationships require contracts that differ from those appropriate to 'adversarial' relationship, in which there is very low trust and heavy reliance on the contract itself to manage the delivery of the good or service.

For managers, therefore, there are no simple answers to the question of how to establish and manage contractual relationships. On the one hand, there are market structure considerations and efficiency and effectiveness considerations which would provide some guidance as to the most effective way to do things. In some cases, these might lead to a preference for long-term contracting, in others for short-term. The nature of the market may lead to a desire to establish long-term close relationships with suppliers, or may lead to

frequent competitions in order to keep prices down. On top of these influences on practice are the legal considerations. The law itself and the regulations may force people to behave in a particular way, even though they know that the results will not be as good as if they behaved in other ways. There are some more local legal influences. Legal advice may, in itself, lead people to behave in ways which they do not think make managerial or contractual sense. Lawyers accustomed to caution may be more interested in generating apparently detailed and enforceable contracts which professionals know cannot be enforced in practice. Politics can also determine managerial decisions. While managers may know that it would make more sense to keep a service in-house, they are not able to exercise that choice. The opposite can also be true : managers may wish to contract out but are instructed to retain a directly managed provision of the service.

However, there is still some discretion. In the rest of this paper we look at the elements of the contracting process and ask what the best approach to each of these elements in different circumstances would be.

Obligational and adversarial contracting

'Relational' contracts are sometimes referred to as 'Obligational' contracts, in which the two parties have obligations to each other to make success of their joint efforts beyond the terms of their immediate contractual relationship. 'Obligational' contracts are contrasted with 'adversarial' ones in which each side is out for their own advantage from the immediate contract and is unconcerned with the success of the joint enterprise.

Sako has developed a framework for understanding contracting behavior, using these two archetypal relationships. At one extreme is the Obligational Contractual Relationship (OCR), where the two parties trust each other, work together for mutual benefit, share risk and things with each other which go beyond the details in the contract. Adversarial Contractual Relationship (ACR) is at the other extreme, where there is low trust, the expectation that each side wishes to gain at the expense of the other and contracts are used to protect each side from the other. Sako breaks down the contracting process into eleven elements: transactional dependence; ordering procedure; length of trading; documentation; the approach to 'contractualism' or contingencies; contractual trust; competence trust; goodwill trust; technology transfer and training; communication channels and intensity; and risk-sharing.

Transactional dependence

If a purchase wants to be able to switch from one supplier to another, they will have contracts with a large number of people. They can then use the threat of switching suppliers to make a supplier do what they want. On the other side, suppliers may wish to maintain contracts with a large number of purchasers to minimise their dependence on one. In these

circumstances, the relationships are likely to be distant. Under OCR, the purchaser may wish to develop closer relationships with a smaller number of suppliers and offset the dependence created by fewer closer relationships.

Experience with regard to dependency is varied. Local authorities which have established contracts for items such as refuse collection (as in the case of the Municipality of Elbasan and the Commune of Bradashesh) have sometimes become completely dependent on a single firm, which has won the contract for the whole of that local authority area.

We would expect high dependency to result in a close relationship between the two parties. In practice, the legal constraints and the lack of experience on the part of purchasers led to the development of detailed contracts and specifications with complicated procedures for coping with default. As time went on, however, both sides realised that the interdependency which comes from having a single supplier and a single purchaser allows a relationship which is closer than those implied by spot contracts or frequent switching of supplier.

Ordering procedure

The stereotype of the adversarial approach to ordering was encapsulated in the compulsory competitive tendering legislation for local authorities: competitors have to bid for the work, the purchaser then chooses the supplier as a result of the bid, rather than any other aspect of the bidder's work or reputation, and the price was fixed before the contract was agreed. The opposite, OCR, way of ordering may not involve bidding and if it does, the bid price is not the only criterion for placing an order with prices being settled after the decision as to who will be awarded the contract. The way orders are placed has an effect on the relationship between the parties. If a long-term relationship is expected, both sides need to decide whether such an arrangement would be beneficial. This requires more than doing some pre-tender checks and then opening the sealed bids.

Bidding is almost universal in the public sector, for reasons of propriety. Public accountability requires contracts to be awarded fairly, without corrupt favouritism. This is interpreted to mean that the only way to accept bids is through a procedure which distances the two sides. Albanian and EU state regulations require large public sector contracts to be advertised in the Gazette and bids invited from companies from all states. These regulations imply an adversarial style of contract, rather than the development of a close relationship.

The ordering procedure sets the tone for the nature of the relationship between the two parties. If contracts are based on a quotation against a specification which is the same for all bidders, the responsibility for developing the contract and specification rests with the purchasers, rather than being a joint effort between buyers and suppliers. After the contract is let, the process of contract management is therefore concerned with ensuring conformance to the specification.

Once a contract is let, purchasers may try to develop a closer relationship than that which had existed prior to the award. However, contracts are normally for a fixed term, at

the end of which a new bidding process starts. The close relationships are stopped and the distancing implied by distant treatment begins again.

Length of trading

In a ACR contractual relationship, the parties only expect to trade with each other for the length of contract. In OCR, there is an expectation that, if the things go well, there will be further contracts and there will be a mutual long-commitment between the parties. There is the possibility of 'roll-over' contracts in the local authorities where contractors are allowed to continue for a further period. However, lawyers say that it is unwise to include clauses in the initial contract which implies that successful completion of a given contract would most likely result in another.

The length of trading can determine the type of company or charity with which the local authorities trade. Large suppliers with a variety of contracts in the public and private sectors are more likely to be able to cope with a series of time-limited contracts with any purchaser than small local suppliers. This applies especially in community care, where small local voluntary organisations become completely dependent on their local authority for funds. They are, in other words, dependent on the one transaction, the lack of which would result in the end of the organisation. In practice, they often lurch from one short-term contract to the next.

Document for exchange

In ACR, an attempt is made to write all the terms and conditions, including substantive conditions. Every possible item is written down. In OCR, the contracts concentrate on procedural rules which set out how problems would be resolved if they happened to arise, leaving individual issues to be dealt with as and when they occur. Contracts may even be oral rather than written.

In the Elbasan Municipality, contracts and their associated specifications have generally been long and detailed. In some cases, manuals of procedure which were in place when the service was directly managed were used as the basis for the contract and specifications. For example, the original contracts between the social assistant department and tax department with TEC (IT service firm) were the old department area office programme manuals. However, people have realised that it is impossible to write everything down and that in any case, the fact that the contract contains a long and detailed specification is no guarantee of service delivery. Contracts have become less detailed as people have learned that there are other ways of ensuring quality, such as involvement in the suppliers' quality assurance procedures or talking to the users of the services.

'Contractualism'

Sako refers the treatment of contingencies as 'contractualism'. A contingent claims contract is one in which contingencies have to be defined, a procedure has to be established to agree whether a contingency has occurred, and the consequences of the occurrence are specified.

Most contracts have contingent elements: exceptional weather can affect highway maintenance contracts, etc. The question is whether each possible contingency can be sufficiently defined in advance and whether the recognition of its occurrence can be spelled out in advance. The OCR option is to agree procedures in which both sides can agree on contingencies and what should be done as a result, and as such rely on trust and an expectation that an agreement can be reached. The ACR option assumes that an agreement will not be reached or will be difficult, and that every contingency must be defined in advance.

There is a mixture of approaches to this question in the public sector. Attempts to specify contingencies, have not always worked. Local authorities usually have a 'banding' system in which progressive disabilities trigger progressively intensive service, but there have to be procedures in which the purchasers of service and the provider agree the extent of an individual's difficulties.

Trust: contractual, competence and goodwill

Sako distinguishes three areas of trust: contractual, competence and goodwill. The ACR approach to contractual trust means that the supplier does not do anything without a prior, written order. In an OCR relationship, supply or change to specifications can be effected as a result of oral communication. Competence trust is concerned with the degree to which the purchaser trusts the supplier to deliver the correct quality of a product. If there is low trust, the purchaser will inspect heavily and presume that the supplier will try to cut corners. In a high trust relationship, the purchaser may be involved in the supplier's quality assurance procedures, but will not carry out much, if any, inspection. Goodwill trust refers to the degree to which each side is willing to become dependent on the other.

Trust is a very important element of public sector contractual relationships. The degree of trust depends partly on the sort of relationship established during the ordering procedure. If the order is placed on the basis of the bid price only, it is likely that the chosen suppliers will be operating on low, or even negative, profit margins. In order to make a profit, the supplier has to shave the quality as close to the specification as possible, if not below it. The purchaser's main function then becomes one of trying to make sure that the specifications are met, requiring inspection and checking. If the winning contractors believe in any case that the purchaser did not wish to contract with them but was forced into it by the legislation, there is no initial basis for establishing trust, and adversarial relationships are probably inevitable.

Trust can develop during the contract period or as a succession of contracts are completed. It is natural for buyers to be wary of new suppliers until they have seen proof that they can be trusted. Sometimes the voluntary sector may be trusted more than the private sector, whose profit motive causes immediate suspicion by some sectors managers of the local authorities.

Technology transfer and training

In an OCR relationship, the purchaser is willing to help the supplier develop the best technology and skills. This may involve helping the supplier to organise training or allowing them to join in with joint training, which may not be charged. In an ACR relationship, help is given only when it is fully charged and paid for. One area in which this is important is in the cleaning service of Elbasan. If purchasers do not fund the development of new technologies, research and development has to be funded in other ways. In practice, since prices are supposed to be a little bit higher than the cost in the cleaning service contract, there is no surplus available for research, which is funded through a separate mechanism.

It is unlikely that there would be much transfer of technology and training in the mainly adversarial relationships which have developed: public accountability for funds, which pushes the relationship in an adversarial direction, makes it unlikely that free funding of development would occur, as a routine part of long-term contractual relationship.

Communication channels and intensity

In ACR, the communication channels between the two contracting parties are specified in the contract. Nominated officers on each side are allowed to speak about technical and financial matters, according to their individual competence. In an OCR relationship there are multiple channels of communication as each side tries to understand the other. As with other aspects of the relationship between public organisation and contractors, frequent contact is treated with suspicion, especially informal contact. Lunches are viewed as corruption. While there may be some basis for suspicion, it is unfortunate that the need for proprietary stops beneficial exchanges between the two sides.

The national audit office surveyed the concessionaire contract (Concession...2000) for the water supply of the Elbasan with the Berliner Wasser Betriebe and showed that both parties, Albanian and German were still mainly concerned with achieving their own distinct objectives rather than coming to a jointly beneficial agreement. Both parties surveyed thought that forming joint long-term strategies and providing comprehensive and timely information as well as maintaining regular communication between chief executives and different public authorities, were vital in achieving good relationship (Report... 2003).

Risk-sharing

In an OCR relationship risk is shared, based on principles of fairness. In ACR, risk may not be shared but the acceptance of risk is defined in advance. There are three aspects of risk in public service contracts: risk of price change, risk of change in the volume of demand, and the risk that arises from suppliers innovations.

With relatively low inflation, the risk of price change being very different from that predicted at the time of signing the contract is small. However, there are prices which may fall suddenly, because of technical changes. For example, much cheaper computer processing, may produce a 'windfall' increase in profits for the supplier. A risk-sharing approach would lead to such windfalls being shared between the supplier and the purchaser.

The second type of risk refers to the possibility that the volume of work predicted will be not forthcoming. The supplier sets up an operation to provide the predicted volume and incurs costs which are not recouped. Again, a risk-sharing approach would involve sharing a proportion of these costs. One way of doing that is for the purchaser to guarantee a certain volume of service will be purchased, even though it may not be required.

The third element comes from innovation; a supplier may invent and offer a new way of providing a service, which turns out to be unsuccessful. Without such innovation, the contracting process will stop the development of new services, as all specifications are based on already accepted practice.

Public-Private Partnerships are based on the premise that the contract can allocate the risk between the private and public sector and the contract can be formulated to reward risk taking. In the case of unpredictable volumes, such as water supply of the Elbasan where the revenue to the contractor depends on number of customers and volume of water that each of them consumes, risk avoidance cannot be achieved by changing contractor behavior.

The specification

Inputs, process and outcomes

Sako's work dealt mainly with the supply of components, which could be specified in physical terms. The purchase of a service can be more complicated. Firstly, it may be difficult to specify the result required from the service in an unambiguous way. Even in a relatively simple, physical service such as green-grounds maintenance, the result of the work will be hard to describe: what is a well-maintained flower bed, when the answer to the question determines whether a contractor gets paid or not? Attempts to answer such questions have resulted in elaborate schemes of measuring the length of grass and counting the number of flowers.

In other services, the problem can be more acute. What is the satisfactory outcome from the water supply if the water is clean and drinkable? There are ways of defining these things, but if specifications are to be used as the basis for a legal contractual obligation,

they are more difficult to define and measure than material things, which can have measurable characteristics and tolerable deviations from them.

Because of this, many specifications rely on a description of the processes by which the services are provided. If the removal of the garbage and cleaning of the roads is specified by quantity, it is enough to ensure that the bill will be paid. If the processes cannot be described in detail, then the specification may rely on the inputs used : the number of hour of a landscape-gardener's attention for the maintain of the green. These descriptions of the input may include the qualifications and skills of the staff.

Information quoted in the specification has a big impact on the relationship between a purchaser and a provider of services. In general the provider has a professional or technical expertise, which they are offering as a part of the contract. If that expertise is usurped by the specification, the purchaser has to have all the skills required to write the specification and monitor performance to ensure that a good job is done.

The use of outcomes as the basis for a contractual agreement has two implications for the relationship. It assumes that the providers have the expertise to decide on the appropriate inputs and process required to produce the desired outcome. It also implies that the purchaser trusts the provider to make those decisions in the interests of arriving at the outcome, rather than in the interests of the provider or their profits. The higher the degree of trust, the more possible it is to use outcome specifications.

However, in low trust environments, the use of inputs and processes as the basis for the contract can produce problems of its own. How will the purchaser stay up to date with the best procedures? In services such as cleaning, for example, technology changes. New chemicals and machines increase efficiency and change working practices. If such a service specifies exactly the routines used and never change them, best practice cannot be achieved.

As time goes on the purchasers have less direct experience of services. While they may be appointed to the post of purchasing manager with the recent relevant direct experience, it is inevitable they will become detached from it over time. As their expertise deteriorates relatively to that of the providers it becomes harder for them to confidently specify inputs and processes.

Who should write the specification?

Therefore, the question 'what is in the specification?' begs another question: 'who should write the specification?' If technical and professional expertise is heavily weighted towards the providers' side, then it is sensible that they should at least be involved in writing the input and process part of the specification, with the purchasers becoming increasingly involved in specifying the required outcomes.

This brings us back to the beginning of the argument. If the purchasers are to allow the providers to specify the inputs and process, with the intention of providing the best possible

outcome for the money available, this implies a high degree of trust. If the providers are only to be trusted as far as to carry out their duties to the letter of the contract, then that contract must contain enough details to reassure the purchaser that they are getting a good deal. If they are to be trusted to make an impact on the service user and the left to decide how to achieve that, then there has to be a high degree of goodwill between the two parties.

There are two separate issues here, which are frequently confused. The first is whether the purchasers have the technical competence to write and monitor an input and/or process based specification. The second is whether the purchaser has sufficient trust in the provider doing their best to produce the desired outcomes and therefore has the confidence to write an outcome-based contract. A lack of trust was a product of uneven knowledge and profit-maximising behaviour on the part of the contractor.

Learning to manage through contracts

People have now learned that adversarial contracting is unproductive and expensive to maintain. Contractors for the Municipalities in Elbasan have complained about over-complicated paper-work and procedures. Elbasan Municipality's social service departments are trying to establish more collaborative relationships with the voluntary sector for the provisions of community care services.

However, people have also realised that there are constraints on the development of obligational relationships. Legal requirements to follow procedures put purchasers and providers at a distance from each other and emphasize the elements in which interests are opposed.

While the number of actual and potential suppliers varies between the sectors, there seems to be a relationship between market structure and contracting style : monopolies or near monopolies in the cleaning and green maintenance of the Elbasan have led to the development of longer-term relationships, less reliance on detailed inspections and other aspects of ACR relationships. In the relationship between Elbasan Municipality and their contractors there are still signs of adversarial relationships.

If there is an underlying suspicion of the private sector, it is likely that contracts will remain adversarial. The implication is that there will be a continuation of detailed contracts, harsh penalty clauses, heavy inspection and generally poor relationships.

Expensive failures

The contracting system that was imposed through the imposition of internal markets and enforced outsourcing improved as people, especially in local government, learned how to manage through contracts. Buildings streets procurement in Elbasan was one case which got out of hand and delays were sometimes measured in years rather than in months. In 2008, the public controlling Committee (Report... 2009) in Elbasan Municipality investigated

32 building street contracts that produced 1.1 million Euro of overspending. The average slippage was 8 months, or 11% of the projects' lifecycles.

In the year 2000, the Berliner Wasser Betriebe (a German firm) through a Public-Private Partnership-concession contract, entered to provide the water supply and to remove the waste water for the Elbasan Municipality. This contract was expected to last 25 years, but resulted unsuccessfully, and the German side did not go ahead with the work. The conclusions of the failure of this contract were:

- The project did not find the support of the other public institutions in Elbasan.
- There was no clearance on the specifications of the rights of public institutions.
- There was not a shared approach to risk management.
- It was the first contract of this type in the local authorities and there was no experience.

Benefits of the long-term relationship

The contractor relationship of the Elbasan Municipality and voluntary organisation 'Happy ours' in the resettling of the orphan children has lasted a long time. It led to the establishment of a collaborative relationship between the social service department of the Municipality and this voluntary organisation.

The contractor relationship of the Elbasan Municipality and the cleaning firm-Victoria Invest has been established for 12 years. This has brought the Municipality less reliance on detailed inspections and less cost.

CONCLUSIONS

The eagerness of the Elbasan Municipality to contract out large parts of the work required to deliver public services has sometimes overtaken the capacity to make contracting succeed. There are some structural reasons for this. Firstly, a contract between a local authority and a contractor is not equivalent to a joint venture between two or more companies collaborating to make a project or business venture successful: in most cases the revenues to the company come from public funds, not from customers who are attracted to the product of the joint venture. The available finance is finite, subject to renegotiation as costs rise, rather than subject to success in the market. Companies' profit will only come by getting more money from the local authorities buying their service than the service cost to produce, rather than from jointly making the service profitable.

Secondly, there is an almost inevitable information impactedness. Regardless of the sector, the expertise is more likely to be with the contractor rather than the purchaser: that is where the best returns to individuals are and where the greatest professional satisfaction is. Given the first condition, that there is a finite amount of money and therefore a zero-sum

game, the fact that the expertise is likely to be concentrated in the provider side of the transaction is very likely to lead to opportunism.

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