

## **A Guide to Smarter Contracting**

*Simon Domberger and Christine Hall (eds), The Contracting Casebook: Competitive Tendering in Action, AGPS, Canberra, 1995*

*Reviewed by Stephen King*

**C**OMPETITIVE tendering and contracting (CTC) has transformed Australian public-sector management. Since the mid-1980s, there has been a continuous shift away from 'in-house', untendered service provision by the public sector. Competitive tendering and contract-based services are now the standard particularly for 'non-core' business activities such as cleaning, waste management, maintenance and information technology services.

Despite the clear evidence that CTC brings efficiency gains, its introduction has not been free from disagreement about how to measure its costs and benefits and about service quality. For individual contracts, disputes can also arise over inspection procedures, liability and penalties for non-performance or inadequate performance, cost allocation, and contract termination. Moving to CTC may involve significant costs. The tendering process may involve vetting potential bidders and preparing an in-house tender. If in-house workers believe that they will face unemployment, then this can lead to reactions ranging from a loss in morale and performance to deliberate sabotage of equipment. Even after the preferred or winning bidders are chosen, a successful contract involves considerable negotiation before it is implemented. Such negotiations may well continue over the life of the contract as new issues and unforeseen circumstances arise. While the potential gains from contracting are high, these can easily be overwhelmed by the costs of a mismanaged tender. It is important to understand the risks and potential mistakes that can arise from contracting in order to better evaluate the size of the potential benefits and where these benefits are most likely to be achieved.

*The Contracting Casebook*, a product of the CTC Research Term at the University of Sydney's Graduate School of Business, provides a series of useful case studies which help to fill this gap between individual experience and overall performance. The case studies (mostly drawn from New South Wales) cover a range of services from grass-slashing to the building and operating of plant at a power station. The book canvasses both success and failure in contracting. It provides a complete discussion of the background, issues and outcomes for each study. The cases are well written, absorbing and thought provoking. Most important, they provide powerful insights into the CTC process.

Preparation for the contracting process is crucial. The cases clearly show that using contracting to side-step unions and eliminate restrictive work practices is fraught with danger. Introducing contracting without adequately consulting existing workers and the relevant unions can lead to delays and unforeseen expense. Attempts by the NSW Government Cleaning Service to introduce contracting without

union consultation led to legal action, strikes and direct political lobbying by the union. A subsequent industrial relations hearing made a redundancy award of about \$25m against the Government Cleaning Service.

One study of hospital cleaning services shows that unions successfully used more subtle means to undermine contracting. After gaining a guarantee that staff unwilling to work for the successful contractor would be redeployed, the union 'instructed its members not to get involved with the contract, forcing the contractor to start with a full complement of new staff' (p. 121). This loss of continuity and inside knowledge contributed to the termination of the contract after only six months' operation. Yet unions risk losing member support if they blindly oppose contracting, as the Mosman Council case study shows.

Numerous other issues need to be addressed before the contracting process can begin. What services are to be contracted? Government trading enterprises (GTEs), such as Pacific Power, may face legal restrictions on their ability to contract out 'core functions'. Will whole projects be tendered or will there be a split in responsibilities between contract and GTE staff? For an infrastructure project covering design, construction and operation, should tenders be called for each component, for the project as a whole, or on a mixed basis? For what period of time should the contract apply? The cases consider contracts ranging from twelve months for medical services to 20 years for a capital works project. Should an 'in-house' tender be allowed or encouraged? If so, how is 'fairness' to be maintained, particularly when the in-house bidders may have an informational advantage? How should overheads be allocated to an 'in-house' bid? Each of these issues arises in a variety of cases. The success of the contracting process often depends on how they are resolved.

Once tenders are called, there will usually be some form of pre-bid vetting. Potential bidders may be eliminated because of financial or other constraints on the operation of the contract. Further hurdles may be raised because of political or industrial-relations concerns. The process does not finish once the contract is awarded. Success or failure often depends on events after the contract commences. The transition period between in-house and contract provision is crucial. Politics may create disputes, as occurred with garbage-collection contracts in the Sutherland Shire. If the supporters of the original contract face re-election, their opponents may undermine the contract to gain votes.

Even the best-designed contract may have flaws that will need to be resolved as they are discovered. One clear, practical lesson from the cases is that successful contracting depends on the ability of each party to respond with both trust and flexibility when conflicts arise. Renegotiation and opportunism may be difficult to separate. Attempts by the contractors to pursue what they see as legitimate areas for negotiation may be viewed as an attempt to weaken the contract conditions. Hostility to renegotiation can result in the failure of the contract. Both the Sutherland Shire case and the 'hospital C' cleaning contract provide useful examples.

The cases show that although the savings from contracting may be high, they are extremely variable. In some cases the contracting process led to a loss (as in Suther-

land Shire) or an insignificant gain (as with part of the Pacific Power tender). In others cases, the gains were apparently large but involved hidden costs. The case of medical-services contracting shows savings of 84 per cent. However, the study also notes that these savings ignore the implicit costs of providing parking to the contracted doctors, a privilege valued by one doctor at about \$10,000 a year. The measured savings may also have been unsustainable, with the cost rising by 30 per cent when the contract was renewed. Yet successful contracting does appear to result in cost savings. For example, one successful hospital cleaning contract led to savings of 29.7 per cent.

What is the source of these savings? The cases shed some light on the conflicting claims of efficiency gains and worsened worker conditions. Both arguments are partially correct. Efficiency gains arose from a variety of sources. Even cleaning productivity can be improved by carefully analysing how the tasks are performed. The savings under the Government Cleaning Service contract were partially based on the introduction of team cleaning. Hospital cleaning benefited from the retraining of staff to use newer, more suitable equipment. A reduction in time spent in meetings by the hospital cleaning manager, from one day per week to 15 minutes a week, also helped. At the same time, successful innovation often boosted staff morale and productivity. But some savings clearly came from worse conditions. The tumultuous transition period in the Sutherland Shire contract involved garbage truck drivers working 'a longer day, sometimes up to nine hours in duration' (p. 67). Even in the successful case of the Government Cleaning Service, union representatives 'firmly believed that the contractors' notion that they were making cleaners work smarter, not harder, was simply not true' (p. 27).

The weakest aspect of *The Contracting Casebook* is that it presents the facts but often avoids drawing conclusions. Only when considering hospital cleaning does the book explicitly compare cases. However, the great value of the book is that it provides a variety of CTC cases, which enable the reader to consider why some contracts succeed and others fail. The type of cases considered present lessons that would be hidden by more formal empirical analysis. The important lessons can easily be distilled from the above summary. Preparation for the tender is crucial, particularly if costly labour disputes are to be avoided. Contracting must be viewed as a continuing relationship, not an excuse to delegate and ignore. All parties to a contract must show flexibility and a willingness to consider any grievances. Significant benefits from contracting are likely to reflect true efficiency gains, albeit of the sort that lead the outsider to wonder why these benefits could not be seized with in-house provision. Perhaps organisations need the competition created by the tender process to focus better the mind on potential efficiency gains. Cost savings may reflect a fall in quality or a worsening in worker conditions; but this is more likely to be true of unsuccessful contracts. Overall, CTC presents significant gains, if applied carefully to the correct services.

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