

Module 6

CONTRACTING FOR PERFORMANCE



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An Overview for Workshop Participants



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Introduction

Contracting out the provision of “government” services is not new. But what *is* new is the number and type of functions which are being opened to “outside” competition.

The Alberta government has transferred some services to various third party service delivery agents. The government prescribes the policies and standards to be followed by third party agents, and contracts with these organizations to deliver certain government services.¹ The government is still ultimately accountable to the public for ensuring that services delivered by third party agents are being adequately provided.² For example, the Minister of Education is the Legislature’s and Government’s agent for education matters, and is accountable to the people for the education system, even though education programs are delivered by local school boards.

Alberta Environmental protection has created Delegated Administrative Organizations. These organizations are arms length responsible to the Minister of Environmental Protection, committed to meeting certain objectives. The department has developed an accountability framework and a DAO Evaluation Workbook to help managers monitor the activities and accomplishments of DAOs, consistent with department and government goals and performance expectations.

Experiences in other jurisdictions cover a wide range of services:

- Over 15 years ago, the city of Phoenix, Arizona introduced competitive bidding in the solid waste division of its public works department. Since that time, the practice has spread to include services ranging from airport landscaping to low-income housing.
- In fiscal year 1996 alone, the state of New Jersey privatized medical services in correctional facilities, adult activities centers, day-care centers, motor vehicle agencies, janitorial services in the state house complex, and a managed care health plan for Medicaid patients.

As in Phoenix, the use of contracting among local governments has moved far beyond the traditional procurement of engineering services or the letting of street resurfacing contracts. In fact, as shown in *Figure 1*, a recent survey suggests that local governments’ use of contracting is skyrocketing in areas ranging from janitorial services to data processing.

Similar trends can be seen at the state level, with privatization becoming particularly popular in the areas of mental health, social services, and transportation. From the Governor’s Commission on Privatization of Government Services in Georgia to the Governor’s Council on Management and Productivity in Maryland, many states have formed commissions to study the privatization of state services. Perhaps most telling are the results of a 1993 study, in which over 85 percent of state auditors, budget directors, and controllers predicted increased privatization over the coming five years.³

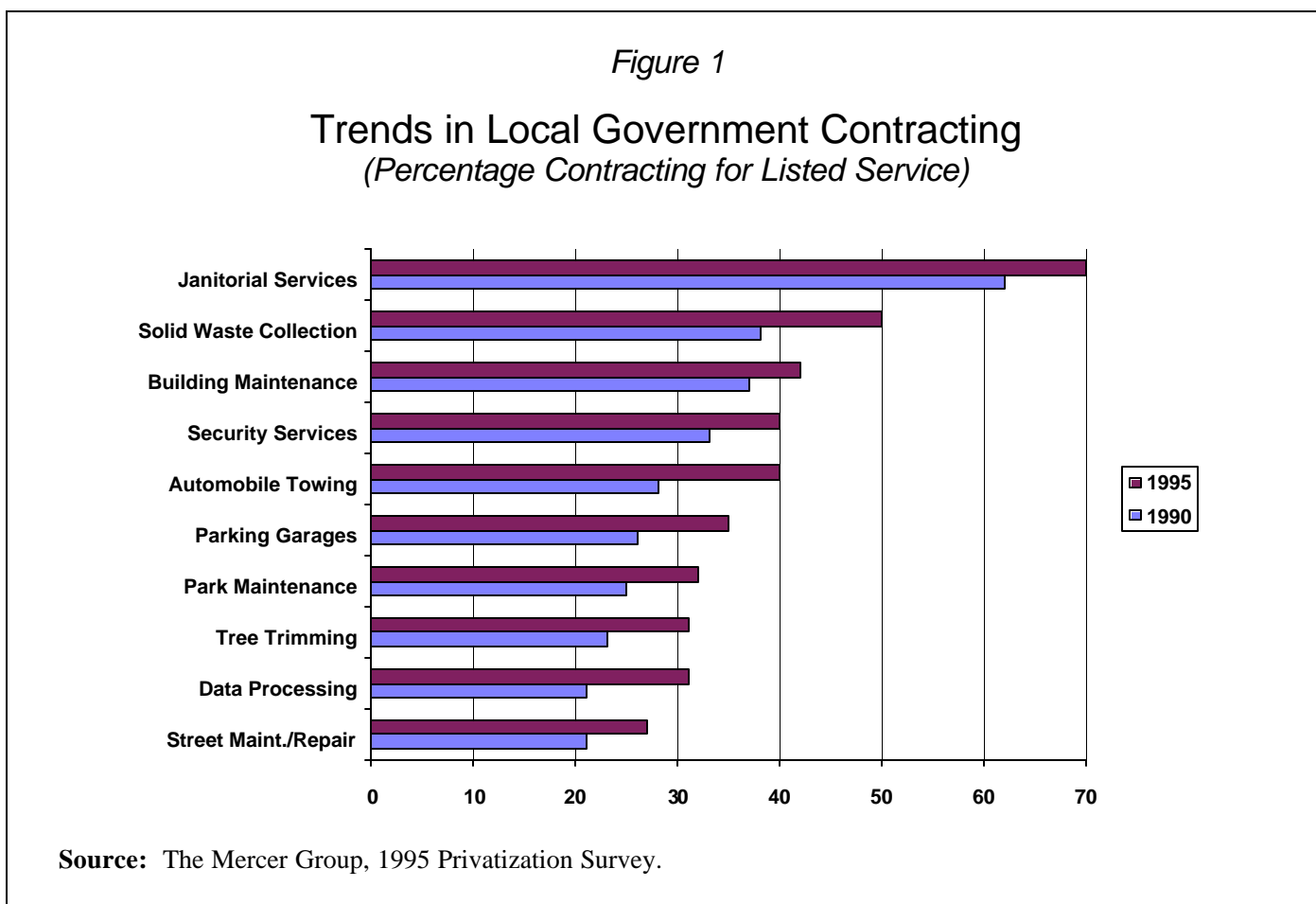
Why are Governments Turning to Contracting?

The primary lure of contracting is the potential for saving money. Over 90 percent of the 1,400 cities and counties responding to a 1992 survey by the International City/County Management Association indicated that fiscal pressures had prompted their privatization efforts.⁴

Although cost savings are not guaranteed by contracting out, a number of states and localities have achieved significant savings. The city of Indianapolis, for example, cut more than \$100 million from its budget over three years, attributing much of the savings to the introduction of competition in the provision of its municipal services.

Other reasons for the increased interest in contracting include the potential:

- To reduce the size of government;
- Gain access to specialized skills and/or equipment;
- Improve service quality and productivity;
- Achieve greater flexibility; and
- Gain economies of scale.



It is important to recognize that many of these potential benefits are the result of competition, not “the magic of the private sector.” Phoenix, for example, takes pains to describe its process as “managed competition,” not “privatization.” Rather than simply turning over the city’s business to private firms on the assumption that they can do the work better or cheaper, Phoenix offers private firms and city employees the opportunity to compete to win the right to deliver certain services. Of the 56 service delivery decisions the city has made since 1979, 34 have gone to the private sector while 22 have remained in-house. An added benefit of this process? Phoenix has found that it

establishes efficiency and customer satisfaction as important values, helping to influence positively expectations about government and gain public support.⁵

Potential Problems

Despite the potential promise, contracting is not always a positive experience. Cost savings don't always materialize, contractors don't always produce quality work, and the impact on public employees can be especially severe. Virtually every major city in the United States has experienced problems with contracted services ranging from simple service interruptions to outright fraud, and newspaper headlines are quick to trumpet these examples of privatization arrangements gone bad.

Clearly there is a big difference between entering into a contract with an outside vendor and contracting for performance with confidence that the desired results will be achieved. Incorporating performance measurement into contract bidding and monitoring procedures allows governments to control the risks and help assure the quality of services to their citizens.

In Alberta, contracting out has been initiated for a number of services, both with the provincial government and municipalities. Evaluation of performance indicates variable results.

What is Performance-Based Contracting?

Most governments already include performance specifications in their contracts. But, more often than not, these specifications detail how many job training sessions are to be held or the types of equipment that are to be used in road repair. While this type of information can play a role in contract monitoring, it tells you little about program results and quality. Of more value are measures that tell you whether or not desired results are being achieved. In other words, are students obtaining employment and increasing their earning capacity following completion of the contracted job training program?

Just as governments are discovering the value of outcome-oriented performance measures as a tool for internal improvement, they are also discovering the value of such measures in contracting. For example, in 1991, Tennessee's Bureau of Alcohol and Drug Abuse Services began evaluating its contractors based on the results they produced, not just the activities they provided. Whereas nonprofit agencies running programs for at-risk youth once promised a certain number of school assemblies (output measures), they later became responsible for demonstrating reductions in failing grades and truancy (outcome measures).

Performance-based contracting requires that government determine exactly what it needs to accomplish and to establish standards of performance and quality that become part of the contract. With those expectations clearly spelled out, the competition between multiple vendors assures that the government can demand and achieve the quality of service it desires. Many times, the process of defining performance expectations for a bid invitation or request for proposals (and developing good performance measures to monitor the contract) leads to improved service quality even if you opt not to contract for the service.

At its best, performance-based contracting is just plain good management:

- The analysis required to contract for performance gives managers the information they need to make good decisions.
- It provides incentives and opportunities for change, where change is needed. Management and labor practices grown stale and outdated often require some driving force to provide the impetus for change. Considering contracting out a service, or introducing competition and performance measures, provides just such an impetus.
- Performance contracting demands that performance standards be created and often introduces performance

measures where none existed previously. Introducing these accountability mechanisms improves communication of expectations to persons doing the work, while also forcing decision makers to decide precisely what they want a program or service to accomplish.

Is Contracting Right for You?

Contracting can lead to great results, but it is not a panacea and it is not right for every environment. Successful contracting requires:

- **Time for careful planning and execution.** It is not necessarily the solution to an emergency.
- **Agreement among top officials about program goals and objectives.** It might not be right in an environment where leadership is deeply divided on such issues.
- **Good management skills from within government.** It might not be a good option where talented management is scarce.

In any case, the approach you take to contracting must be adapted to your own culture, political environment, and management capabilities, not just imported from somewhere else. The city of Phoenix, one of the leaders in competitive contracting, notes that while its experiences may serve as a useful starting point for another locality, its process was developed over 15 years of trial and error. Localities with different organizational cultures, governing bodies, and labor relations histories will need to develop their own unique approaches.⁶

Implementation Steps

Successful performance-based contracting begins when you can assure three things:

- You know precisely what you want to accomplish;
- Those desired outcomes can be effectively achieved by a variety of providers—not just government; and
- You can assure results and accountability through careful negotiation of contract language and professional monitoring of the contract.

Key steps include the following:

Step One: Identify appropriate services for competitive contracting.

Any service is potentially a candidate for contracting, but some of the most common ones in the USA or across North America are:

- Professional Services (e.g., Auditors, Compensation Analysts, Graphic Designers, Engineers, or Lawyers)
- Information Technology: support and systems development, software customization and installation
- Collection Services (e.g., Taxes or Child Support Enforcement)
- Employment Training or Retraining
- Management of Public Facilities (e.g., campgrounds or convention centers)
- Property Management
- Surveys and Forecasts
- Transit System Operation and Maintenance
- Janitorial Services
- Drug/Alcohol Abuse Treatment Centers
- Solid Waste Collection and Disposal
- Street Repair, Roadway and Bridge Maintenance and Construction
- Security Services
- Worker's Compensation Claims Management
- Fleet Management/Vehicle Maintenance
- Food Services (e.g., in Parks, Prisons, or Museums)

- Groundskeeping and Snow Removal
- Laundry Services
- Community-Based Counselling and Family Violence Shelters
- Pest Control
- Effluent Removal
- Office Equipment Maintenance
- Prison Construction and Management

Selecting the services that are ripe for competitive contracting in your organization, municipality, or community will require careful study and analysis, encompassing four major steps:⁷

1. Identifying all existing services;
2. Using a checklist or other analytic tool to identify the best potential candidates for contracting;
3. Conducting in-depth feasibility studies of these candidates, including a detailed look at costs, personnel, and other important issues; and
4. Regularly reviewing and updating your analysis to take into account changing conditions and needs.

A sample of a decision checklist that the state of Colorado uses to identify contracting candidates is included as *Exhibit 1* at the end of this *Overview*. In developing your own checklist, you will want to consider some of the following factors:

- Potential for cost savings
- Political resistance
- Availability of potential contractors
- Complexity of service
- Impact on service quality
- Equity
- Impact on public employees
- Legal barriers
- Potential for service disruption and other risks
- Impact on other government services
- Ease of contract administration
- Long-term effectiveness
- Experience of other jurisdictions

Special consideration should be given to issues or concerns that are unique to your organization or community. For example, the weight you place on each of the factors may depend on your fiscal status, political climate, the degree of unionization among employees, the type of service being considered for contracting out, and the possible downside risks of turning over the service to a non-governmental entity.

Who should be involved in making contracting decisions? Many jurisdictions and localities have established high profile commissions to study opportunities for competitively contracting for services. Most share a focus on introducing competitive processes and developing performance standards to which either governmental departments or outside contractors can be held accountable.

The city of Philadelphia's Competitive Contracting Committee, for example, identifies potential areas for competitive contracting and establishes procedures and guidelines for analyzing and pursuing a competitive contracting process. Florida's Council on Competitive Government is a similar vehicle at the state level.

While this type of organizational focal point provides a high profile for the effort, it is by no means necessary to successfully pursuing competitive contracting. The most important point to recognize is that high levels of communication and inclusion result in coalitions of support for decisions, as well as in more informed decisions. It is never too early in the process to involve citizens, clients, employees, union representatives and outside experts. Broad

participation can help raise awareness about issues related to service quality and cost, build employees' capacity to identify "in-house" improvements, and ensure that analysis is fair and accurate.⁸

Step Two: Determine the full cost of in-house service provision, as well as the avoidable costs if a service is contracted out.

Getting a handle on costs is one of the biggest challenges of moving to competitive contracting. Although the most common reason that governments contract out is to save money, survey data suggests that fewer than half of those making privatization decisions have established procedures for making accurate cost comparisons between government and private providers.⁹

The first step toward making an accurate cost comparison should be to calculate in-house service delivery costs. This is not as easy as it sounds. You may know what the total Parks and Recreation budget is for community sports, but you are less likely to know what it costs to mow the grass in a city park or maintain sports fields and facilities. Yet, you must be able to get this information in order to answer any of these key questions:

- Are we paying a fair price for the service we are getting?
- How do our costs compare to those of comparable organizations?
- Can we save money if we place this activity out for open bid?
- Can we afford the level of performance quality that we currently expect?

Activity-Based Costing (ABC) is a technique that captures the "fully loaded" costs of delivering a specific service or product. Life cycle costing is a related costing approach which looks at all costs associated with the purchase, use and disposal of a piece of equipment. For example, the life-cycle costs of a computer printer would include the original purchase price, plus the ongoing maintenance costs and supply of ink. As shown in *Figure 2*, the full cost of "in-house" service includes not only direct costs such as wages, benefits, equipment, and supplies, but also administrative and other shared overhead costs. These shared costs are typically allocated to various activities or programs in proportion to their budget or staff size.

Figure 2

Analysis of In-house Costs

<u>Cost Factors</u>	<u>Amount</u>
Salaries of dept. personnel (including taxes, unemployment insurance, pension costs, and other fringe benefits)	_____
Other direct costs (travel, utilities, materials and supplies, printing)	_____
Equipment (rental, capital outlay, interest costs, maintenance)	_____
Operation and maintenance of buildings	_____
Insurance premiums (or claims paid if self-insured)	_____
Allocated administrative costs	_____
Allocated overhead cost of other executive and staff agencies	_____
Management/supervision/oversight	_____
Other cost factors	_____
TOTAL IN-HOUSE COST =	_____

Source: Adapted from *Privatization Assessment Workbook* (Denver, CO: Office of State Auditor, 1989), p. 25.

While activity-based costing can provide you with a clear picture of in-house service delivery costs, it does not provide the entire picture necessary for making decisions about contracting out services. Why not?

First, all of the costs associated with government provision of a service will not be avoided by contracting out. Unless outsourcing a certain service results in a significant reduction in your workforce, for example, it is likely that you will continue to need the same number of administrative workers to process your payroll checks. And, unless the outsourced service occupied an entire building that will no longer be needed, it is likely that your building, utility and maintenance costs will remain roughly the same. For this reason, it is recommended that avoidable costs rather than full costs be used when analyzing the likely cost savings of contracting out an activity.

HINT: Near the end of an equipment replacement cycle is a good time to do this type of cost analysis. Contracting out for an activity at this point will allow government to avoid the capital costs of equipment replacement.

There is a second reason why in-house costs cannot be compared directly to private sector bids. The bid amount, in fact, is not the only cost involved in private service delivery. In addition to the cost of the contract, you must also consider start-up or transition costs, such as developing the invitation to bid or request for proposals, bid analysis and selection, contract development, and compensation for any government employees who are terminated; the costs of contract administration and monitoring; as well as support costs provided to the vendor such as space, equipment, or use of government staff to field questions or complaints. There is at least the potential for incurring one more additional cost. If the contracting arrangement doesn't work out there will be costs associated with bringing the service back in-house. As more services are contracted out, some organizations are finding the experience to be less than satisfactory. For example in the area of information technology, an 1997 Information Week article noted that many organizations are finding that "outsourcing hasn't lived up to its promise". Because of their negative experiences, some firms are canceling contracts and trying to rebuild their in-house structures. In response to such experiences, increasingly, procurement professionals, aware that there is a risk that the contracting out might not work, are advising organizations to take into account the potential costs of having to repatriate services contracted out in making such decisions.¹⁰

Figure 3

Analysis of Contracting Costs

<u>Cost Factors</u>	<u>Amount</u>
Start-up Costs	_____
Primary Contracting Costs	_____
Contract Oversight Costs	_____
Contract Support Costs (space, equipment, or other support provided)	_____
Subtotal =	_____
Minus New Revenues (taxes, fees, disposal of assets)	_____
TOTAL CONTRACTING COST =	_____

Source: Adapted from *Privatization Assessment Workbook* (Denver, CO: Office of State Auditor, 1989), pp. 27-29.

In the final analysis, the actual cost savings of contracting out a service will be:

$$\text{Avoidable Costs} - \text{Total Contracting Costs} = \text{Cost Savings}$$

In order to make an accurate comparison, make sure that in-house costs and contractor's costs are based on the same performance standards and requirements.

HINT: Establish costing policies for the organization to ensure that cost analyses use consistent information over time. For example, careful analysis should go in to assigning indirect costs to activities and departments. Once this analysis has taken place, the use of the resulting allocations should become policy.

Step Three: Prepare solicitation documents and define performance expectations.

There are two major types of contracts used in the public sector: *competitively bid* contracts and *negotiated* contracts. Competitive bidding starts with the "invitation to bid (ITB)" in which the government entity sets the bid specifications, offers the bid to the public and selects the vendor submitting the best bid (by law usually the lowest responsive, responsible, or cost effective bidder). The bid specifications, functional design or combination of both are *very* specific and structured by government, and essentially make up the final contract. The only major difference between contractor's bids will be cost, and there is little to negotiate at this stage. Competitive bidding is most common in services that are labor-intensive, discrete, easy to quantify, and have large economies of scale. Services that are frequently competitively bid are waste management, public utilities, and transportation.

The other major type of contract is negotiated. Contracts are negotiated when there are special needs to be met by a service, a high degree of professional skill is needed, or the unique abilities of individuals are key. Negotiated contracts typically begin with a Request for Proposals (RFP). Proposals are invited for solutions to a set of requirements (functional or design or a combination of the two). RFPs have less structured requirements than competitive bids. As a result, there is likely to be much more variation between contractor's proposals. Although competitive bidding is becoming more common in an era of scarce resources, negotiated bidding is still the most common way to award human service contracts and professional services. The RFP process provides a starting point for the negotiating process by requiring vendors to state their respective positions.

In developing a plan for soliciting bids or proposals, ensure that you are proceeding in accordance with the policies of your organization. If you work in a ministry, and are contracting for supplies including certain IT services, you will be guided by Schedule 12 of the Government Organization Act. If you are contracting for services, the recently approved Accountability Framework applies. Either way you also need to ensure you act within the parameters of the Internal Trade Agreement regarding ensuring that out-of-province business are able to submit bids or proposals. More information on the Agreement and over general information on procurement policies in the Alberta government can be found at Public Works and Supply and Services' website at <http://www.gov.ab.ca/~pwss/its/how2sell/>. Your Finance or Administration staff can also tell you what policies and procedures apply in your circumstance.

General information on best practices in procurement and other resources can be found at the MERX website. MERX is an online bulletin board of listing of major federal and provincial government invitation to Bids or RFPs. In the Marketplace section [<http://www.merx.cebra.com/marketing/market/index.htm>] of MERX, you can find links to recent articles on RFPs and procurement practices and to organizations in this field offering training.

You Can't Get What You Want Unless You Know What You Want

One of the most challenging—but critical—tasks in contracting is adequately describing the scope of work in solicitation documents. It has been noted that “a well-written scope of work can do more for the success of a contract than any other part of the contracting process.”¹¹ Vague or otherwise poorly written specifications, on the other hand, can make later enforcement and administration of the contract difficult and/or costly.

There are three things to keep in mind as you begin this process:

- There must be **consensus** among management staff and elected officials regarding **program objectives** and **performance measures**. A good contract cannot contain internal contradictions or vague language about what is to be accomplished. If consensus at the top is lacking, this may not be a good time to pursue contracting.
- Those objectives are not necessarily achieved best by duplicating what the government has done in the past. As shown in *Figure 4*, specifications should **define what must be accomplished, but not necessarily how it must be accomplished**. Further details on developing appropriate performance measures can be found in Module 3, *Performance Measurement*.
- **Involving stakeholders** in the development of program objectives and writing specifications will not only help ensure that you adequately describe the requirements of the job, but will help you establish the coalition of support that is necessary to keep the process moving forward. Phoenix, for example, has had success with using customer focus groups to help operating managers identify quality results.

It is wise to invite client representatives, employee representatives (including union representatives if applicable), and experts in the provision of service (e.g., executive director of an organization that is involved in contracts for similar activities) to serve on a team to review and establish program specifications. Keep in mind, however, that those involved in writing specifications should have no financial or other interest (e.g., family relationship or potential job if contract is awarded) in the contract. At a minimum such an interest presents the appearance of a conflict of interest. At worst, such a conflict could unfairly bias the selection process and cost the government dearly in reputation, cost of the contract, and potential lawsuits from other vendors.

Figure 4

Performance Specifications

In its mowing contract, the City of Indianapolis specifies that:

- The grass should kept at less than eight inches in height. (OUTCOME)

*It does **not** specify:*

- How often the grass should be mowed (PROCESS)
- What type of equipment should be used (INPUT)

Why?

- Need for mowing varies with the weather. Why mow every six weeks if it is not needed?

In addition to setting forth performance expectations, solicitation documents should include:¹²

- The purpose and objectives of the services to be contracted
- The nature and extent of services to be contracted
- Time-frame for work to be completed
- Information to be submitted on bidder's/proposer's financial status, and technical and managerial qualifications, including references, approach, proposed personnel and their qualifications, equipment and its condition
- Special requests for information on certain key issues (e.g., plan for minimizing displacement of current public employees)
- Reporting and monitoring requirements
- For competitively bid projects, the standard of award (e.g., low bid, lowest responsive and responsible bidder, lowest and best bid) and whether discretion to award is restricted by law—or, for requests for proposals, evaluation criteria and the scoring process required under procurement policy
- Anticipated schedule for decision making and how bidders/proposers will be informed of the decision
- Information on payments, audits, termination, dispute resolution, penalties, bonding, and insurance requirements.
- Status of submitted documents vis-à-vis freedom of information legislation
- Where, when, and how bids/proposals are to be submitted
- Procedures for handling inquiries
- Type and amount of any required bid guarantees
- Format for bid or proposal response
- What costing information is required

HINT: Never allow a single potential vendor to have undue influence on the writing of specifications. Specifications should be written broadly enough to assure that multiple vendors can bid on the contract.

Step Four: Identify potential contractors and solicit bids or proposals.

Whether requesting bids, proposals, or qualifications, you will follow approximately the same procedures, including:

1. Identifying potential contractors;
2. Advertising; and
3. Answering questions.

Identifying Potential Contractors

Competition is critical to realizing the benefits of competitive contracting. How can you help ensure that you will get a good response to your request for bids or proposals? First, make sure that you cast your net widely. The label “privatization” that often gets used when government contracts work out has led many to think that only the private sector firms make good candidates for performance-based contracting. Not true! The list is much longer, including:

- Private Sector Businesses;
- Non-profit Organizations (NPOs)--sometimes referred to as volunteer or non-government organizations;
- Other units or levels of government; and
- Your own employees, including unions!

Make sure that you consider a variety of service delivery options and select the best approach for your particular situation. The contracting approach that is right for solid waste collection may not be the right approach for pre-natal counseling, for example. You may decide to:

- Contract with a single firm or nonprofit organization;
- Contract with multiple firms or organizations;
- Contract out part of a service and retain the remainder in-house;
- Contract out only capital programs; or
- Contract out only management.

About NPOs: As the name implies, non-profit organizations do not exist to make a profit, but to perform some kind of service or to fill an unmet need. They are often formed to address social problems such as homelessness, illiteracy, poverty or unemployment and have close ties to clients at the grassroots level. In Canada, there are over 175,000 non-profit organizations. Of those, over 75,000 are charities, able to issue tax receipts for donations. In the US, as a result of their experience in addressing societal problems, NPOs have become an important part of human service provision in the, accounting for 80 percent of all state and 78 percent of all county human services contracts.¹³

Other Units of Government: Other units of government might be successful contractors as well. For example, the bus maintenance division of the local school district might be a likely candidate for bidding on a city's fleet maintenance contract. In Alberta, this is happening both between ministries within the provincial government and across municipalities. For example, under the shared services initiative, Alberta Treasury now provides human resource services to two other ministries; Alberta Labour and Executive Council. At the municipal level, the Town of Bruderheim, contracts with the neighbouring County of Strathcona for the management of its municipal services. This two year old arrangement was recognized by the Fraser Institute in 1998 as representing an innovative way to save money in government.

Your Own Employees: Don't overlook your own employees as you search for potential contractors. Since it is your employees' jobs that are at stake, they have a strong interest in submitting a competitive proposal. Besides, who knows the work better? Initially, technical assistance may be needed to help government employees make the step towards competition. The city of Charlotte, North Carolina, for example, conducts competitiveness workshops for its public agencies; topics range from full cost accounting to productivity improvement.

How does this translate into developing a list of potential bidders? While you should continue to develop and maintain a list of vendors to which you routinely mail RFPs or ITBs for specific types of services, always seek to reach new potential vendors. Contractor's associations, directories of business and nonprofit enterprises, directories of minority business enterprises, chamber of commerce listings, and even the yellow pages are good sources for mailing lists, as are recommendations from organizations or governments that have contracted out for similar services.

You also have the option [and in some circumstances, must] post your RFP or tender documents on the MERX [www.merx.cebra.com] system, the online bulletin board of tenders and RFPs, mentioned earlier to ensure you reach the maximum number of qualified contractors. The MERX system displays the following Alberta information:

- notices and tender documents for most goods over \$2,500 acquired
- centrally through Alberta Public Works, Supply and Services
- notices and tender documents for services over \$100,000
- notices only for construction projects over \$100,000
- contract award information
- general Terms and Conditions of purchase information/messages of interest to Alberta vendors.

You may also want to explore and address factors which limit the number of vendors interested in bidding on government contracts. The following factors pose problems for non-profit or small and minority contractors in particular:¹⁴

- **Payment procedures.** Paying contractor bills as quickly as possible and permitting more frequent billing can help reduce the potential for cash flow problems among small contractors or non-profit organizations. You might also encourage or assist potential minority contractors to apply for small business loans, including those loans oriented toward minority businesses.
- **Paperwork.** Use plain language to set out job specifications, and keep the paperwork as brief as possible.
- **Bonding costs.** Attempt to help with, or alleviate any bonding costs such as bid and performance bonds. At a minimum, provide technical assistance to help businesses find the least expensive bonding organizations.
- **Contract size.** Small businesses are often unable to bid on contracts for large government jobs. It is helpful to break the contract into smaller segments in order to encourage more competitors. For example, contracts for building maintenance can be issued for a single building rather than for all buildings owned by the government. Contracts for roadside mowing or for garbage collection can be divided into several geographic districts. Letting smaller contracts also has the advantage of being able to compare the quality of service being provided by multiple vendors.
- **Bid/Proposal format.** Some have found that the glitz of proposals from well-heeled consulting firms can outweigh the substance of the proposal. Evaluation teams can be swayed by the attractiveness of full-color documents filling three-inch binders. These types of proposals are time-consuming to peruse as well as disadvantageous to small businesses. For that reason you may want to specify and limit the information to be submitted, and define the simple style in which it is to be presented.

Advertising

Advertising is not always legally required. If it is not, you may get equally good results from a thorough vendor list or electronic posting.

In cases where you do advertise, the advertisement should contain:

- Name of your agency;
- Description of target service;
- Place to obtain complete RFP or bid information;
- Place, time and date of any pre-bid or pre-proposal information workshops;
- Place, time, and date of bid opening or proposal deadline; and
- Details such as the right of the agency to reject all bids.

Answering Questions

A pre-proposal or pre-bid information workshop or meeting provides an opportunity to respond to questions, offer additional information that has become available, and provide a tour of relevant facilities. If conducted with enthusiasm, it also provides an excellent opportunity to heighten vendors' interest in the contract. Attendance at the information workshop can be made either optional or mandatory, depending on how critical you feel the workshop is to gaining a clear understanding of the project.

Throughout the bidding and proposal process, one of the most important points to remember is to keep the process as **fair, open, and transparent** as possible. It is common, for example, for flaws in the RFP or ITB to come to light in information workshops, necessitating an addendum to the solicitation document.

Remember, any addenda must be sent to all entities that received the original document. Other points that will help ensure fairness include:

- Ensure that there is a wide distribution of invitations to submit proposals or bids.
- Do not grant exceptions or waivers to bid or proposal requirements unless that same exception is granted to everyone with adequate notice.
- Limit contact with potential vendors. Information or clarifications provided to one must be provided to all.

- Hold a public bid or proposal opening at the date, time, and location advertised. Record all responses that were received at that time. Do not accept responses received after the advertised deadline.
- Maintain complete records of all who have received the RFP or ITB so that any necessary addendum can be sent. This will also serve as a list of vendors to notify of future contracting opportunities.

HINT: Bids or cost estimates submitted by your employees should be independently verified to assure fairness in the process. It is also important to hold your employees accountable for the costs and proposals they submit if they are awarded the contract or retain the service in-house.

Step Five: Evaluate bids or proposals and award contract.

Within a short time of your advertisement or other notice, “the word will be on the street.” You may be deluged with calls, mail, faxes, personal visits.

Be prepared to answer queries concerning the eventual winner of the contract. In the case of a invitation to bid, or call for tenders, there is often a public bid closing ceremony where the names of bidders and the amount of their bids are disclosed.

Initial Screening

The first step is to screen out bids or proposals that are incomplete or unacceptable. Bids can typically be eliminated only if a determination is made that they are not “responsive” and “responsible.” What does this mean? ¹⁵

- *Responsiveness* refers to the respondent’s compliance with all the requirements of the bid/proposal process and solicitation. In other words, was the bid or proposal submitted on time? Does it include all requested information? Is the response in the required format?
- *Responsibility* refers to the respondent’s ability to do the work called for in the solicitation. Most importantly, does the bidder or proposer have the ability, capacity, skill, and financial resources to perform the work or provide the service required—and within the time specified? Has the proposer or bidder performed quality work on previous contracts? Have they fully complied with any bonding requirements?

A qualification checklist can be used to help perform this initial screening. (Note that in some cases, potential bidders are “qualified” prior to the submission of bids by having met benchmarks at a formal pre-qualifying evaluation of their processes and/or products.)

The screening process for proposals often goes beyond that required for bids in order to reduce the responses to a manageable number for more in-depth review. The selection process typically begins with the formation and training of an impartial committee to screen and evaluate proposals and to make an award recommendation to the governing body.

Who should be involved? You may want to consider some of the following:

- A representative of the department that is to award the contract (if the department is not also bidding on the contract);
- A representative of the department that is to use the service provided;
- A representative of the budget/finance department;
- Purchasing officer;
- An individual with relevant technical skills;
- Clients of the service to be contracted out;
- Citizens or advisory committee members;
- Community leaders; and
- Executive directors of non-profits.

In addition, purchasing officials and legal counsel are often included in an advisory capacity.

Evaluating Bids and Proposals

Once the initial screening is completed, bid evaluation is relatively straightforward. The award typically must go to the qualified bidder offering the lowest price or the most cost-effective bidder, according to pre-established criteria.

Evaluation of proposals is much more complex. After an initial screening, you may find that further information is needed in order to develop your “short list” for final consideration. This may be accomplished in a number of ways, but an interview process is among the most effective. The firms to be interviewed should be notified in writing of the time and date of the interview and asked to bring any key personnel to aid in answering your questions or concerns. Once the interviews are completed, you should be in a position to make an award recommendation or to forward a final list of two to three candidates to the decision makers for a final presentation.

Evaluation of proposals should focus on rating each of them on criteria or factors such as the following:

- *Project understanding.* Does the proposal demonstrate an awareness of client needs? Does the proposer appear to comprehend the scope of services? To what extent does the proposal address the agency’s priorities and objectives?
- *Quality of work.* Based on past performance and/or personnel qualifications, what is the likely quality of the work? What is the technical education, training, and experience of the personnel to be used on this project? What is the firm’s past experience on projects of this nature? What do references say about their experiences with the proposer? How much of the firm’s or organization’s business is with “repeat” customers?
- *Organizational capacity.* Does the firm or organization appear to have the capacity to take on a project of this size? Have they done projects of this size in the past? What are their current commitments to other projects?
- *Adherence to proposal requirements.* Has the proposer complied with proposal requirements, such as providing all documentation, addressing equal employment opportunity considerations or setting out a plan to minimize displacement of current government employees? As noted earlier, a summary of the criteria and their related weightings to be used in the evaluation of proposals should be included in your RFP documents so proposers know what your decision will be based on.
- *Project Approach.* What sets the firm apart in terms of original thinking and analysis of this project? How does the firm plan to organize the project? What is the firm’s management plan and project schedule.
- *Project Budget.* What cost control techniques will be used? What has been the past relationship between the firm’s cost estimates and its actual project costs? What has been the firm’s past record in regard to the percentage of change orders versus the original contract amount? Will the firm be financially responsible for errors or omissions made on the project?
- *Provincial/ Municipal Familiarity.* How familiar is the firm with the project, clients, and regulatory requirements?

Although some communities use point systems when evaluating proposals, this is not always required. Keep in mind that rigid systems may limit discretion to emphasize or reward important qualifications. The criteria you select and the relative weightings you assign to them form the decision model you will use to rate each proposal and make the decision as to which, if any, to accept. Such models can be constructed on paper if they are relatively straight forward or for more complex or crucial decisions by using decision support software. Either way, you build and use the decision model to determine which proposal offers the best "value for money" for your organization. As the Commonwealth of Australia defines it, value for money is "the essential test against which agencies must justify an procurement outcome. It is not an attribute or criterion in itself but is a basis for comparing alternative solutions."¹⁶

Contract Negotiation and Award

With *competitive bids*, the specifications in the bid document essentially make up the final contract. There is little to no room for negotiation on either specifications or price.

Negotiated contracts, as the name implies, are subject to negotiation of both price and specifications. In this case, you will begin your negotiations with the top-ranked organization or firm. The specifics to be discussed, reviewed, and agreed upon during the course of the negotiations include:

- Project schedule;
- Areas of responsibility;
- Performance expectations; and
- Compensation.

One of the most important objectives of the negotiation process is to reach a complete understanding of the scope of services to be provided. While you may have reached a preliminary understanding earlier in the process, the negotiation phase allows for refinement, amendment, and complete definition of the services to be provided, as well as compensation for those services. This portion of the negotiation phase should minimize the possibility for misunderstandings between the client and the contractor as the project progresses.

The compensation to be awarded to the chosen firm can be your biggest hurdle during negotiations. You should already have an approximate cost of your project. Compensation may be negotiated and established according to a number of different formulas—the lump sum or fixed fee is the most popular. Compensation should be detailed in the contract, specifying what costs are and are not included. In addition, agreement should be reached regarding what constitutes an application for a change order to the contract and subsequent additional costs. This process can be facilitated by including a proposed change order process in the IFB or RFP and asking the vendor to agree to it or propose changes to it.

If a contract agreement cannot be reached with the top-ranked organization or firm, do not hesitate to terminate negotiations and begin negotiations with the second-ranked firm. In the event that negotiations fail with all of the top-ranked organizations or firms, you may want to re-examine the project in light of its expectations and funding.

The Contract

As in any contract, both parties have certain responsibilities to perform. The government's and the contractor's responsibilities should be clearly itemized and defined in the contract document. Performance expectations should be spelled out as well, including:

- What will be evaluated and how will it be evaluated?
- What are the acceptance tests on the deliverable(s)?
- What constitutes compliance with performance requirements?
- What constitutes a breach of contract?
- Will penalties be imposed for failure to meet performance expectations?

- Are there incentives for exceeding performance expectations?

The contract can contain a wide variety of provisions that will influence the performance of the contractor and help assure compliance with the contract:

- Performance bond requirements;
- Security in the form of an irrevocable letter of credit;
- Hold back amounts against outstanding invoices;
- Penalties for failure to perform such as delayed payments or fines;
- Incentives for early performance;
- Cancellation of the contract for failure to perform;
- Financial incentives for completion of work ahead of schedule or achieving a specified high level of performance;
- Compensation tied directly to performance (such as % of gross collections);
- Performance reporting and monitoring requirements;
- Requirements to participate in technical assistance or training opportunities; and
- Fairly frequent re-bidding of contract in order to maintain competition and avoid complacency of vendors (although this will need to be weighed against the time required to start-up and retrain new contractors).

The above should all be identified in the RFP or IFB to make sure they are provided for in the price bid.

Step Six: Implement ongoing monitoring of performance.

A contract is only as good as the monitoring and follow-up conducted by the contract manager. The contract must contain enforceable provisions and requirements for data collection and monitoring reports, but it is up to the manager to develop the knowledge and skills necessary to detect and resolve problems that can arise.

A post-award conference between representatives of the government and the contractor can help to set the foundation for a successful contracting experience. Not only does such a meeting provide an opportunity to review contract documents in detail and minimize the possibility for misunderstandings, but it also helps to establish a “partnership” between government and the contractor.

Items discussed at a post-award conference typically include:

- Detailed contract provisions;
- The roles and responsibilities of each party;
- Performance expectations;
- Procedures for monitoring and measuring performance;
- Procedures for resolving citizen complaints;
- Procedures for resolving any disagreements between government and the contractor;
- Billing and payment procedures; and
- Security and confidentiality requirements

Ongoing monitoring should focus on four basic issues: customer satisfaction; timeliness; productivity; and performance problems.¹⁷ Monitoring tools include:

1. *Periodic contractor reports.* Reports submitted by the contractor should be verified by government for accuracy, then reviewed for contract compliance and adherence to the project schedule.
2. *Inspections.* Inspections may include a random sample of completed work (e.g., the cleanliness of curb miles of street); on-site observation of work in progress; or inspection of equipment for safety. In some cases, it may be appropriate to obtain samples for laboratory testing.
3. *Review and analysis of complaints.* Some communities maintain a central hotline for citizen complaints, enabling them to monitor the type and volume of complaints. Others require contractors to report on citizen

complaints on a periodic basis. In either case, it is important to monitor how the contractor resolves any complaints.

4. *Client and/or citizen surveys or interviews.* Surveys or interviews can help you obtain information about customer satisfaction with contracted services.

What should you do if a performance problem is detected? Clearly, you can cancel a contract or enforce penalties if a contractor is not performing as desired. However, it is much better to develop a good working relationship with the contractor such that performance problems are resolved rather than having to resort to cancellation or penalties.

In the case of human services in particular, switching contractors can be very disruptive to clients. For example, a child that has been physically abused may be further traumatized if forced to give up a counselor with whom he or she has formed a bond. Or, if a group of clients depend upon a particular non-profit organization to provide meals in their neighborhood, they may face serious problems if a contract is switched to an other organization that is across town.

In cases such as these, provision of technical assistance is one option for resolving problems. The Human Services Department in Ramsey County, Minnesota, for example, has had good results with using “successful” contractors as mentors to those experiencing difficulty in meeting performance expectations.¹⁸

HINT: A contract manager must be careful not to become too close to a contractor—partnership does not mean “cronyism.” Government still must be objective in its treatment of its contractors and the contracting process. Contract administrators can provide technical assistance, but *they do not work for the vendor*; they work for the taxpayers and clients who access the service.

Barriers to Competitive Contracting

There are a number of barriers that you may face as you pursue outside contracting, including:

- Lack of competition;
- Concerns about service quality; and
- Concerns about financial risks or service interruptions.

Approaches to dealing with these barriers include:

- Maximizing competition through careful selection of services, consideration of a wide variety of potential contractors, simplification of paperwork, breaking the contract into smaller segments, and other similar strategies;
- Including citizens and elected officials in conducting contracting feasibility studies and developing contract performance specifications;
- Establishing clear procedures for resolving any complaints related to service quality;
- Developing strategies for reducing risk, such as breaking a service into smaller projects and developing an emergency plan to deal with service interruptions; and
- Maintaining communication with elected officials, employees, citizens, and the media throughout the process.

The prospect of government employees losing their jobs is also a barrier. You may want to consider strategies that:

- *Accommodate existing employees through attrition, transfer and early retirement.*
 - Developing an early retirement package;
 - Instituting a temporary hiring freeze in related departments to create openings in which to transfer affected employees;
 - Delaying implementation of the contract in order to allow natural attrition to occur;
 - Providing for phased implementation of the contract so that work is transferred to outside

- contractor over a period of time, allowing employees more time to seek alternative employment;
- Providing in-house job transfers; and
- Retraining employees for new positions (e.g., contract administrator).

- *Require contractors to give preferences to government employees.*
 - Requiring contractor to give qualified government employees the right of first refusal for all jobs created by the contract; and
 - Requiring the contractor to offer wage and benefits packages similar to government.

- *Provide outplacement services to affected employees.*
 - Notifying employees of their rights (e.g., bumping rights or transfers to other departments);
 - Providing information about unemployment benefits and severance pay, benefits for the continuation of health insurance, and pension options for vested employees;
 - Providing career counseling and assistance with filling out job applications;
 - Providing office services such as copying and telephone use to assist with the job search process; and
 - Providing personal counseling through an Employee Assistance Program.

Sensitive management of the transition will have a tremendous impact on the morale and productivity of all employees, not just those affected by the contract.

Implementation Tips

You will maximize your chances for success by considering the following tips:¹⁹

- Obtain consensus and commitment from top leaders;
- Research and plan the process thoroughly;
- Address employee concerns;
- Encourage competition;
- Ensure that objectivity is maintained in awards, monitoring, and renewals;
- Establish a monitoring plan before you contract;
- Define the contracted service in terms of desired results;
- Enforce contract performance standards;
- Maintain good communication with the contractor, elected officials, public, and government employees;
- Invest in the necessary expertise;
- Identify your financial exposure and negotiate contract safeguards; and
- Be prepared to walk away when red flags signal trouble ahead.

Suggested Readings for More Information about Performance Contracting

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- p.3 [add reference to Unit 2 endnotes and to overview suggested readings }

Endnotes

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- ² Auditor General, Alberta, *Government Accountability*, February, 1997
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- ⁷ John Tepper Marlin, *Contracting Municipal Services: A Guide for Purchase from the Private Sector* (New York: John Wiley & Sons, 1984), pp. 13-14.
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- ⁹ *Findings of a National Survey of Local Government Service Contracting Practices* (Atlanta, GA: Mercer/Slavin, Inc., 1987), p. 2, pp. 13-14 as cited in Lawrence Martin, "How to Compare Costs Between In-House and Contracted Services (Los Angeles, CA: Reason Foundation, March 1993), p. 2.
- ¹⁰ Outsourcing Backlash, by Bruce Caldwell and Marianne Kolbasuk McGee in *Information Week*, September 29, 1997 *Figure 3* provides an abbreviated worksheet for calculating the total cost of contracting out an activity.
- ¹¹ Donald Harney, *Service Contracting: A Local Government Guide* (Washington, DC: ICMA, 1992), p. 45.
- ¹² Drawn primarily from "Purchase of Service Contracting," *Service Delivery in the 90s: Alternative Approaches for Local Governments* (Washington, DC: International City/County Management Association, 1989) and Harney, p. 47.
- ¹³ Eggers and Ng, p. 3.
- ¹⁴ Drawn from Harry P. Hatry, Elaine Morley, George P. Barbour, Jr., and Steven M. Pajunen, *Excellence in Managing: Practical Experiences from Community Development Agencies* (Washington, DC: The Urban Institute Press, 1991).
- ¹⁵ Harney, p. 202.
- ¹⁶ <http://www.ctc.gov.au/publications/purchasing/cpg/cpg.htm>
- ¹⁷ Ibid.
- ¹⁸ Laura Skaff, *Ramsey County, Minnesota: Performance Contracting at the County Level* (Washington, DC: American Society for Public Administration, 1996).
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