# HOW TO PREVENT CORRUPTION WITHOUT AFFECTING EFFICIENCY? AN OVERVIEW OF SAFEGUARD MEASURES FOR CONTRACTING OUT PUBLIC SERVICES

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*The paper addresses the issue of finding the right balance between regulatory oversight, decision-making flexibility and reliance on market forces to safeguard the contracting-out process from corruption. The paper analyses the corrupt practices associated with contracting out local public services and the causes and consequences of this behavior. Taking into consideration new anticorruption strategies, we make recommendations for attaining equilibrium between flexible safeguard measures and accountable and transparent practices aimed at verifying whether regulations and standards are met. The strategy also emphasizes the training of public officials, to provide them with appropriate skills and professional capacity to identify and manage corruption risks. The last part of the paper recommends future research to identify best practices among different communities and states attempting to control corruption practices when contracting out public services.*

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**Introduction**

The public entrepreneurial movement is more than 30 years old. Starting in the 1970s in the US, fiscal constraints forced local governments to find alternative ways to provide public services (Borins 2002). Over that three-decade period nation states all over the world have been inclining toward decentralized public sectors, market-oriented private sectors and greater partnerships among sectors (Kettl 1998) (Perlmutter and Cnaan 1995) (Hamlin and Lyons 1993). Europe greatly intensified its swing in this direction in the last ten years and the European Commission issued a Green Paper to assist member states and sub-state governments to deal with this trend (Commission des Communautés Européennes 2004). Aspects of this transformation have been called “new public administration” (Kettl 1998) or “reinventing government” (Osborne and Gaebler 1992). The general term, “public-private partnerships” is often applied to many activities (Hamlin and Lyons 1995).

Some examples of new approaches to government include: 1) the privatization of government owned properties; 2) governmental use of incentives to promote public goals through the success of privately owned businesses (Hamlin and Lyons 1996); 3) public choice in the consumption of government services through fees instead of taxation; 4) performance or results-oriented allocation of resources to public organizations (Ostrom and Ostrom 1971); 5) joint ventures between private businesses and public organizations; 6) greater use of third sector organizations to deliver public services (Lyons and Hamlin 2001); 7) greater use of fourth sector individuals (citizens groups and voluntary associations) to deliver and evaluate public services (Hagiwara 1996) (Roubon 1999); 8) contribution of public resources to private capital formation of private businesses (Hamlin and Duma 1999) (Hamlin and Neamtu 2005); 9) use of public powers such as eminent domain and police powers to accomplish public goals by promoting the success of private organizations; and, 10) the contracting out of public services (Osborne and Gaebler 1992); to name a few.

Various factors explain the increased recourse to public-private partnerships. In view of the budget constraints confronting local governments, public-private partnerships meet a need for private funding for public sector activities. Governments also wish to benefit more from the expertise of the private sector in areas like marketing and supply chain management (Cobarzan and Hamlin 2005). The development of public-private partnership is part of the more general change in the role of the government in the economy, moving from direct operator and provider of public services to organizer, regulator and controller (Commission des Communautés Européennes 2004).

The present paper will center its analysis on one form of public-private partnership, the contracting out of public services. In its simplest form, contracting out public services means that the municipality chooses a private company to provide a service normally provided by government and pays the company a contract fee for providing the service. More generally, a wide variety of effective methods exist for inducing the private sector to provide public services. They include management contracts, operating contracts, exclusive franchises and flexible franchises. These forms of contracting out will be discussed later in the paper.

On the surface, the advantages of contracting out seem straightforward. In the case of the service contract, if the fee that the city would pay the private company for this service were less than what it would cost for city employees to do the job, then municipal taxpayers would save money that could be used on other activities or to reduce taxes. And, good reasons exist for why a private company might be able to do the job for less. Some reasons include lower labor costs, better management, greater experience from providing the same service in other communities, better equipment, and better technology. A private company that is in competition with other companies might have more incentive to be innovative, seek lower cost labor, and develop better technology (Cobarzan and Hamlin 2005).

Yet, even this simple process of contracting out government services raises a multitude of issues and problems. The contracting-out process is vulnerable to many corrupt deals. This process usually involves a large expenditure of funds and has a major impact on the government budget. As this paper discusses, the process creates several reasons to pay off public officials. A firm may pay to be in the pre-qualified bidders, to get inside information, to structure the bidding specifications so that the corrupt firm is the only qualified company, to be selected as the winning contractor, or to skimp on quality, to name a few. Other reasons and forms of corruption related to contracting out public services will be presented later in the paper.

Corruption in contracting-out is widespread around the world; it is not limited to developing nations. It takes many forms and can impose large costs upon communities. No strict relation exists between the size of public sector and level of corruption (e.g., Scandinavian countries do not conform the rule) (della Porta and Vannucci 1999). The size of this phenomenon can go beyond our limited understanding.

Without strict supervision of the quality of the works or of the services delivered, corruption can affect people's safety. Corruption can become systemic, affecting all levels of an institution. Those bureaucrats, who might have found out about corruption, can be gradually brought into the precise system of corruption that provides each person a certain percentage of the take (della Porta and Vannucci 1999).

The gravitation towards public-private partnership, and particularly increased contracting out public services to promote efficiency, challenges and sometimes strains some of the most basic values of any public system, such as equity, transparency and ethical behavior. How, for example, does a government of the people, engage in various forms of private negotiations and interactions with private businesses and citizens? How does the public sector ensure that the views of the general public are properly included? How does government maintain objectivity in selection, oversight and compensation of the private partners? When public-private partnership is used, how are disadvantaged groups and areas served if private contractors find it difficult to make a profit serving them, or, what if the resulting price for a public service is so high that the less fortunate are financially excluded (Cobarzan and Hamlin 2005).

Some forms of public-private partnership can increase transparency, but many forms of public-private partnership complicate governmental control and oversight as they put greater trust in decisions made in the private realm, outside of public view. The less transparent these interactions become the greater the chance for and temptation for corrupt practices to be inserted. This fact often leads to calls for greater regulation of those private decisions. On the one hand, pursuing a more entrepreneurial approach to government in combination with increased governmental regulations might increase governmental efficiency in the narrow sense of the word. On the other had, over regulating contracting out can destroy the benefits of flexibility, innovation and responsiveness of the entrepreneurial spirit (Blendermann et al. 2004). Achieving a balance is difficult, and that balance varies with changes in technology and from culture to culture.

The question that this paper raises is how to design safeguard measures that prevent corruption while not hindering the efficiency of the contracting-out practices. In other words, what is the right balance? The number of studies that analyze corruption related to public-private partnerships and consequently contracting out is limited. The major emphasis of these studies is on procurement and privatization, and, in this context, some of the discussions can be transferred also to the contracting-out process. The previous research concentrates on analyzing the mechanisms, causes and consequences of corruption. The strategies for solving this problem are designed to address the broader problems grounded in the administrative and political system.

The paper will concentrate in the first part on presenting the debate over the desired level of regulations with regard to the general activity of a public institution. This debate can be transferred also to the contracting-out process of public services. The second part will briefly present the mechanisms, the advantages and some issues raised by the contracting-out process. The third part will present some corruption problems that can occur during this process and after the contract is awarded. The fourth part analyzes causes and consequences of corruption. The fifth part will bring into discussion new approaches in designing anticorruption strategies. The sixth part will present general recommendations to prevent corruption. The last part will propose a design for a future research program. We intend to compare how contracting-out processes are regulated in different countries with different cultural values, find examples of successful practices and learn how these practices can be transferred to a different cultural contexts to solve a similar problem.

**Level of regulation**

From the perspective of anti-corruption strategies, the goal of regulations is to limit the opportunities to extract bribes. But, an endless debate continues regarding the optimum level of regulation to prevent

corruption. On one side, neoliberals claim that excessive regulations are responsible for the explosion of corruption. Other authors argue that deregulation increases the number of corrupt opportunities substituting a corrupt public official with a corrupt private one (Susan Rose-Ackerman 1978). The conditions that generate corruption in the absence of intervention are the same as many of the market failures that justify government intervention (Susan Rose-Ackerman 1978). A third group of authors argue that the amount of regulation is not important. Corruption is present in any state, whether it is laissez-faire or interventionist (della Porta and Vannucci 1999). Corruption originates in state apparatus characterized by both an excess or a lack of regulation (Susan Rose-Ackerman 1999).

The desired goal of the rules regulating the activity of public institutions should be to achieve the general public interest and to increase citizen trust that taxes are being used wisely (1993 National Performance Review Commission in US). But how is the level of regulations actually set? What forces drive this process? Two major theories try to explain how regulations are adopted: rent-seeking theory and state capture theory.

Rent-seeking theory argues that politicians use regulation to create opportunities to extract rents (bribes). They intentionally create inefficient and unclear rules only to generate rents for the public officials. They create excessive regulations that give more opportunities for corruption. In this context, private companies might pay to get a favorable interpretation of the rules (della Porta and Vannucci 1997; Varese 2000, Lambsdorff 2002).

State capture theory argues that firms shape the regulations through payments and favors to public officials. The problem of state capture is particularly prevalent when firms face insecure property rights and firms pay bribes to obtain certainty. According to this theory, firms that benefit from payoffs will resist efforts to improve the clarity of rules and laws (Hellman et al. 2000). They want to preserve the advantages that they have over the public officials and to extract benefits for their own interest.

This brief analysis raised some issues regarding how to design appropriate contracting out regulations. How much should this process be regulated? How does one prevent the interference of interest groups and of politicians in this process? How does one prevent corruption without hindering efficiency? To attempt to answer these questions we need to explain the mechanisms of contracting out and the corruption cases related to the process.

**Defining contracting-out process**

One area of public-private partnership is the privatization or contracting out of government services. In the U.S. the term "privatization" often refers to this contracting-out process. In Europe the term "privatization" usually refers to the selling of state-owned enterprises, which is not the subject of this paper. Therefore the term "privatization" will be avoided in this paper.

Examples include contracting out of such services as garbage and refuse collection, snow removal, merchant patrol, public housing, and parking. As we mentioned before, a wide variety of methods exist for inducing the private sector to provide public services, like management contracts, operating contracts, exclusive franchise and flexible franchise.

One approach is to utilize government employees and equipment, but to contract out management services. In the case of snow removal, for example, a management company may specialize in or have particular experience managing this kind of service. They may know best how to allocate human resources for particular sized storms, as an example, to minimize personnel costs.

The second approach, service contract, means to hire a company to take care of the job using its own equipment and employees. This might reduce costs for some of the same reasons mentioned above. Also, the private company might be able to acquire labor more cheaply since they are able

to access the labor market in a more flexible way than can a government. In both of these cases, the government would pay a private firm a fee specified in the contract.

Alternatively, in a service like garbage collection, a fee might be collectable from the citizen-customer at the point of the service. In some communities a bag that can hold a certain volume of garbage can be sold to residents, extracting a fee for removal of that amount. In a case such as this where a revenue stream can be generated, the government need not collect the fee. An exclusive franchise can be "sold" to a private company. This means a reputable company will be given the exclusive right to make the collections and also sell the bags. The exclusive franchise means that the private company would have no competition, but the price of the bag would be fixed. The company might have to pay the government a fixed franchise fee for the right to the franchise, or a percentage of the company's revenues. Also, the quality of service should be closely regulated by the government. If the company's service does not live up to expectations, the franchise could be withdrawn and given to another company.

A flexible franchise is where multiple companies might be given a franchise for the same area and allowed to compete. For something like garbage collection, two companies might be given overlapping areas. The price of the bag might be fixed, or set within a range, but residents could choose the company that provides the best service. If one of the companies provides poor service, they will be out of the business quickly.

As we mentioned in the introduction, this simple process of contracting out government services raises a multitude of issues. What type of bid is used to chose the company? Is the selection process objective? What companies have the right to bid? What is the quality of the work done? Who decides the specifications of the contract? Is the process of bidding transparent? How is the conflict of interest prevented? Who decides which companies are to be invited to bid? How are the selection criteria set? How does the municipality oversee quality and performance? Is the oversight process objective? What happens if low quality or non-compliance is detected? How does the municipality implement controls? Can people submit complaints? (Cobarzan and Hamlin 2005)

**Problems related to contracting out public services**

In this section we will analyze the opportunities for corruption related to the contracting-out process. We will show why it is important to answer the questions raised above, and probably many others. We will analyze these problems by referring to the phases of the contracting-out process.

During the initial phase of determining the need for a service to be contracted out, different methods favor one company over another. The public officials in charge of determining need can justify a level of service that is unnecessary or disproportionate to actual needs.

For example, public officials can justify the preference for expensive services when the community needs only the basics. According to Tanzi and Davoodi (1998), in countries facing extreme corruption, public officials prefer to undertake new infrastructure projects while the existing infrastructure is left to deteriorate. The public officials intentionally neglect "the operation and maintenance of the physical infrastructure, so that some infrastructure will need to be rebuilt" (Tanzi and Davoodi 1998, pg. 3). These projects mean more funds invested and allow corrupt officials to extract additional bribes from new investment projects.

The authors concluded that how public officials define the works or services to be contracted out is proportionally related to cost of the bribes that they can receive. They argue that the politicians and public officials tend to increase the size and the cost of the projects in order to receive a larger "commission" for helping a company to win a bid.

The public officials can commission unjustified studies. Jean-Pierre Bueb and Nicola Ehlermann-Cache (OECD 2005) explain how this mechanism works. The decision-makers can decide to contract out a study that will never be delivered, even though the money has been paid. Alternatively, they

contract out a study that could be done by the public institution but argue that internal results would be biased.

Before starting to negotiate a contract, one must define the type of bid to be used to negotiate the contract that is awarded. Among different types of bids, direct negotiation is subject to many corrupt opportunities. Decision-makers can be bribed to award a contract without organizing an open competition arguing the extreme urgency of the situation.

Defining when direct negotiation is acceptable and what type of contracts can be awarded without competitive bid is extremely important (TI 2000; Tina Søreide 2002). According to TI (2000, pg. 3), cases when direct negotiation is acceptable are: 1) during extreme urgency because of disasters, 2) where national security is at risk, 3) when additional needs arise during an existing contract, 4) when only a single supplier is in position to meet a particular need.

Setting the criteria for negotiating the contract can offer new corruption opportunities. Public officials can set pre-qualification criteria to limit the number of companies that are qualified to bid and or be included on a short list (Strombom 1998, Rose-Ackerman 1999). The inclusion on a short list may depend on bribes, instead of price, quality or experience.

Unnecessary requirements can be established to disqualify potential companies and favor the company that paid the bribe. The bid requirements can be designed in such a way that can be met only by the bribing company. For example, public officials might decide, arguing budgetary reasons, that the collection of garbage and the cleaning of the streets must be done by same company. But, only one company is able to provide both services, so this company is guaranteed to win the contract.

A contract can be deliberately under or over estimated. Underestimation is used to facilitate the initial awarding of the project. A company winning the contract will then add cost by justifying new events or conditions found after the contract is awarded (Tanzi and Davoodi 1998). The company decides to proceed in this way because the supplementary work is rarely negotiated. On the other hand, public services will be overestimated when the company is certain that it will receive the contract and the decision maker is certain that they will receive a percentage of the cost of the project. Even though the actual cost of delivering a service is lower, the company that wins the contract will return a part of the surplus money to the decision maker as a way of paying back for receiving the contract (Tanzi and Davoodi 1998).

A contract can contain excessive specifications. By imposing specifications that are much more rigorous than general standards, the public officials can create new opportunities for asking for bribes. The excessive specifications can be negotiated and overlooked if the company pays the bribe. Or, the contract can be negotiated on the terms set by the public institution, but the maintenance is latter carried out under conditions imposed by the supplier. The maintenance services can be performed at a higher cost than other companies would perform.

The public officials can be bribed to ignore work that is left out of the promised project activities yet is necessary for the successful implementation of the project. In this way, after the contract is awarded, the company that paid the bribe can renegotiate the contract. Those officials who define what is counted as supplementary work may be corrupted.

Advertising a contract can be done in many ways. The process of notifying potential bidders offers a good opportunity for public officials to limit the companies invited to bid and therefore to advantage the company that paid a bribe. The institution can invite all the qualified companies to bid for the contract or decide to invite only the pre-qualified bidders. But in the case of pre-qualified bids, who decides to which companies to send the invitation?

The tender invitation can be sent to companies with a completely different area of specialization or without any experience in the relevant field. In this case, the public institution can claim that

bidding was organized and a large number of companies were invited. Yet, companies invited were not real competitors and only the company paying the bribe meets the pre-qualification requirements to negotiate the contract.

Even if rules require the announcement of the contract to be made public, the public officials may decide to keep the process secret from the public as long as possible. In this way, they can control which companies actually tender by providing friends with advanced warning. Usually these companies are those that the public officials want to pay back a previous service or those companies that have the reputation for being willing to pay bribes.

If the regulations give only general recommendations that the contract should be advertise, public officials can decide to make just a minimum effort to advertise it. The notification of bidding opportunities can be made in the smallest, most obscure circulation source that satisfies the advertising requirements (Søreide 2002). Reduced publicity can be falsely justified claiming that the urgency of the situation required a shorter advertising period (Bueb and Ehlermann-Cache 2005).

Public officials might even decide to eliminate publicity entirely by using as justification legal grounds such as "state secrecy, exclusive rights, research or experimental work or additional supplies" (Bueb and Ehlermann-Cache 2005, pp. 165).

Offering accurate information about the contract is a basic and simple requirement for the public institution. But by offering intentionally incomplete and inaccurate information to all the companies interested in the contract, one can argue that it was just a mistake. Then, the favored firm is quietly told about incomplete or inaccurate information. In this way the company can discount the inaccurate condition in its proposal and win the contract by making a bid that is lower or better than other bids (Bueb and Ehlermann-Cache 2005, pp. 164).

Providing confidential information can rig the decision-making procedure or other decisions influencing the process (Rose-Ackerman 1999). When a company knows in advance the criteria that are important for evaluating a contract, it can obtain the contract formally without any irregularity. According to Donatella della Porta and Alberto Vanucci (1999), the value of confidential information is inversely proportional to the number of people who posses it.

This method is the easiest way to steer a contract to a "friendly bidder", and it is the most difficult to demonstrate that corruption took place. Information that a preferred company can obtain, might be related to aspects of the contracting process that are important to remain secret in order to ensure fair competition, such as: minimum and maximum pre-qualified bid price or the price that competing companies bid, or which criteria are the most important for evaluating the projects (della Porta and Vannucci 1997).

During the phase of proposal evaluation, different methods can be used to make sure that the favored company wins the contract. The selection criteria can put more weight on one criteria met by only one company. Members of the awarding commission might revise the criteria after the bids are opened. They can create or modify weightings allocated to each criterion or they can add further criteria. In this way, they can favor the company that bribed the commission. For example, when it seems obvious that several competitors had a better offer, the commission may change the evaluation criteria by arguing the extreme importance of one particular evaluation element met only by the bribing company.

When only one of the pre-qualified companies has bribed the tender board, and the other companies have better bids, justification of the awarding contract may be difficult. In this situation, the evaluation commission can use ethical or political reasons (such as trade with countries or groups in conflict with the government) to disqualify the unwanted companies. Also, the bid may be delayed or recalled on grounds of changed priorities, shortage of finance or a larger/smaller scope of work.

Most serious and costly forms of corruption may take place after the contracts has been awarded. As we mentioned before, the company may pay a bribe to get supplementary funds for work that was not included in the contract specifications and for under evaluation of the project costs. Also, the company may pay a bribe to contract supervisors to induce them to overlook the quality of the work done or the services delivered (Tanzi and Davoodi 1998). The contractor may falsify the quantities and the quality of the services. Also, the company can pay bribes to get a time extension for the implementation of the program (della Porta and Vannucci 1999, Rose-Ackerman 1999).

"Winners" have every intention of recovering their bribing cost. The methods they can use are to inflate their bid price, to reduce the quality of materials used for construction or to deliver poor quality services (Strombom 1998). With respect to contracted-out services, an example might be to promise in the proposal to maintain a customer service office for citizens complaints and support, but after the contract is secured, open the office for very few hours per week.

**Causes and the consequences of corruption related to contracting out public services**

Why does corruption take place in contracting out public services? What mechanisms support corrupt behavior? What are the consequences for communities? We do not attempt to give comprehensive answers to these questions, but merely to bring a better understanding of the phenomenon.

Sometimes, it seems that public officials select projects and make decisions regarding contracting out services with little or no economic rationale and the argument that they give does not resemble the general public interest. The question that this scenario raises is why do they behave in this way? Did they pursue other private interests?

Many researchers tried to explain why companies pay bribes to win a contract for delivering a public service or for performing a public work. One of the reasons private companies most often suggest is that they want to be sure that their company obtains the contract. Preparing for a bid is costly and time consuming. In countries with high levels of corruption, the firm may not trust its chances of winning the contract only on a legal basis. Therefore, the bribe becomes necessary to justify the large and constant cost of bid preparation. (Søreide 2004).

In 2004 Tina Søreide performed a study on 82 Norwegian private companies regarding the corruption in international business transactions. The respondents were asked to suggest the motivation behind bribery. The rationale that was most often suggested for giving bribes was the fear of losing contracts because someone else has bribed the decision-makers. The same study showed that 31% of companies that have anti-corruption codes of conduct say that they would adjust their strategies to the local business culture if they were losing contracts because of corruption. In some countries, it is apparently impossible to win a government contract without first paying a bribe (Søreide 2002; Tanzi and Davoodi 1998).

Other authors (Tanzi and Davoodi 1998) explain that the private companies are willing to bribe politicians because the projects that they can obtain to execute can be very profitable. Usually public works, like building roads, public buildings or damns have a big budget. A private company is even more willing to bribe public officials if it can secure the monopoly over delivering a service.

Many times it is important how politicians define the public interest that they want to achieve through a project. Private companies can bribe politicians to define the public interest in the way they want. Sometimes, they can intentionally present facts to justify projects that they want to implement and that are not necessarily justified by people's needs. Public services can be contracted out at a price lower than the market price. Public officials can argue that it was in the interest of a minority group that otherwise wouldn't have access to that service. Or, they can create the demand for a new service or work that otherwise would not have been purchased.

Having stricter regulations does not limit corruption. Della Porta and Vannucci (1999) analyzed how, in Italy, in the context of strict regulations, bureaucrats create new opportunities to extract

bribes from private companies. These authors explain that even though they have limited capacity of initiative, bureaucrats still hold a strong veto power, which enables them to delay processes or to make omissions in resolving requests. The bureaucrats can refuge themselves in legalism and delay the request for an approval as much as is legally possible. In this context, the companies will be willing to pay bribes proportional to the time saved.

The companies can pay bribe for other reasons such as: to reduce political risk, to attain special modification of laws, to obtain financial incentives (like tax reductions), to obtain secret information about a bid, to directly negotiate a contract, to define the evaluation criteria of a bid, to counterbalance poor quality of a service or work or the high price, to name a few. In cases of endemic corruption, the firms can just pay bribe to induce government employees to perform their jobs.

The bribe does not always involve money. It can be in the form of other resources, which have particular value for the corrupt politicians. When offering a bribe, the firm that wins is the one offering the higher utility to the government official. The public officials want to achieve public sector welfare and in this way to gain the public support in order to survive politically. But at the same time, they may wish to obtain personal benefit from contracting out a public service. The successful firm is the one that offers the preferred combination between price and quality and the higher utility for the public official (Søreide 2002). The personal benefit for politicians can take such forms as money, personal relations, publicity, vacations, and tuition fees for children.

The main premise of involving the private sector in delivering services is that competition among potential contractors will drive down the cost of production and ensure that the service will be of high quality. But corruption can make the benefits of contracting out illusory. It can lead to decrease in government revenues, increase in public investments, deterioration of infrastructure, and poor quality of services delivered.

One of the most severe consequences of corruption is that it is associated with low government revenues. Tanzi and Davoodi (1998) argue that corruption can reduce government revenues by creating many loopholes for tax exemptions. According to Strombom (1998), where corruption is systemic, it probably adds at least 20 to 25% to the costs of government procurement. Bardhan (1997), Bjorvatn and Søreide (2005) argue that the acquisition price is likely to be higher when government official are highly corrupt.

When corruption plays a role in the selection of a project, public officials will be more willing to contract out investment contracts in infrastructure and will intentionally let the existing public infrastructure to deteriorate. High spending on investment projects will reduce the resources available to other projects. Corruption can severely affect the quality of the work done. Some projects of public infrastructure can be built but never used. Others projects are so poorly built that they need continuous repair (Tanzi and Davoodi 1998). Public inspectors can be bribed to overlook the poor quality of the work or of the service delivered. But, by overlooking the poor quality of the public works, life of the people can be put in danger. Just think what happens if public housing does not respect safety measures.

Corruption can lead to more market concentration. If a firm bribes the public officials to acquire a monopoly over delivering a service, then other potential competitors are shut out of the market and may eventually die off. Ultimately, only the people that collect the bribes change (Bardhan 1997). If only one firm in the area is capable of providing the service, then contracting out may no longer be a good idea. Competition stimulates improvements in the quality of the services delivered. But if the competition between contractors is weak, or existing companies engage in collusion, then the benefits of competition cannot be achieved.

**Recent discussions regarding how to design the regulations related to contracting out services to private sector**

In the last few years at international meetings, researchers and professionals have started to talk more about new strategies of preventing and combating corruption in procurement and contracting out. The new approach is formulated as a possible solution to the question of how to limit the opportunities for corrupt practices. This old question didn't receive yet a response, and different solutions have been formulated having a limited applicability to a different cultural context.

This new approach tries to give an answer to two questions concerning anticorruption strategies. One open issue is whether we should assume that public officials would apply the law impartially if the environment were right, or should we assume that personal interests would always affect some decisions? The other one is whether we should develop rules for every kind of situation that may arise or should we pay attention to objectives of each single process.

These questions emphasize the new discussions that challenge the effectiveness of adopting new layers of regulations in eliminating corruption. As we mentioned in the introduction, the economic development challenges that the local government confronts, ask for flexibility and innovation in establishing public-private partnerships. In this context, the new trend in this field calls for designing safeguard measures that emphasize the aims of contracting-out processes that do not hinder the efficiency of the procedures (Peter Trepte in OECD 2004).

This idea was formulated as one of the findings of the Global Forum Conference on "Fighting Corruption and Promoting Integrity in Public Procurement" organized by OECD and hosted by the French Ministry of Economy, Finance and Industry[1]. The participants at the conference agreed that "additional regulations do not necessarily prevent corruption" because they can easily be bypassed. The recommendation that was formulated was to emphasis the training of the public officials responsible for the procurement process.

In 2004, the European Commission adopted the Green Paper[2] that created a forum of debate about the need to clarify, complement or improve the current legal framework regarding procurement laws and how they apply to the different forms of public-private partnerships developing in the Member States. The main idea that guided the discussions and resulted from the recommendations that were formulated was the need to provide the general guidelines to ensure competition for public-private partnerships without limiting the flexibility needed to design innovative and complex projects[3].

The limiting effect that the procurement regulations have on preventing corruption is supported by results of the research conducted in 2004 among 82 private firms with headquarters in Norway (Søreide 2004). Among other objectives, the research explored also the efficiency of procurement rules in preventing corruption. It was assumed that the presence of procurement regulations would reduce the opportunity for awarding the contracts on corrupt criteria. The results showed that 55% of the respondents believed that public procurement regulations did not prevent corruption. Only 6% of the respondents considered the rules to be efficient in preventing corruption. Based on these results, the author concluded that corruption "takes place independently of such procedures" (Søreide 2004).

[1] The conference took place on 29 and 30 November 2004 in Paris. Participants at the conference were from the public and private sector, nongovernmental organizations, academic institutions, international organizations and trade unions.

[2] Livre Vert sur les Partenariats Public-Prive et le Droit Communautaire des Marches Publics et des Concessions, COM(2004) 327 final, Bruxelles, 30.4.2004

[3] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee of the Regions on Public-Private Partnerships and Community Law on Public Procurement and Concessions, COM(2005) 569 final, Bruxelles, 15.11.2005, pag. 4

**Strategies for safeguarding contracting-out processes**

These recent discussions call for a new design of the regulations that give flexibility to public officials in contracting out public services and, at the same time, safeguard against corruption. Good regulations are not sufficient conditions for efficiency, because laws might not be enforced or the participants might not act according to economic rationality. On the other side, it is not enough to have lax regulations and to presume the honesty of the public officials. We can adopt this strategy, but it will not lead to overall efficiency. Beside flexible regulations, we need to verify whether the general regulations are being met. The accountability of the public officials and the transparency of the procedures are two critical measures that an anticorruption strategy should emphasize. Tina Søreide (2002) calls for a stronger emphasis on the execution part of the anti-corruption laws, and less on the designing process. In her opinion, it is critical that the implementation of these measures be guided by accountability and integrity rules. Another critical element of the strategy should be to train public official to identify and manage the risks of corruption.

A strategy that safeguards against corruption should perform four functions: to define, to expose, to correct and to prevent (Witting 2005). To define the rules, to expose the contracting-out process and project implementation to strict scrutiny, to correct the deviations from the rule implementation and to prevent possible corrupt practices.

**Define the rules**. The rules safeguarding against possible corruption opportunities are not always included in a law applying specifically to the contracting-out process. But these rules are found in laws such as criminal law, public procurement law, government regulations and professional codes of ethics. Also, in some cases, customs and previous practices play an important role. The majority of the authors argue for the simplification of the rules. As we stated before, the greater the number of regulations affecting contracting-out processes, the more opportunities exist to use these regulations to manipulate information.

Rules should require the transparency of procedures, by making public all the information pertaining to the bid and then implementation of the contract. These rules should define exactly when the terms of the contract could be altered by negotiations between the winner and the public institution, after the contract was awarded. Otherwise, vague rules will lead to contracting something different from what was tendered. Another issue that the regulations should address is when direct negotiation can be used and what rules are applied in negotiating the contract.

The safeguard measures must be reviewed continuously because companies seek new ways to bypass the regulations in order to win contracts. Regulations should evolve in order to catch up with the evolving techniques that actors develop to maximize their expectations (Witting 2005).

To encourage the most competitive and able suppliers to bid, procedures must be fair, non-discriminatory, transparent and credible. The regulations should provide the incentives to encourage competition among companies.

**Expose to strict scrutiny.** The main mechanisms to expose the contracting-out process are through internal and external audits, whistle blowers, transparency of rules and procedures, disclosure of the financial interests and mechanism for protesting contract award. The mechanisms of control and audit should be independent from any influences. They are used to monitor whether the company respected the requirements included in the contract, and whether the service delivered met the quality requirements.

Whistle blowers should be encouraged to disclose information about unethical or corrupt practices regarding the decision-making process and contract implementation. The disclosed information should be checked first. If corrupt or unethical practices are found, appropriate measures should be taken. It is important to build confidence in this system by ensuring the confidentiality of the whistle

blowers and by taking appropriate measures to correct the deviations from the rules. If people feel that their effort and the risk that they took had a contribution to reveling corrupt practices, they will be encouraged to report other cases. At the same time, public officials will pay more attention to how they make the decisions and supervise the implementation of a contract.

One of the most important measures is to ensure the transparency of the process, because corruption is most likely to occur in situation where public officials are at a low level of accountability. Transparency requires the release of sufficient information to allow the average participant to know how the system is intended to work as well as how it is actually functioning (Bertók 2005, pp. 86).

The contracting-out opportunities should be made accessible to a wide range of potential suppliers. Private companies should receive the information that they need for bidding at the right time and in the right form. The announcement of the bid should clearly describe the service or the work to be contracted out. So that changes that were not previously specified in the contract may not occur. The decision-making process should be explicitly stated in the announcement and should be based exclusively on objectively measurable factors.

Transparency and accountability can be achieved when the relevant stakeholders are actively engaged in the course of the contracting-out process (Bertók 2005, pp.88). Citizens should have the opportunity to follow the contracting-out process. Transparency requires the release of information on successful bids and, equal important, informing the unsuccessful bidders about the reasons why they were not selected.

Disclosure of financial interests means that the public officials involved in the decision-making process should declare any private interests that might affect their decision with regard to contracting out a public service. Some large public institutions established additional layers of supervision and control to prevent conflict of interest of public officials. For example, New York created a Conflict of Interest Board that requires divulging personal finances of the contracting personnel and the Department of Investigation investigate city employees' declarations (Blendermann et al. 2004).

Also, before the contract is negotiated with the bidding companies, it is important to obtain information about the performance of the company under past contracts. Some cities created additional procedures for checking the companies that apply for a contract. New York City created a vendor database that includes information such as past violations, indictments and convictions. Also, the Department of Investigation checks if a contractor is eligible for a city contract.

The regulations should guarantee the bidding companies and the public the right to administratively contest the decisions. If they are not satisfied with the answer they received, the regulations should offer them the right to judicially contest the decisions.

**Correct the deviations from rules.** The non-performance of the contracts should be penalized. If no penalties exist, or if the penalties are not applied, the opportunistic companies will maximize profits by executing only the easiest part of a contract. Punishments and controls are the factors exerting the strongest effect on implementation of the rules. Or better stated, the fear of punishment plays a key role in inducing the private companies and the public officials to respect the rules. A key condition is to build people's confidence that the rules are respected.

**Prevent further corruption cases**. The recent call in this field is for strategies that emphasize the training of the public officials responsible for the contracting-out process. Some authors (Beth and Trepte in OECD 2004) argue that these public officials should be provided with appropriate skills, professional capacity and incentives to identify and manage risks of corruption.

Enhance the professional independence of public officials and protect them from the influence of politicians. Some countries took a proactive approach regarding this problem by asking public officials responsible for procurement or contracting out to go through special training sessions at

regular intervals of time. In the U.S., some public institutions even created institutions responsible only for training in this field (Blendermann et. all 2004).

Strong rules should set what is acceptable and what is unacceptable. They can help safeguard the independence from political influence and other private interests. Knowing that the government is strictly enforcing the rules can help discourage any request for favoritism.

**Future research agenda**

As described in this paper, public-private mechanisms of governmental management have been popular in nearly every part of the world, and are expanding rapidly in Europe. The contracting-out of government services to private companies is one common form of public-private partnerships. While some forms of public-private partnership promote citizen participation and responsiveness to citizen-customers, greater involvement of the private sector in governmental service delivery makes transparency more complicated and challenging. It sometimes leaves a door open for unethical behavior and corrupt practices. The political response to resolve corruption problems is often to add more levels of oversight and regulatory compliance. This sometimes destroys some of the efficiency and flexibility of a public-private partnership system and may even add to opportunities for public officials to extract rent. Therefore, finding the right balance between regulatory oversight, decision-making flexibility and reliance on market forces is very important for the future of public administrations. And, this balance may vary among different cultural milieu. Little research effort is currently focused on these issue related to the contracting out of public services. A research agenda is needed to answer the questions suggested in this paper.

A first step in this research agenda will be to develop a complete list of the points in the public-private partnership process where corruption might creep into the system. This paper has tried to describe the contracting-out process and to list some of points of corruption vulnerability. A second step in the research agenda will be to investigate how different communities and states attempt to control corrupt practices at each of these vulnerable public-private partnership decision points. This investigation should be extended internationally so as to see how methods of corruption mitigation compare across cultures. In one society small but blatant bribes or "tips" might be a common practice, while a second culture might be dealing with more sophisticated, larger, in-kind favor trading. In a third society the more common practice might be collusion such as price fixing and bid rigging rather than bribing. A third level of this research will be to develop indicators and metric techniques that measure the effect on efficiency and effectiveness of various corruption control mechanisms in various societies using a combination of cross-national surveys and case studies.

The ultimate goal of this research is to guide publics toward the most effective mechanisms for mitigating corruption while allowing democratic societies to reap the benefits of new entrepreneurial approaches where the walls between the public and private sectors are breaking down.

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