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Contracting and Outsourcing in Public Sector in the Czech Republic

Beata Mikušová Meričková

Matej Bel University, Faculty of Economics, Slovakia

Marketa Šumpíková

College of Regional Development and Banking Institute – AMBIS, a.s., Czech Republic

Nikoleta Jakuš Muthová

Matej Bel University, Faculty of Economics, Slovakia

Juraj Nemec

Masaryk University, Faculty of Economics and Administration, Czech Republic

Abstract

The study builds on the original research of contracting and outsourcing in the Czech public sector and assesses them from a comprehensive perspective. The aim of this study is to contribute to the recent discussion about contracting/outsourcing in public sector and its results. The research goal is to analyse the results of contracting and outsourcing in the Czech Republic. Following research questions are set: "Does contracting/outsourcing in public sector in the Czech Republic bring efficiency gains?" and "If not, why contracting/outsourcing services in the public sector in the Czech Republic does not bring efficiency gains?". To answer the research questions two alternatives of services provision, namely internalisation and contracting, were evaluated. The three criteria, 1) expenditure on the provision of the service per citizen/employee, 2) the expenditure per performance indicator and 3) the quality of services evaluated on the basis of citizen/employee satisfaction as consumers of services were used in evaluation. To evaluate the efficiency of contracting services in the public sector was used the method of multi-criteria evaluation for selected samples - the method of the best values of criteria. It is not possible to come to the final conclusion about higher efficiency of internal versus external production. However, what can be clearly and un-doubtfully documented is the fact that depending on the concrete case the more efficient solutions differ. The core factor of the limited success of contracting and outsourcing is the quality of contract management, which represents critical problem in the Czech Republic.

Keywords

Contracting, Outsourcing, Public Service, Contract Management, Czech Republic

JEL Classification

H41, H57

Introduction

Contracting public services and outsourcing internal services in public organisations represent the most commonly used alternative service delivery arrangements in the public sector. Under this arrangement, the state is responsible for the service delivery, but the production is transferred to private bodies. This approach was promoted especially by the New Public Management (NPM) ideology (Pollitt and Bouckaert, 2011), which suggested that contracting should contribute to increasing the efficiency of service delivery because of competition. The importance of contracting/outsourcing (externalisation) grew significantly especially after 1990.

Compared to the expectations related to the NPM ideology, contemporary literature is increasingly less positive regarding the impact of externalisation on efficiency and quality of public services. Recently published books speak about the need (and trend) of "remunicipalisation" or "public ownerships" especially in relation to contracting. The edited volume by Kopric et al (2017, 335) concludes that "The ideological belief that NPM-related mechanisms such as contracting out, outsourcing, public–private partnership, privatisation, and others will bring about better solutions for users may or may not be supported by firm data on efficiency and user satisfaction. It depends on the type of service, municipality size, national legal and institutional contexts, the level and nature of competition in

Corresponding author:
Juraj Nemec, Masaryk University, Faculty of Economics and Administration, Department of Public Economics, Lipová 41a, 602 00 Brno-Pisárky, Czech Republic
Email: juraj.nemec@econ.muni.cz

particular local service sectors, local regulatory and managerial capacities, and other variables. Furthermore, contrary to ideological beliefs, the privatisation and implementation of NPM-driven arrangements may result in price increases, disinvestment, and other significant detrimental long-term effects, whether those are the consequences of model inappropriateness, regulatory deficiencies, or implementation inconsistencies“. Kishimoto et al (2020, 230) argue that “(Re)municipalisation is one of the key strategies to address the challenges of our time, including pandemics such as Covid-19“. This book identifies more than 1,400 successful cases of (re)municipalisation, involving more than 2,400 cities in 58 countries around the world.

In the past, the majority of academic studies focused on the issue of contracting/outsourcing (we will use the term contracting for both alternatives in most parts of this text) by comparing the cost-effectiveness between internalisation and contracted services, perceived simply from the perspective of the principal-agent theory. Such a perception of the problem is limited to solving the issue of "make or buy" - i.e. whether to provide the service with its own capacities or to contract it. The up-to-date world economic theory and practice no longer focuses on the question whether to contract public sector services or not, but on the question which factors should be evaluated and how to manage the contracting process with the gradual change of competitive relationship between the principal and agent (contracting authority and supplier) in a partnership. The aim of this study is to contribute to this recent discussion about contracting/outsourcing in public sector and its results. The study builds on the comprehensive set of data, collected especially by the original research of authors in the Czech Republic, and its goal is to assess contracting of public services in the Czech Republic from a comprehensive perspective.

The research goal is to analyse the results of contracting and outsourcing in the Czech Republic and to define the core determinants of these results. Building on the content and causal analysis of knowledge and the historical chronology of development in the researched issue, we want to answer – for the Czech conditions – the following questions:

- Does contracting/outsourcing in public sector in the Czech Republic bring efficiency gains?
- If not, why contracting/outsourcing services in the public sector in the Czech Republic do not bring efficiency gains?

The flow of the text is as follows. In the first part, the processing of the theoretical backgrounds of the study should answer the question: when and why contracting/outsourcing (authors will use only expression “contracting” in the following text, where appropriate) services in the public sector should bring efficiency gains. The question is answered through the content and causal analysis of the knowledge gained via the secondary collection of information and the historical chronology of the evolution in the subject matter, the method of abstraction, approximation in the theoretical analysis of the knowledge and the results of previous studies in this field. Theoretically, contracting out should increase the efficiency of public service provision (by eradicating the public production monopoly), provided that the risks associated with contracting are minimised (moral hazard and the hidden information problem). However, the effective management of the contracting process is a precondition for minimising contracting risks.

The analytical part of the study processes primary data collected by our own research, with the aim to provide evidence for answering the defined research questions - whether contracting services in the public sector in the conditions of the Czech Republic bring efficiency gains and if not, why. The synthesis part discusses the results and formulates policy lessons.

Theoretical background

The study responds to the matter of externalisation of the production of services in the public sector. Contracting of public service production is based on a contractual relationship - a contract between a public institution and an external entity (Cooper, 2003; Kettner and Martin, 1990; MacNeil, 1978; Rehfuss, 1989). Worldwide, the problem of contracting public sector services has roused the curiosity of both the expert and non-expert public for three decades (Savas, 1987; Osborne and Gaebler, 1993; Kettl, 1993) due to the fact that the government of each country spends a significant quantity of public funds to finance contracted services every year, and the importance of contracting continues to grow (Kettl, 1993; Donahue, 2002; Martin, 1999; Brudney, et al., 2005; Miranda and Andersen, 1994).

The first studies related to contracting concentrated on the problem of comparing the cost-effectiveness of internalisation and contracting services perceived from different perspectives (Brudney, et al., 2005; Greene, 2002 and many others). The authors attempted to investigate if, and to what extent, there are differences in performance (primarily economic performance) between the public and private production of local services. Before 2000, Domberger and Jensen (1997), for example, showed that private production of local services led to efficient provision for a number of government services. However, the more recent evidence of the cost efficiency of private delivery (including waste collection and disposal) is rather ambiguous and more mixed (for example Bel and Costas, 2006).

Currently, in terms of contracting services in the public sector, the world economic theory no longer solves the question of whether to contract, but how to manage the contracting process. Despite a number of scientific studies

on the subject, it is problematic to obtain an answer to this question mainly for the reason that many, especially older, foreign studies concentrate on the problem of comparing the cost-effectiveness of internalisation and contracting out services simply perceived from the perspective of the principal-agent theory (Brudney, et al., 2005; Greene, 2002; Dilger, Moffett, and Struyk, 1997; Hodge, 2000; Kamerman and Kahn, 1989; Savas, 1987; Sclar, 2000; Siegel, 1999).

This simplified perception of the problem of contracting out services in the public sector is limited in only addressing the issue of "make or buy", which does not answer the question: Why contracting services in the public sector do not increase efficiency? To solve the question of the controversial effects of contracting services in the public sector to ensure their effectiveness is possible by shifting the subject of the problem investigation from the level of cost-effectiveness of contracting to the level of those factors determining efficiency of contracting, including the issue of process control.

The current research assumes that one of the critical contracting effect factors is the quality of the contractual relationship management between the principal (the contracting authority) and agent (supplier). Both the principal and the agent pursue their own aims, which may or may not be consistent with each other (DeHoog, 1990; Sclar, 2000; MacNeil, 1974, 1978; Maceják, Šebo, 2008). The discrepancy between the principal's (service provider / contracting authority) and agent's (service producer/supplier) aims is the source of two basic contracting problems: 1) moral hazard or problem of hidden activity, and 2) incorrect selection or problem of hidden information (Arrow, 1985; Kettl, 1993; More, 1984; Pratt, Zeckhauser, 1986). The result or the success of contracting depends on the extent to which the mentioned problems or risks are minimised.

Several authors mention the contributing factors of contracting and services in the public sector based on the quality of contracting process management: the level of competition in obtaining a public contract – it could be evaluated according to the public procurement procedure used (Savas, 1987; Kettl, 1993; Greene, 2002) Hodge, 2000), ex-ante evaluation of the tenderer (Rehfuss, 1989; Marlin, 1984; Romzek and Johnston, 2002), clearly defined subject of the procurement (Rehfuss, 1989, Wasemann, 1981; Marlin, 1984), the extent and intensity of external production (Rehfuss, 1989; Marlin, 1984; Prager, 1994; Lavery, 1999; Seidenstat, 1999; Brown and Potoski, 2003; Hefetz and Warner, 2004), penalties for non-compliance (DeHoog, 1990; MacNeil, 1974, 1978), the contracting authority's knowledge and experience in contract management (DeHoog, 1990; Rehfuss, 1989; Romzek and Johnston, 2002), and the contracting authority's expertise on the technical parameters of the contract service (Kettl, 1993).

With the exception of the conventional perception of contracting in terms of the principal-agent theory where the service provider, in the relationship between the provider, service provider, and producer, is perceived as manager or controller (considering the diversity of the stakeholders' aims and their efforts to enforce them), there also exists a newer interpretation perceived in the scientific literature (DeHoog, 1990); Williamson, 1986; Sclar; 2000; Smith, 1996; Kettner and Martin, 1996; Bennett and Ferlie, 1996) that understands this relationship as a partnership created on flexible collaboration. Additional factors appear to be the determinants of contracting benefits: frequency of communication between the service provider and producer (Behn and Kant, 1999, DeHoog, 1990), common problem solving (Cooper, 2003; Sclar, 2000), mutual trust, shared values, change from sanctions to negotiation (MacNeil, 1978, 1974).

The issue of contracting of local public services has been the object of systematic research in the Czech Republic for the last twenty years. In addition to papers (like Ochrana et al, 2008; Páleniková, 2012; Rousek et al., 2009) and books (Ochrana et al., 2007 and Meričková et al., 2010) prepared or co-authored by the authors of this article, there are several other interesting publications analysing contracting of local public services in the conditions of the Czech Republic. We should mention especially the analysis by Pavel (2006), documenting the limited transparency and inefficiency of local companies responsible for the delivery of local services. The Czech contracting research focuses especially on the area of waste management – Soukopová and Klimovský (2016), Soukopová et al (2017), Hrebicek and Soukopová (2010).

Methods

The research starts with the standard procedure used by international studies to evaluate the effectiveness of contracting - by comparing the cost of contracting and the internalisation of services. This procedure is considered to be limited by many factors (see the discussion part of this paper), however, we try to improve the methodology for assessing the efficiency of contracting services in the public sector by considering another cost-effectiveness indicator, namely expenditure on the performance indicator and also by considering the quality of services assessed by the level of satisfaction of consumers in the last phase. This approach results in the use of multi-criteria efficiency evaluation using the method of the best value criteria (input and output indicators) whose application in the field is innovative in an international context and unique in the national context of knowledge. The method of best values of criteria used (Engelbeck, 2004; Epstein, 1984; Shetterly, 2010; Fiala et al., 1994) is easily applicable to the conditions of evaluation of public sector services and is a typical weighted sum algorithm. Through the evaluation of the set criteria, we can determine the most efficient alternative for providing a specific form of service among all those monitored, and we can also determine the order of individual alternatives according to the degree of efficiency. The

ability of the evaluation process depends mainly on the suitability and scope of the set of selected evaluation criteria and the method of their quantification through individual indicators. In our research, we chose three criteria. The first criterion is the expenditure on the provision of the service per employee (indicator A), the second criterion is the expenditure per performance indicator (indicator B) and the third criterion is the quality of services evaluated on the basis of employee satisfaction as consumers of services (indicator C).

In the article, we evaluate two alternatives for the provision of services, namely internalisation and contracting on the basis of the three criteria, indicators. We normalise the achieved values with respect to different units of expression of indicators. We multiply the normalised values by the weights determined for the individual criteria according to the Saaty method (Saaty et al., 1983), as shown in Table 1.

Table 1. Saaty matrix and calculation of weights of multicriteria evaluation criteria.

Criteria	K1	K2	K3	s_i	Ri	v_i (weight of the i-th criteria)	weight of the i-th criteria in %
Expenditure on providing the service per employee K1	1	1	1/3	1/3	0.693361	0.3	30
Expenditure on providing the service per employee per performance indicator K2	1	1	1/3	1/3	0.693361	0.3	30
The degree of employee satisfaction with the quality of service K3	3	1/3	1	1	1.000000	0.4	40
∑					2.386723	1	100

Source: Authors´own

A more efficient alternative to providing the service is that which achieves a higher value within the evaluation.

The core issue is the question of why the efficiency of contracting services in the Czech public sector delivers limited results. From numerous possible factors, we decided (based on already existing knowledge – for instance Soukopová and Klimovsky, 2016) to test the significance of the impact of contracting efficiency factors.

We measure the quality of contracting process management using all the relevant sub-factors, using our own methodology of quality assessment contract management affecting the risks and thus the actual outcome of the contracting. The relationship between the risks of contracting and the monitored factors arising from the quality of management of the contracting process is shown in Table 2.

Table 2. Factors of the resulting effect of contracting public sector services in relation to contracting risks.

	Contracting risk		
	Lack of transparency	Hidden information	Hidden activity
FACTOR based on the quality of contract management	the degree of competition in obtaining a public contract	ex-ante evaluation of the bidder	frequency of service production monitoring
	clear subject of procurement	expertise of public service employees in the technical parameters of the service	procedure for non-compliance with contractual obligations length of contract the type of payment to the external supplier for the service

Source: Authors´own

Table 3. Quantification of the factors resulting from the contracting effect of public sector services in relation to contracting risks.

Risk	Factor	Qualitative character	Quantification
Lack of transparency	the degree of competition in obtaining a public contract	open tender	100
		restricted procedure	70
		negotiated procedure	50
		price offer	30
		direct award	0
	the contract stipulates the clear subject-matter of the contract	I fully agree	100
		I agree	50
		I disagree	0
		I strongly disagree	0
	ex-ante evaluation of the tenderer	the most economically advantageous tender	100
		the lowest price	50
Hidden information	the employees of the municipality who provide the contracting process have sufficient professional knowledge of the technical parameters of the service provided	I duly agree	100
		I agree	50
		I disagree	0
		I strongly disagree	0
Risk of hidden	frequency of monitoring the production	regularly	100

Risk	Factor	Qualitative character	Quantification
activity	of the contracted service (how often the service is controlled by the municipality)	continuously as needed	50
		without monitoring	0
	procedure of the municipality in the event of failure to comply with contractual obligations	revocation and termination of the contract	100
		financial penalties	70
		requesting remedy	30
		other procedures	0
	the duration of the contract	up to 1 year (inclusive)	100
		up to 2 years (inclusive)	70
		up to 5 years (inclusive)	30
		an unlimited time	0
	the method of payment to the external contractor for the service	payment for performance	100
		fixed payment + performance, i.e. combination	50
		fixed payment	0

Source: Authors´own

The higher the score achieved by the contract under consideration, the more effective the implementation of contract management with a positive influence on the elimination of contracting risks and therefore on the efficiency of contracting can be expected. For our analysis we use data from the samples shown in Table 4.

Table 4. Research of contracting services in the public sector in the conditions of the Czech Republic.

Period of implementation of own primary research	The research sample	
	Contracting local public services	Contracting of ancillary services in public service organisations
2000	53 municipalities of different size groups	
2001		19 organisations providing public services
2005 /TIS	100 municipalities of different size groups, data for 2004	
2007	900 municipalities of various size groups, data for 2005	
2009		162 municipal authorities
2010	673 municipalities of various size groups	
2011		98 organisations providing public services
2012		42 organisations providing public services
2014a	102 municipalities of various size groups	102 municipal authorities
2014b	1,300 municipalities of various size groups	
2015a	675 municipalities of various size groups	
2015b	1962 municipalities of various size groups	
2018-2019	90 municipalities of various size groups (waste collection), 68 municipalities of various size groups (maintenance of lighting, care of the appearance of the village and public greenery, cemetery administration and maintenance, maintenance of local roads)	41 municipalities of various size categories from the selected region

Source: Own research + research of Pavel, J., 2006; Páleníková, M., Mikušová Meričková, B., 2012, Soukopová et al., 2017, Soukopová and Klimovský, 2016

We are aware that several data problems limit the chance for exact comparisons. One problem is the fact that because of the existing accounting system the costs with contracting/outsourcing must be higher. Municipalities do not monitor overheads and the transaction costs connected for example with public procurement or subsequent monitoring of external delivery. However, the invoiced costs from external subjects include direct costs, overheads (including most transaction costs), value added and in most cases also profit. Another problem is the limited reliability of data collected. In the beginning the cost data were collected by questionnaires – not all data inserted must be really correct. More recent economic data for the Czech Republic are collected from the national information system (ARIS), but also may not be fully reliable. The final critical problem is weighting – used studies do not use the same approach to weighting results.

In the final part of the research, the method of partial induction is applied to verify the validity of the established research assumptions and the method of synthesis and deduction to identify the main problems of the contracting management process.

Problem solving

The first question on which the research focuses is the comparison of the extent of contracting with other internal forms of service provision, or the degree of contracting of local public services and ancillary services in public organisations and the dynamics of its development. The results are shown in Tables 5 and 6.

Table 5. The degree of contracting of local public services and the dynamics of its development (in %).

Service	2000	2005	2007	2010	2014a	2014b	2015a	2015b	2018 2019
Collection and disposal of municipal solid waste	71	80	65	83	91	65	79	96	93
Cemetery services	42	26	60	x	47	x	x	x	32
Maintenance of public greenery	45	24	49	x	22	x	x	x	26
Maintenance of local roads	31	38	55	x	52	x	x	x	22
Maintenance of public lighting	23	60	56	x	49	x	x	x	41

Source: Own research + research of Pavel, 2006; Soukopová et al., 2017, Soukopová and Klimovský, 2016

The data show that the most frequently contracted service is waste management. Furthermore, it can be seen that the service of maintenance of public lighting was relatively often contracted on the examined samples of municipalities over the years. For all other services the "figures" jump up and down, which is a bit surprise for the service maintenance of local roads (probably weighting problem, explained in discussion). Because of methodological problems (especially weighting in this case) stated in the methodology part, the figures provided in the Table 5 (and partly also in the Table 6 later on) show different results also for the same year, but the general picture is evident.

Table 6. The degree of contracting of ancillary services in public organisations, municipal authorities and the dynamics of its development (in %).

Service	2001	2009	2011	2012	2014a	2018 2019
Cleaning	33	7	37	24	23	2
Catering	52	31	42	35	84	NA
Building management and maintenance	40	11	9	20	35	5
Information technology management	49	38	63	44	58	33
Security services	31	26	68	36	75	53*
Transportation	x	18	20	46	86	NA

* 53% are from 19 municipalities that provide internal or external services, the remaining 22 municipalities do not have security services

Source: Own research, Páleníková, Mikušová Meričková, B., 2012

For ancillary services in public organisations providing public services, the most frequently contracted services are catering and transport of employees, security services and IT administration services. On the contrary, for some services, the internal method of provision still dominates (cleaning, maintenance and administration of buildings). There is no clear answer to the question from local governments whether public organisations "make or buy", i.e. to produce or buy a service.

Efficiency of contracting services in the public sector

The effects of contracting services in the public sector on the efficiency of their provision are standardly assessed formally by a simple comparison of the costs of internalisation with the costs of contracting services. The problem is the complexity of capturing the service cost indicator, which cannot be guaranteed given the available data either when monitoring internalisation costs (absence of cost centres in the first years of research, their formal functioning in subsequent years) or monitoring contracting (municipalities and public organisations do not monitor transaction costs associated with public procurement or subsequent monitoring of external production). In reality, we therefore compared expenditures from municipal budgets in the internalisation of services with expenditures on contracting services per citizen. The results are shown in Table 7 (per employee – Table 8). The values represent the percentage expression of the monitored indicator when contracting services, while the value of the indicator when internalising services is 100%.

Table 7. Cost efficiency of contracting local public services in the conditions of the Czech Republic in % (expenditure on providing the service per citizen).

Service	2000	2005	2007	2010	2014a	2014b	2015a	2018	2019
Collection and disposal of municipal solid waste	76	137	136	115	116	125	158	144	116
Cemetery services	x	95	x	x	x	x	x	34	76
Maintenance of public greenery	x	86	x	x	x	x	x	71	80
Maintenance of local roads	x	142	x	x	x	x	x	197	194
Maintenance of public lighting	x	118	x	x	x	x	x	62	51

Source: Own research + research of Pavel, 2006; Soukopová et al., 2017, Soukopová and Klimovský, 2016.

Table 8. Cost efficiency of contracting ancillary services in public organisations and municipal authorities in the Czech Republic in % (expenditure on providing the service per employee).

Service	2010	2011	2012
Cleaning	104	80	107
Catering	94	114	107
Building management and maintenance	97	90	117
Information technology management	117	99	236
Security services	105	51	44
Transportation	128	142	226

Source: Authors´own

The results are controversial, in some cases contracting is a cheaper form of providing services, while in some cases the costs of it significantly exceed the costs of internalising services. Contracting is, on average, 15 to 30% more expensive than internalisation. However, this fact is also due to the fact that internalisation does not quantify the real costs of providing the service, only expenditures from the budget due to the malfunction of cost centres.

To evaluate the efficiency of contracting services in the public sector, we subsequently used the method of multi-criteria evaluation for selected samples - the method of the best values of criteria. The results are shown in Table 9 – Table 10.

Table 9. Basic evaluation matrix of multicriteria evaluation of the efficiency of providing ancillary services in selected public organisations in the Czech Republic, 2011.

Public sector organisations			Culture		Social services		Education	
Service	Criteria	Variants	I	K	I	K	I	K
Cleaning		A	8,428.59	8,250.47	1,7481.07	1,2445.77	1,1169.96	520.66
		B	202.18	242.79	430.28	342.54	135.54	643.12
		C	65.17	77	78.6	79.93	66.41	65.5
Catering for employees		A	5,097.55	3,798.21	1,167.65	2800	3,560.77	4,600.85
		B	5,097.55	3,798.21	1,167.65	2800	3,560.77	4,600.85
		C	78	67.26	79.08	54	72.53	61.65
Building management and maintenance		A	7,946.13	(-)	1,0305.3	(-)	10,116.83	8,473.03
		B	3,557.4	(-)	2,130.51	(-)	1,827.06	2,853.51
		C	70.5	(-)	74.83	(-)	58.99	63.88
Information technology management		A	2,038.46	3,520.09	2,382.87	1,144.85	2,197.38	1,864.87
		B	2,894.74	913.14	900	819.27	1,495.68	417.86
		C	82.5	81.88	78	72.45	59.29	60.33
Transportation		A	3,772.15	1,484.85	1,429.13	(-)	3,408.73	1,428.57
		B	6.89	4.49	14.39	(-)	11.44	10.92
		C	84.33	86.75	74.4	(-)	48.7	57.9
Security services		A	8,000	1,8562.1	3,867.21	1,311.86	2,348.86	333.16
		B	12.69	49.43	26.95	17.66	26.68	13.29
		C	67	59.33	82	56.65	60.15	59.28

Legend: I – Internalisation, K – Contracting, A – Expenditure on providing the service per employee, B – Expenditure on the performance indicator, C – Quality of services evaluated on the basis of employee satisfaction as consumers of the service

Source: Authors´own

Table 10. Results of multicriteria evaluation of the efficiency of providing selected ancillary services in the monitored public organisations in the Czech Republic, 2011.

Public sector organisations	Culture		Social services		Education	
Service Variants	I	K	I	K	I	K
Cleaning	98.42	100	84.5	100	94.2	100
Catering for employees	90.04	100	100	52.4	100	80.2
Building management and maintenance	(-)		(-)		100	96.96
Information technology management	91.49	100	84.05	100	73.1	100
Transportation	70	100	(-)		74.7	100
Security services	100	56.3	79.91	100	59.44	100
Average	89.99	91.26	87.12	88.1	83.57	96.19

Source: Authors´own

However, based also on these more sophisticated results, it is not possible to unequivocally confirm or reject the assumption of a positive impact of contracting on the efficiency of the services provided.

Contract management as a factor of contracting efficiency

This fact that higher efficiency of contracting cannot be confirmed (but also cannot be rejected) raises the question: "Why does the contracting of services in the public sector in the conditions of the Czech Republic not bring regular efficiency gains?"

From several possible factors of the resulting contracting effect (the efficiency of service provision) we decided to evaluate the core one - the quality of contract management. The first simple question is, if correct and transparent selection of service provider dominates. In the conditions of the Czech Republic, this area of the contract management is problematic, as documented by the results of our research monitoring public procurement procedures (Tables 11 and Table 12).

Table 11. Public procurement procedures of selected local public services in the Czech Republic in %.

Procedure used for public procurement of services	2000	2005	2007	2010
Tender	12	12	24	43
Restricted procedure	4	40	15	6
Negotiated procedure	3	-	9	4
Price offer	10	-	-	23
Direct award	49	48	32	17
The municipality did not state the procedure of public procurement	22	-	20	7

Source: Own research + research of Pavel, 2006

Table 12. Procedures for public procurement of selected ancillary services in the Czech Republic in %.

Procedure used for public procurement of services	2009	2012
Tender	0	17
Restricted procedure	0	4
Negotiated procedure	-	5
Price offer	7	44
Direct award	45	27
The municipality did not state the procedure of public procurement	48	3

Source: Authors´own

In the next stage we calculated (Tables 13-15) the achieved score of contract management quality of contracting public services in the Czech Republic, according to the methodology described above for selected samples.

Table 13. Evaluation of the quality of the contract for the management of ancillary services in public organisations in the Czech Republic, 2011 in %.

Ancillary services		Cleaning	Catering for employees	Building management and maintenance	IT administration	Transportation	Security services	Average
Risk of non-transparency	Degree of competition in obtaining a public contract	46.25	27.43	34.3	41.53	38.87	44.03	38.73
	Clearly defined subject of procurement	50.63	52.35	55.8	58.03	44.13	58.18	53.18
Risk of hidden information	Ex-ante evaluation of the tenderer	66.27	81.5	49.3	69.17	60.15	58.33	64.12
	Professional knowledge	60.43	56.53	60.7	49.3	51.03	49.98	54.66
	Frequency of service production monitoring	59.08	66.23	60.83	59.08	34.13	65.65	57.5
Risk of moral hazard	Procedure in case of non-compliance with the contractual obligations	42.2	45.18	52.5	45.08	50.9	53.6	48.24
	Contract length	25.88	34.68	4.3	25.65	36.13	19.2	24.31

Source: Processed according to Páleníková, Mikušová Meričková, B., 2012.

Table 14. Evaluation of the quality of the contract management of local public services in the Czech Republic, 2014 in %.

Local public services	Risk of non-transparency	Risk of hidden information	Risk of moral hazard		
	Degree of competition in obtaining a public contract	Ex-ante evaluation of the tenderer	Frequency of service production monitoring	Procedure in case of non-compliance with the contractual obligations	Type of payment to the external supplier for the service
Maintenance of public greenery	37.50	34.38	34.38	21.88	37.50
Public lighting	50.00	20.27	37.84	18.11	44.59
Maintenance of local roads	52.70	21.62	37.84	19.19	56.76
Collection and disposal of municipal solid waste	58.20	21.31	60.66	24.43	50.82
Cemetery services	41.67	25.00	29.17	10.00	33.33
Average	48.01	24.52	39.97	18.72	44.60

Source: Authors´own

Table 15. Evaluation of the quality of the contract for the management of ancillary services of municipal authorities of the Czech Republic, 2014 in %.

Ancillary services	Risk of non-transparency	Risk of hidden information	Risk of moral hazard		
	Degree of competition in obtaining a public contract	Ex-ante evaluation of the tenderer	Frequency of service production monitoring	Degree of competition in obtaining a public contract	Ex-ante evaluation of the tenderer
Cleaning	55.00	25.00	55.00	29.00	25.00
Catering for employees	45.00	5.00	45.00	26.00	45.00
Building management and maintenance	57.50	12.50	35.00	20.50	52.50
IT administration	47.30	12.16	37.84	24.05	36.49
Transportation	28.95	10.53	23.68	6.32	26.32
Security services	50.00	13.33	36.67	19.33	26.67
Average	47.29	13.09	38.86	20.87	35.33

Source: Authors´own

The results indicate serious problems in the quality of contract management in the public sector, which increase the risks associated with contracting. The risk of non-transparency of public procurement processes, which is illustrated by inappropriately chosen procedures and a vaguely defined subject of public procurement, may cause the contracting authority / principal not to select the most suitable supplier / agent for external production of services. In this case, this is done for subjective reasons on the part of the principal - the contracting authority "does not want" to choose the most suitable offer. However, incorrect selection of the supplier may also occur for objective reasons in the case of a high risk of hidden information, if there is no ex-ante evaluation of tenderers then the contracting authority "does not know" how to choose the most suitable tender. Both risks can manifest themselves in the first phase of the contracting process, when choosing a service provider and seriously jeopardise the resulting effect of contracting, namely its impact on the efficiency of service provision.

Because the contracting process does not end with the selection of a supplier, which many public institutions contracting services forget about. Improperly defined contractual conditions (especially the length of the contract, sanctions, type of payment) together with insufficient monitoring of external production increase the risk of hidden activity and moral hazard. Moral hazard creates space for the external service provider to promote their own interests to the detriment of the interest of the contracting authority, which should be, economically, efficiently and effectively spending public funds to provide the service.

To summarise we may argue on the base of our samples that the largest reserves in the quality of management of contracts evaluated by us in terms of these risks can be seen in the process of public procurement services (often a price offer or direct award as a public procurement procedure, despite the fact that, given the nature and scope of the activity to be procured, a tender is the most appropriate procedure; the lack of a clear definition of the subject of public procurement; there is often a lack of a clear definition of the subject of public procurement; the only criterion for evaluating bids is the lowest price) and subsequently in the process of monitoring external production of the service and solving identified problems (irregular control of external production, "soft" punishment of the external supplier in the case of a breach of contract by the provider, limited room for negotiation, or a change of supplier given the disproportionate length of the contract).

Discussion and conclusion

Our two core research questions were as follows:

- Does contracting/outsourcing public services in the Czech Republic bring efficiency gains?
- If not, why contracting/outsourcing services in the public sector in the Czech Republic do not bring efficiency gains?

Before answering the first question we mapped the frequency of contracting local services and outsourcing internal services in the Czech public sector. The data from our samples indicate that both approaches are frequently used. From local public services the most frequently contracted service is waste management. The indisputable reason for this is the limited personnel and capital capacities of fragmented municipalities (the Czech Republic has almost 6,000 municipalities, but only 10 million inhabitants), which do not allow municipalities to respond flexibly to the growing demands of citizens for the scope and quality of these public services. The solution to the problem is the use of private sector capacity and the transition from an internal way of providing a service to an external one - contracting public services. From the point of outsourcing, it is again true that these are services whose internal provision would represent increased demands on the capital or personnel capacity of public organisations.

We are aware that the data provided by the tables summarising the scale of contracting and outsourcing are not fully comparable (this explains some "extremes" due to different weighting methods used for different samples), however, they clearly show general trends. The data confirm that “re-municipalisation”, as indicated by the recent literature on the topic (Kopric et al., 2018), is not an issue for the Czech Republic. Concerning the second question, it is not possible to come to the final conclusion about higher efficiency of internal versus external production. However, what we can clearly and un-doubtfully document is the fact that depending on the concrete case the more efficient solutions differ. For example, in the most recent sample the most expensive municipality spending for external delivery of waste services was 2051 Czech Crowns (27 CZK≈1 EUR) per inhabitant, but we also found municipalities with costs on the level of 14 CZK, 34 CZK or 40 CZK. Such extreme difference cannot be explained by other factors (like costs of waste transport and disposal).

These data not only document local differences, but also suggest that the data provided by municipalities and the data collected from central information system are not fully reliable, as municipalities do not use high quality financial management systems, which allow for calculation of overheads. The figures for external production, moreover, include added value and profit for most cases, so obviously they should be higher. Another problem, mentioned also above, is weighting, whereby a different form of weighting can significantly change the results, especially if one of the larger towns is in an extreme position.

Concerning the second research question, our data clearly confirm that the core factor of the limited success of contracting and outsourcing - the quality of contract management represent critical problem in the Czech Republic. This fact to a large scale explains why, in some cases, external production is highly effective, but in others not.

Our findings are fully in line with conclusions of other authors dealing with the issue of externalisation of services in the Czech public sector – including studies, not directly included into this text (like Soukopova et al. 2017). All authors confirm that large proportion of public services is delivered by external suppliers and the fact that economic results from externalisation differ case by case. Based on our finding and findings of other existing studies on the topic, we are able to provide critical policy recommendations - short guidelines in how to improve the current situation.

The key is the system process of providing the service, the aim of which is to provide the service economically and with quality. As this is a publicly funded service, the requirement of economy, efficiency and effectiveness of public spending should be met, which presupposes an ex-ante evaluation of possible alternatives for the provision of services in terms of meeting the objective. The choice of possible alternatives should be based on the conditions for providing the service, which are given by the legislative, economic assumptions and the assumptions of the public institution itself for the provision of the service.

If contracting is one of the options for providing the service, the next step is to evaluate the alternatives for providing the service, i.e. comparison of internalisation and contracting in relation to the achievement of the set goal, namely the cost-effective provision of a quality service. This process can be referred to as service testing. The process of testing, comparing internalisation and contracting includes information obtained by legal analysis of legislative conditions of service provision, market research, reallocation of indirect costs (through the creation of cost centres), an estimate of transaction costs in the event of contracting the service, supplemented by an evaluation of the material, technical and personnel capacities of the public institution to provide the service needed for the internalisation of the service.

The result of testing should be the selection of the optimal alternative, the form of providing the service and the subsequent production of the service that meets the conditions of economical, efficient and effective use of public funds. If contracting appears to be the optimal form of provision, contract management steps should be applied.

The first step is to define the subject of the public contract, to define the subject of the procurement, which should

again be based on the legislative conditions for the provision of the service defined on the basis of a legal analysis. This is followed by an estimate of the value, the price of the public contract based on the results of the market investigation and the quantification of the total costs of the internal production of the service after reallocation of indirect costs. After taking into account the subject, the price of the public contract and other circumstances and requirements defined by the legislation, the public procurement procedure can be chosen. Here, our analysis revealed shortcomings in the correctness of the chosen procedure of the public procurement for the contracting of services in the public sector in the conditions of the Czech Republic. The next step is the processing of tender documents and the announcement of the start of the tender, in this step it is important to select and enter the criteria for the evaluation of tender proposals. The analysis again pointed to a problem in this area, where the price is often decisive or the only decision criterion. The evaluation of tender proposals according to the set criteria is carried out in the next step.

The systematic implementation of the mentioned steps of the contracting management process can to a large extent eliminate the risks of information asymmetry and non-transparency of public procurement arising from the contracting of services in the public sector. Unfortunately, the analysis showed serious shortcomings in the quality of contract management, which in turn increases these risks. However, contract management has shortcomings not only in the phase of public procurement service, but also the subsequent control of its external production. It appears that public organisations forget that the contracting process does not end with the conclusion of the contract, it continues in the form of monitoring external production and building relationships with external suppliers, which together with well-defined contractual conditions eliminate another risk associated with contracting services in the public sector, namely the risk of moral hazard. These risks then affect the resulting effect of contracting, and the results appear controversial regarding its expected higher efficiency. This was also proved by our analysis. There will be the text of the contribution.

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