University of Bristol

Law Research Paper Series
Paper #008 2019

# Classic Debates in Public Service Outsourcing

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bristol.ac.uk/law/research/legal-research-papers

ISSN 2515-897X

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## Deciding on the private delivery of public services

Where the state decides that certain goods and services – for example, healthcare - are not provided in sufficient quantities or in just distribution by the market (for example, on account of high transaction costs or the inequality of purchasing power), it might consider it necessary to intervene by expending public funds, and to take on political responsibility for their provision as public services. In making such a commitment, its first challenge rests in framing the exact scope of its political responsibility. It must define exactly what people need and expect from the public service - what public needs it considers must be met to serve the public interest, given limited public resources. This usually involves considerations of pricing, scale and service quality, which can be oriented towards a range of policy and regulatory goals of a general and specific nature. Currently, for example, decisions on public services provision and funding should be oriented to the achievement of, among other localised goals, the overarching UN Sustainable Development Goals.[1] These political decisions involve trade-offs between competing needs for public funding - for example, balancing the goal of fair and equal access against the desirability of high-quality services, as well as competing demands across different public services. The state must also anticipate complexities in how to measure the public benefit of a service.[2]

Assuming responsibility for a public service does not mean the state will step in directly as provider. Instead, it will consider whether to deliver the service directly (in-house) or by passing the responsibility for its delivery on to private actors by contract (outsourcing). These decisions may be understood through the lens of discretion and agency. The complexities involved in the delivery of multiple services invariably require the state to delegate some discretion over the delivery process to certain private or public actors (agents). By selecting either a public (in-house) or private (outsourcing) delivery model, the state determines where this discretion should lie and by what means it wishes to impose control and accountability on those who exercise it. Opting for in-house delivery, the state choses for this discretion to fall on officials within one or several public agencies, subject to oversight by way of a public legal and administrative regime. It triggers a public mode of governance, with

[1] See Fayyaz Baqir, Nipa Banerjee and Sanni Yaya (eds), *Better Spending for Localizing Global Sustainable Development Goals. Examples from the Field* (Routledge 2020).

[2] On this, see extensive literature in the field of public administration studies, e.g. Mark H Moore, 'Public Value Accounting: Establishing the Philosophical Basis' (2014) 74(4) *Public Administration Review* 465-477; John J Kirlin, 'What Government Must Do Well: Creating Value for Society' (1996) 6(1) *Journal of Public Administration Research and Theory* 161-185; Iestyn Williams and Heather Shearer, 'Appraising Public Value: Past, Present and Futures' (2011) 89(4) *Public Administration* 1367-1384; Gene A. Brewer, 'Public management contributions for improving social service performance: public values, public service motivation and rule functionality', in Peter Leisink et al (eds), *Managing Social Issues: A Public Values Perspective* (Edward Elgar 2013) 19-36; Julian Christensen et al, 'How do Elected Officials Evaluate Performance? Goal Preferences, Governance Preferences and the Process of Goal Reprioritization' (2018) 28(2) *Journal of Public Administration Research and Theory* 197-211. See also Marc Cowling, 'Measuring public value: The economic theory' (2006) Work Foundation Papers, available at https://pdfs.semanticscholar.org/1aaa/e3662d6a1738850c0da6ae1ad296e245b015.pdf (accessed 28 November 2019).

emphasis on administrative procedure and the rule of law, a split between policy and administrative functions and reliance on public sector hierarchies and bureaucracies to directly deliver public services.[3] When it chooses instead to outsource, the state is prepared to confer some discretion over the execution of service delivery on private providers and to exercise oversight chiefly by specifying for this in a contract. This contractual (private) mode of governance typically incorporates the 'use of markets, competition and contracts for resource allocation and service delivery.'[4]

Which of these options the state will select ultimately depends on whether, given associated costs and existing capacities, it considers the public or private sector likely to provide a better (and this might include a more accessible, sustainable, high-quality, transparent, ethical, etc.) public service for less. The state's objective, in other words, is to maximise the "public value" it is able to provide with available means, even where this value might be difficult to define and to measure, especially in relation to certain qualitative or distributional service aspects.[5] The state determines whether, given limited resources, a public or private delivery (and governance) model will be better suited to support the pursuit of the public interest in the expenditure of public funds to the largest possible extent.[6] This is not to ignore a certain type of ideological argument that sees outsourcing, for example, as a means of "shrinking" the state in the interest of individual liberty, or public organising as an instrument to protect inherent state functions or fostering public solidarity and a "strong" state.[7] However, at the level of practical decision-making, those arguments rarely feature as a formal justification for out- or in-sourcing, at least not in explicit terms. Instead, concrete decisions or policies tend to prioritise what Freeman calls 'pragmatic'[8] choices between public or private delivery that centre on cost-effectiveness, conceptualised usually as long-term savings and better services (again, defined according to a multiplicity of politically constructed values). In other words, they are about improving service outcomes (in terms of quantity and quality) while managing cost and the expenditure of resources (long-term savings) in order to serve the public interest (provide best public value) consistently with democratic values and political choices.[9]

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[3] Patrick Dunleavy, *Democracy, Bureaucracy and Public Choice. Economic Explanations in Political Science* (Routledge 1991), in particular part II.

[4] Stephen Osborne, *The New Public Governance? Emerging Perspectives on the Theory and Practice of Public Governance* (Routledge 2009) 4.

[5] See literature above fn. *.

[6] Joseph E. Stiglitz and Jay K. Rosengard, *Economics of the Public Sector* (4th end, W W Norton & Co 2015). More generally, Anthony Ogus, *Regulation: Legal Form and Economic Theory* (Clarendon Press 1994).

[7] Jody Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116(5) *Harvard Law Review* 1285-1352, 1295.

[8] Jody Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116(5) *Harvard Law Review* 1285-1352, 1291.

[9] For evidence in the British context, see the Barber Review, *Delivering better outcomes for citizens: practical steps for unlocking public value* (2017) available at https://www.gov.uk/government/publications/delivering-better-outcomes-for-citizens-practical-steps-for-unlocking-public-value (accessed 4 July 2018); National Audit Office, *Delivering public services through markets: principles for achieving value for money* (2012), available at https://www.nao.org.uk/wp-content/uploads/2012/06/Delivering_public_services_through_markets.pdf (accessed 4 July 2018); and National Audit Office, *Deciding Prices in Public Services Markets: Principles for Value for Money* (2013), available at https://www.nao.org.uk/wp-content/uploads/2014/01/10333-001-Deciding-prices-in-public-services_30-Dec.pdf (accessed 29 May 2019). For discussion, see Julian King, *Assessing Value for Money* (2018) available at https://www.opml.co.uk/files/Publications/opm-approach-assessing-value-for-money.pdf (accessed 4 July 2018).

For decades, these questions have stood at the heart of public service organisation in most developed market economies. An example is the evolution of public services in modern Britain, especially in England and Wales where a shifting blend of public and private models has consistently shaped the delivery of public services over the last forty or so years - from the introduction of markets (or quasi-markets) and compulsory competitive tendering under the Conservative Thatcher government in the 1980s; New Labour's attempt at partnering the market and the state, and the introduction of public-private partnerships in the 1990s and early 2000s; to more recent attempts to rely on privatisation as a strategic cost-cutting response in a policy context of public austerity under the consecutive Coalition and Conservative governments. The growth of outsourcing is only one aspect of this evolution which has also seen, for example, the liberalisation of public utilities and full privatisation ("selling off" as opposed to "contracting out") of some public infrastructure.

The decision to involve markets in the delivery of public services is a feature across the West. Most systems currently involve a mix of public, quasi-public and private provision, often contrasted with a state-centred delivery model which dominated the late 19$^{th}$ and first half of the 20$^{th}$ century especially in Europe and North America, as public agencies stepped up direct provision of services as part of emerging welfare models. This contrast, while it can be useful, should not be overplayed. In historical terms, the state-centred model was itself only a short-term phenomenon. Before the modern epoch of greater ambitions, states used to be more like "night watchmen": their role was primarily to guarantee law and order. Providing basic welfare and services, on the other hand, was left squarely to local communities, charities and philanthropy. It might only be possible to understand modern debates on outsourcing fully if we consider them in the context of this "insourcing" that happened earlier: rather than seeing the relationship between market and state exclusively in the modern context of privatisation, we might be better off looking at it from a historical perspective of continuity. From this perspective, while the last few decades might be seen as a response to earlier centralisation that has led to rising privatisation and outsourcing, they might also actually be seen as a return to an even earlier period where the state was less involved in service provision at all. The difference is that in the modern context, outsourcing (i.e. the withdrawal of direct public delivery) means not automatically a reduction in the state's ambition to provide the services in question. Rather the converse, public authorities resort to outsourcing as a tool to "buy-in" additional capacity from within the private sector to realise these ambitions.

Regardless of where we are on this continuum, the choices involved in the decision whether to deliver a public service in-house or by outsourcing are complex. They usually draw on a mix of economic and political arguments, and depend on a whole set of contingencies like: where do relevant public capabilities lie in terms of service delivery and management? Is the service involved complex or straightforward to specify? Is there an existing market for it and is it competitive? Is delivery envisaged on a national or local scale, and does it involve specific structural characteristics, for example a natural monopoly (e.g. water)?

Addressing this complexity invariably requires a combination of evidence- and policy-based decision-making. It is necessary, on the one hand, to ground these decisions in careful empirical assessments and case-by-case analysis that surveys the available evidence of existing or projected needs and of delivery models, ongoing and past.[10] The challenge is to find suitable evidence-driven solutions most likely to ensure that 'aptitude [is] maximised, expense minimised'[11] provided a given set of circumstances and requirements. On the other hand, far from being an isolated empirical choice, and however evidence-based a choice it might be, decisions on whether to deliver a service in-house or to outsource are invariably connected to wider policy programmes set by central or local government. These programmes implement a set of normative and strategic options that designate certain practices and delivery models as preferred *modus operandi*, not least to render practice across the public sector more consistent and easier to assess and to coordinate. Incorporating political choices (for example, what qualitative service elements to emphasise) as well as factual evidence collated over time, they provide formulas – an instruction manual (of sorts), or 'playbook' in current jargon – that act as both guidance and constraint on individual public decision-makers and agencies.

The UK public service sector again provides a good example of how transformative such policy programming can be, not least because it often generates widely held assumptions and expectations about the role of the state and the market in providing public services. In Britain, this applies not only to the initial major outsourcing programmes of the 1980s and transition to partnership-based models of collaboration between public and private sector in the 1990s (see above). More recently, polices of "strategic commissioning" based on a cycle of assessing public needs and securing appropriate outcomes have heavily influenced practical decision-making. These in turn have influenced a widely used 'two-tier' model of private delivery involving prime- and sub-contractors (sometimes with several levels of sub-sub-contracting) where the prime contractor acts as "commissioning coordinator", 'managing provision and deciding on which sub-contractors …. Are most suited to achieving the outcomes for priority clients.'[12]

Our aim in this chapter is to examine four key areas of debate where normative tensions play out and empirical challenges arise that are central to decisions relating to the (private) delivery of public services. They will play on the minds of policymakers and of public commissioners having to consider, within an existing political and policy framework, whether to outsource a public service, or set of services, or whether to provide it in-house. Clearly, a great deal of organisational diversity exists within public and private delivery (and this will re-emerge later in the book) – compare for example a de-centralised public-public collaboration with a central government bureau; or a co-decision structure involving multiple stakeholders at delivery and management level, with a traditional procurement. At this stage, our focus is on characterising the key normative arguments and empirical concerns that tend to define decisions on whether one or other of these broad models would be preferable to deliver a public service. These relate to public and private capabilities, public service markets and competition, service quality and innovation considerations, as well as democracy and accountability.

## Public and private capability

Outsourcing offers an opportunity of integrating private actors into service delivery to strengthen the state's capacity to deliver the political objectives of a public service. Given public capacity constraints

[10] See Sandra Nutley, Annette Boaz, Huw Davies and Alec Fraser, 'New development: What works now? Continuity and change in the use of evidence to improve public policy and service delivery' (2019) 39(4) *Public Money & Management* 310-316.

[11] Jeremy Bentham, *Constitutional Code* (Oxford: Clarendon [1830] 1983), p. 297.

[12] Tony Bovaird, 'The ins and outs of outsourcing and insourcing: what have we learnt from the past 30 years?', (2016) *Public Money and Management* 67-74, 68.

and the existence of complementary or additional private sector capacity, this might prove essential where, without outsourcing, the state would lack the capability to deliver ambitious welfare programmes to its citizens. Once it has made the political choice to provide a public service, private delivery might be the only way for the state to find the resources to follow through on that choice, at least in the short to medium term.

But these effects of supplementing public capacity must be looked at carefully as comprehensive assessments of resourcing are far from straightforward. First up, it is necessary to assess whether there is enough in-house capacity within the public sector to take on – or, in cases where outsourcing is currently in place, to take back - the delivery of public services and enough public sector capability to apply public governance mechanisms to internal activities directly (e.g. through a public agency or bureau). The concern is whether the public sector has the capacity to deliver services *better (quantitatively and qualitatively) and cheaper* than the market, and under adequate governance frameworks. This requires an appropriate level of investment in the public sector, especially where previously outsourced services are taken back in-house after a period of private delivery. Where the state identifies a lack of capacity to provide a service in-house, it faces a choice of whether to build-up the public sector or to buy-in private sector resources. Where it is theoretically capable of providing multiple public services in-house, it must decide on the basis of adequate evidence,[13] whether by outsourcing some of them it can usefully free up resources to invest elsewhere.

Secondly, it is necessary to consider that both in-house delivery *and* outsourcing demand public resources – albeit not necessarily of the same type or within the same public agency or department. To operate outsourcing effectively, strong public capacities are needed.[14] Managing complex and long-term public contracts requires investment in organisational structures and especially in skilled personnel, for which the public sector must compete with market actors.[15] In Britain for example, supporting the 'skills and capabilities of civil servants' as service commissioners has been identified as 'pivotal' to ensure successful outsourcing.[16] Decisions whether to in- our outsource therefore always involve balancing one set of public capabilities against another, namely, the resources to provide a service directly against those available to tender, manage and monitor outsourcing contracts. This happens especially where the state considers transitioning from one delivery model to another: where, after a period of outsourcing them, it wishes to move services back in-house or, conversely, where it chooses to outsource services that it had thus far provided through public agencies. In either case, it must ensure that it has the right kind of resource available: in one case, spare capacity to

[13] UNDP Global Centre for Public Service Excellence, *Is the Private Sector more Efficient? A Cautionary Tale* (2015) available at https://www.undp.org/content/dam/undp/library/capacity-development/English/Singapore%20Centre/GCPSE_Efficiency.pdf (accessed 13 December 2019).

[14] Jonas Prager, 'Contracting out Government Services: Lessons from the Private Sector' (1994) 54(2) *Public Administration Review* 176-184.

[15] Report on administrative capacity for procurement at EU Member State level: https://ec.europa.eu/regional_policy/en/policy/how/improving-investment/public-procurement/study/

[16] See Institute for Government, *Commissioning for success: how to avoid the pitfalls of open public services* (2012), p. 13 available at https://www.instituteforgovernment.org.uk/sites/default/files/publications/Commissioning%20for%20success.pdf (accessed 6 June 2019). See also Institute for Government, *Making public service markets work. Professionalising government's approach to commissioning and market stewardship* (2013) available at https://www.instituteforgovernment.org.uk/sites/default/files/publications/Making_public_service_markets_work_final_0.pdf (accessed 4 July 2018).

absorb the direct provision of the public services currently outsourced; in the other, the capability to effectively design and monitor the outsourced delivery and to manage the relevant contractual relationship.[17]

To operate an effective public service system sustainably, the state cannot afford to limit its focus on the short-term impact that outsourcing might have in delivering an operational or frontline capacity boost. Instead, it must also consider the long-term effects that turning to private delivery models might have on the development of public sector resources over time. Here, the concern is that any positive impact on capabilities in the short-term could be offset by negative long-term consequences, which in some cases might be sclerotic – landing the state with a model of public services that makes it overly dependent on private providers, yet insufficiently resourced to function as an effective in-house provider or diligent manager of its own public contracts (or, at least, capable of doing so only after a period of expensive reinvestment).

Extensive and repeated outsourcing, in multiple sectors and over long periods, merely reinforces those path-dependencies.[18] The concrete risk is that following extended periods of privatisation and reinforced by public policies of economic austerity, resources are drawn away from public sector agencies and reinvested, indirectly through public contracting, in the private sector, or simply lost. This however means that over time the capability of the public sector itself is being eroded – forcing the state increasingly to buy-in private sector capacity, including e.g. for tasks that it might otherwise have chosen to keep in-house.[19] These situations can create a vicious spiral where short-term (outsourced) capability contracts absorb the funds that could otherwise be used to (re)generate long-term public sector capabilities-and which can only be stopped and reversed with significant levels of additional investment that might be too difficult to mobilise. The negative effect of course will be that at some point, public sector capacity might be reduced so far that the state is "stuck" with the private delivery model: it then becomes very difficult to take services back in-house without, at least, a longer transition period and/or expensive re-investment. At the same time, and perhaps more worrying, in a scenario of depleted public capabilities post-privatisation, particularly when combined with politically driven economic austerity, a trimmed-down public sector is hardly in a strong position to manage complex contractual arrangements in a way that e.g. shields the public interest from strategic exploitation by private providers.

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[17] This is e.g. particularly clear, and worrying, in the recent report by NAO, *NHS England's management of the primary care support services contract with Capita*, HC 632 Session 2017–2019, 17 May 2018, available at https://www.nao.org.uk/report/nhs-englands-management-of-the-primary-care-support-services-contract-with-capita/ (accessed 4 July 2018). Similar issues keep being raised as a continued problem, eg NAO, *Government Commercial and Contracting: an overview of the NAO's work* (2016), available at https://www.nao.org.uk/report/government-commercial-and-contracting-an-overview-of-the-naos-work/ (accessed 4 July 2018). For a more general assessment, see National Audit Office, *Improving government procurement*, HC 996 Session 2012-13, 27 February 2013, available at https://www.nao.org.uk/wp-content/uploads/2013/03/government-proc-full-report.pdf (accessed 4 July 2018).

[18] See José M Alonso & Rhys Andrews, 'How Privatization Affects Public Service Quality: An Empirical Analysis of Prisons in England and Wales, 1998–2012' (2016) 19(2) *International Public Management Journal* 235-263.

[19] For a crude and rather damning assessment of the situation in the UK, see National Audit Office, *Capability in the civil service*, HC 919 Session 2016-17, 24 March 2017, available at https://www.nao.org.uk/wp-content/uploads/2017/03/Capability-in-the-civil-service.pdf (accessed 4 July 2018).

A recurring theme in debates over privatisation, and one that we will pick up at various points within this book, is therefore the necessity to factor these risks of path-dependency carefully into outsourcing decisions in the first place and take steps to avoid them. Failure to do so means the state will face their consequences when it considers re-internalising a service after a period of outsourcing e.g. when political circumstances or public needs change, or a specific outsourcing arrangement is perceived to be faulty. Such deferred effects of current in- or outsourcing and public sector funding decisions compound their political intractability, as governments adopting decisions with significant but deferred effects are unlikely to be held accountable for them, and can potentially exploit short-termist policy interventions for political gain.[20] Therefore, even in an outsourcing context, it is essential for the state to retain enough capabilities within the public sector not only to ensure effective contract management, but also potentially to step back in as provider – to guarantee that switching between public and delivery models, while not cost-free, is a manageable task. Here, the difficulty rests particularly in guaranteeing the availability and continued access to the valuable resources of information, data and knowledge that usually come with being involved directly in the delivery of a public service. With outsourcing, these resources are handed over and made accessible to the private sector, risking asymmetries that mean suppliers hold more relevant information than the state due to the displacement of 'institutional memory'.[21] These resources are usually very difficult (and expensive *if* possible) for the public sector to replenish and may be permanently lost unless concrete institutional structures are put in place to control and secure continuing access to them for public institutions.

On these issues, evidence that charts the recent evolution of public services in Britain offers a cautionary tale. It suggests that in terms of capacities management, the UK government might have currently chosen the worst of both worlds. On the one hand, the capacity to deliver in-house has been undermined as a result of years of public austerity and systematic outsourcing policies. On the other hand, the same policies have also undermined the state's management capacity, and studies have identified weaknesses in contract management across all UK government departments as a 'long-standing issue', with government unable to afford 'either to bring in or retain commercial experts to match the combined expertise of its contractors'.[22]

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[20] For classical discussion, R Barro, 'The control of politicians: an economic model' (1973) 14(1) *Public Choice* 19-42. For a more positive outlook, see I Garri, 'Political short-termism: a possible explanation' (2010) 145(1-2) *Public Choice* 197-211.

[21] This has recently become obvious in the UK, and the Government is piloting a scheme to try to correct this information asymmetry; see e.g. Dominic Brady, 'Government announces "living wills" pilot to protect public services' (21 Nov 2018, *Public Finance*) available at https://www.publicfinance.co.uk/news/2018/11/government-announces-living-wills-pilot-protect-public-services, (accessed 29 May 2019). For discussion, see John Tizard, 'Will 'living wills' add life to public outsourcing – or create complacency?' (26 Nov 2018, *Government Opportunities*), available at http://www.govopps.co.uk/john-tizard-will-living-wills-add-life-to-public-outsourcing-or-create-complacency/ (accessed 29 May 2019). See also Government Commercial Function, Resolution Planning. Outsourcing Guidance Note (Feb 2019), available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/801427/Resolution-Planning-Guidance-Note.pdf (accessed 29 May 2019).

[22] National Audit Office, *Transforming Government's Contract Management*, September 2014, p. 10, available at https://www.nao.org.uk/wp-content/uploads/2014/09/Cabinet-office-cross-government-transforming-governments-contract-management-summary.pdf (accessed 31 January 2019). See also National Audit Office, *Improving government procurement*, HC 996 Session 2012-13, 27 February 2013, available at

## Markets and competition

Outsourcing is invariably related to economic arguments that point to private delivery as a means of improving allocative and productive efficiency by providing services within a competitive market system which does not (generally speaking) apply to public delivery.[23] Many of these arguments are grounded in neoclassical and transaction cost economics.[24] Applying rational choice approaches, these theoretical frames analyse the delivery of public services in transactional terms, expecting the state to approach the task like an economic actor would: business-like with an objective of 'obtaining high-quality services at *the lowest possible* cost, thereby freeing up resources that might otherwise go to waste and allocating them elsewhere to maximise welfare.'[25] The emphasis on competition is seen to introduce high-powered financial incentives[26] motivating market actors and their personnel to deliver services more efficiently (to save on delivery costs) in ways that the public sector, without the same level of exposure to competition, cannot offer. In outsourcing, competitive tendering for public contracts means provider organisations and their operatives are under constant pressure to perform better and cheaper than others. These markets are expected to exert enough competitive pressure on private providers to ensure they deliver services as best they can at the lowest cost.[27]

Public hierarchy, on the other hand, is seen to encourage 'a loss of incentive intensity and added bureaucratic costs'[28] by traditionally shielding in-house organisations from such competitive market pressure. It subjects individual employees to rewards and sanctions typical for public sector employment which are different from those in private labour markets.[29] But the lack of external pressure from competition in large public organisations is viewed as making people less likely to work as hard and effectively as they otherwise would or could - producing so-called 'x-inefficiencies'.[30] Bureaucracy requires a high-level of resource to be maintained permanently even in times of lower

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https://www.nao.org.uk/wp-content/uploads/2013/03/government-proc-full-report.pdf (accessed 4 July 2018).

[23] Oliver E. Williamson, *Markets and Hierarchies: Analysis and Anti-Trust Implications* (Free Press 1975).

[24] For a starting point on emerging behavioural approaches, see eg Stephan Grimmelikhuijsen, Sebastian Jilke, Asmus Leth Olsen and Lars Tummers, 'Behavioral Public Administration: Combining Insights from Public Administration and Psychology'(2017) 77(1) *Public Administration Review* 45-56.

[25] Jody Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116(5) *Harvard Law Review* 1285-1352, 1296.

[26] Howard Frant, 'High-Powered and Low-Powered Incentives in the Public Sector' (1996) 6(3) *Journal of Public Administration Research and Theory* 365-381.

[27] Oliver Hart, Andrei Shleifer and Robert Vishny, 'The Proper Scope of Government: Theory and an Application to Prisons' (1997) 112(4) *Quarterly Journal of Economics* 1127-1161.

[28] Oliver E. Williamson, 'The Economics of Governance' (2005) 95(2) *American Economic Review* 1-18, 11. For discussion, see John B Goodman and Gary W Loveman, 'Does Privatization Serve the Public Interest?' (1991) 69(6) *Harvard Business Review* 26-38, available at https://hbr.org/1991/11/does-privatization-serve-the-public-interest (accessed 4 July 2018); Jean Tirole, 'The Internal Organization of Government' (1994) 46(1) *Oxford Economic Papers* 1-29.

[29] E.g. Evan M Berman et al, *Human Resource Management in Public Service: Paradoxes, Processes, and Problems* (6th edn, Sage/CQ Press 2020).

[30] Harvey Leibenstein, 'Allocative Efficiency vs. X-Efficiency' (1966) 56(3) *American Economic Review* 392-415, 413; Kenneth Button and Thomas Weyman-Jones, 'X-inefficiency and regulatory regime shift in the UK' (1993) 3(4) *Journal of Evolutionary Economics* 269-284, 270. See also Alan Peacock, 'Public X-Inefficiency: Informational and Institutional Constraints', in Horst Hanusch (ed), *Anatomy of Government Deficiencies* (Springer 1983) 125-148; Jonathan Haskel and Amparo Sanchis, 'Privatisation and X-Inefficiency: A Bargaining Approach' (1995) 43(3) *Journal of Industrial Economics* 301-321.

need and, in the absence of competitive pressure, incentives to curb over-bureaucratisation and seek out efficiency inside the organisations' working practices are seen as relatively low.

Barring significant changes in other aspects (e.g. the technology underpinning the delivery of the service), this perspective therefore views as relatively implausible the possibility that in-house delivery would be more cost-effective than outsourcing. A well-functioning market system, on the other hand, that exposes organisations to pressure by requiring them to offer themselves up as service providers in a competitive tender for public contracts, is considered to make it more likely for them to operate efficiently in the longer term than hierarchies. Given these constraints, it has been suggested that, from a transaction cost perspective, 'internal organization is usefully thought of as the organization form of last resort: try markets, try hybrids, and have recourse to [public hierarchy] only when all else fails.'[31]

The counterpoint to these arguments based on the theoretical superiority of the allocative efficiency of markets can be found in a body of theoretical and empirical studies which conclude that both public and private sectors can operate efficiently, and that there clearly are situations where the public sector will organise delivery more cheaply and better than the market.[32] They suggest, in other words, that the question of which model might ultimately deliver greater efficiency cannot be normatively fixed but is fundamentally contingent on context, including the nature of the service in question, political choices (e.g. related to distributional issues) and institutional issues, such as whether the public service falls within the responsibility of a local authority, a non-governmental commissioning body (e.g. an NHS trust) or a central government department. .[33]

From this perspective, the observation that public hierarchies produce low-efficiency, low-powered incentives, is seen as an oversimplification.[34] Incentivisation within the public sector is difficult but its study has reached a high level of sophistication in advancing financial and non-financial incentives.[35] This comprises, not least, the extensive literature on the development of a 'public service ethos' in the

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[31] Oliver E. Williamson, 'The Economics of Governance' (2005) 95(2) *American Economic Review* 1-18, 12.

[32] Jonas Prager, 'Contracting out Government Services: Lessons from the Private Sector' (1994) 54(2) *Public Administration Review* 176-184; B Villalonga, 'Privatisation and efficiency: differentiating ownership effects from political organisational and dynamic effects', (2000) 44(1) *Journal of Economic Behaviour and Organization* 43-74; Mildred E. Warner and Amir Hefetz, 'Insourcing and Outsourcing: The Dynamics of Privatization Among U.S. Municipalities 2002–2007' (2012) 78(3) *Journal of the American Planning Association* 313-327; Hulya Dagdeviren & Simon A Robertson, 'A critical assessment of transaction cost theory and governance of public services with special reference to water and sanitation' (2016) 40(6) *Cambridge Journal of Economics* 1707-1724; Raymond Gradus and Tjerk Budding, 'Political and Institutional Explanations for Increasing Re-municipalization, (2018) *Urban Affairs Review* 1-27.

[33] Tony Bovaird, 'The ins and outs of outsourcing and insourcing: what have we learnt from the past 30 years?', (2016) *Public Money and Management* 67-74.

[34] Jensen and Stonecash refer to it as a 'naïve' observation. See Paul H Jensen & Robin E Stonecash, 'Incentives and the Efficiency of Public Sector-outsourcing Contracts' (2005) 19(5) *Journal of Economic Surveys* 767-787, 781.

[35] E.g. Simon Burgess and Marisa Ratto, 'The Role of Incentives in the Public Sector: Issues and Evidence' (2003) 19(2) *Oxford Review of Economic Policy* 285-300; Paul H Jensen & Robin E Stonecash, 'Incentives and the Efficiency of Public Sector-outsourcing Contracts' (2005) 19(5) *Journal of Economic Surveys* 767-787; Josse Delfgaauw & Robert Dur, 'Incentives and Workers' Motivation in the Public Sector' (2008) 118(525) *Economic Journal* 171–191; Evan M Berman et al, *Human Resource Management in Public Service: Paradoxes, Processes, and Problems* (6th edn, Sage/CQ Press 2020) 209-290.

public administration tradition.[36] It comprises, similarly, a 'huge academic industry'[37] charting how in recent decades public bureaucracies have internalised private management strategies including competitive restructuring of their internal organisation.[38] While contested,[39] the policies of 'new public management' dispel the notion of modern public administration as a monolithic and (over-)bureaucratised hierarchical state apparatus of Weberian proportions, or a lack in dynamism.

These arguments suggest that adequate incentivisation of public servants and cost management within public bureaucracies are possible, and that inefficiency is not necessarily intrinsic to the system (i.e. inherently linked to public hierarchies). The economic argument that in-house delivery should be seen as a last resort appears, from this perspective, partial: poor incentive structures and over-bureaucratisation associated with public hierarchies can be avoided with some investment in public management (with the expectation that this will be amortised by resulting cost-savings). There is no reason to assume that the amount required necessarily outstrips what the state might otherwise have to invest in outsourcing to the private sector—which remains an empirical question that requires case by case analysis.

Efficiency, seen from this perspective, clearly is conceived in broader terms and reliance on competition is not all.[40] While the market might be suited to deliver relatively simple public goods, in-house delivery might be better suited to provide complex and long-term service needs that require some joined-up thinking where the state takes into account the full complexity of the service in question rather than addressing aspects of it.[41] This might require the bundling of different services and identifying connections between them and coordinating different public needs, which the public sector is better placed to do than the private sector. It has the capability to draw on different public agencies, and for those agencies to collaborate where necessary. Incentives for individual opportunism are attenuated and motivations to resolve conflict or ambiguity cooperatively are strengthened because 'hierarchy enjoys the advantage for managing cooperative adaptations, and the market for autonomous adaptations.'[42] The public sector can operate as a system that understands public service not just in terms of its technical delivery but is also 'heavily based on [public] values,

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[36] Public Administration Select Committee, 'The Public Service Ethos' HC 263, 2001-2, para. 12; P John and M Johnson, 'Is there still a public service ethos?', in A Park et al (eds.), *British Social Attitudes: the 24th Report* (London: Sage, 2008), 105-125; J Rayner et al, 'Public Service Ethos: Developing a Generic Measure' 21 (2010) *Journal of Public Administration Research and Theory* 27-51; Localis and Grant Thornton, *A New Public Service Ethos*, 2016, available at: https://www.grantthornton.co.uk/globalassets/1.-member-firms/united-kingdom/pdf/publication/2016/a-new-public-service-ethos.pdf (accessed 10 June 2019).
[37] Ruth Dixon and Christopher Hood, *A Government that Worked Better and Cost Less?* (OUP, 2015) 3
[38] Classically, Christopher Hood, 'A Public Management for All Seasons?' (1991) 69(1) *Public Administration* 3-19. See also Stephen P. Osborne, 'The New Public Governance?' 2006 (8)3 *Public Management Review* 377-387.
[39] Critically, Ruth Dixon and Christopher Hood, *A Government that Worked Better and Cost Less?* (OUP, 2015).
[40] M Lee, *Bureaus of Efficiency: reforming local government in the progressive era* (Milwaukee: Marquette University Press, 2008); Mark R. Rutgers and Hendriekje van der Meer, 'The Origins and Restriction of Efficiency in Public dministration: Regaining Efficiency as the Core Value of Public Administration' (2010) 42(7) *Administration & Society* 755-779; Azhar Manzoor, 'A Look at Efficiency in Public Administration: Past and Future' (2014) 34(4) *SAGE Open* 1-5.
[41] See Oliver Hart, 'Incomplete Contracts and Public Ownership: Remarks, and an Application to Public-Private Partnerships' (2003) 113(486) *Economic Journal* C69-C76.
[42] Oliver E. Williamson, 'The Economics of Governance' (2005) 95(2) *American Economic Review* 1-18, 6.

inspirations and human perceptions',[43] drawing on professional incentive structures within public organisations that are different from those of the market.

It also helps overcome problems of incomplete contracting in conflict situations where expensive re-negotiation of public outsourcing contracts becomes necessary and re-internalisation might be required (discussed in more detail in chapter 3). And there will be situations for example where only the public sector might be capable of addressing false economies that contracting might create where, by saving on the delivery of a specific service by outsourcing it, the state indirectly creates costs somewhere else within the public sector, often as a consequence of the fact that private providers are neither concerned about systemic efficiencies or distributional issues at the macro (societal) level: for example where a repression of wages within provider organisations as a result of privatisation creates pressure on the benefit system and more public service workers must rely on welfare to make up for wage losses.[44]

The question, finally, is whether in empirical terms outsourcing markets are competitive enough to deliver allocative and productive efficiency. Evidence on this point cuts both ways but certainly in the UK, concern has risen in recent years – just as outsourcing failures have accumulated – that these market mechanisms tend to work rather imperfectly in reality, in particular where they are not subjected to effective governance mechanisms; and that those imperfections tend to undermine efficiency. For some important supply markets, providers tend to operate as oligopolies that are not cost-effective because certain operators accumulate large numbers of contracts (often concentrating on those of greater scale and higher value).[45] The danger is that this accumulation places them in a relationship of heightened bargaining power vis-à-vis the public sector, increasing the chances of opportunistic behaviour and diminishing the practical possibilities for the public sector to counteract or discipline them. In these situations, ensuring that the delivery of the public service is managed in the public interest and not for the financial benefit of the private provider can become impossible or exceedingly costly.[46] It effectively turns the state's buying buyer on its head, producing situations where the 'government and other public agencies [are], in effect, pleading with firms to "please, accept us as your consumers!"'.[47]

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[43] Azhar Manzoor, 'A Look at Efficiency in Public Administration: Past and Future' (2014) 34(4) *SAGE Open* 1, 1.
[44] Amy Ludlow, *Privatising Public Prisons: Labour law and the public procurement process* (Oxford: Hart Publishing, 2015).
[45] Social Enterprise UK, *The Shadow State: A Report About Outsourcing of Public Services* (2012) available at https://www.socialenterprise.org.uk/the-shadow-state-a-report-about-outsourcing-of-public-services, 2012 (accessed 31 January 2019); National Audit Office, *The Role of Major Contractors in the Delivery of Public Services* (2013) available at: https://www.nao.org.uk/wp-content/uploads/2013/11/10296-001-BOOK-ES.pdf (accessed 31 January 2019); Abby Innes, First-best-world economic theory and the second-best-world of public sector outsourcing: the reinvention of the Soviet Kombinat by other means, *LEQS Paper No. 134/2018*, May 2018, available at http://www.lse.ac.uk/european-institute/Assets/Documents/LEQS-Discussion-Papers/LEQSPaper134.pdf (accessed 18 January 2019); Institute for Government, *Government Outsourcing: What has worked and what needs reform?*, September 2019, available at https://www.instituteforgovernment.org.uk/sites/default/files/publications/government-outsourcing-reform-WEB.pdf (accessed 7 December 2019).
[46] National Audit Office, *Managing government suppliers*, HC 811 Session 2013-14 12 November 2013, available at https://www.nao.org.uk/wp-content/uploads/2013/11/10298-001-Governments-managing-contractors-HC-811.pdf (accessed 4 July 2018).
[47] Colin Crouch, *The Strange Non-Death of Neoliberalism* (Polity Press 2011) 85.

In view of its own capacity constraints, the temptation is for the state to resort to a small pool of (large) private contractors, leaving high entry barriers for other providers. But this not only exposes it 'to huge delivery and financial risks should one of these suppliers fail.'[48] It is also troubling to consider this phenomenon in the context of regulatory capture where outsourcing decisions, driven by a logic of savings or to externalise the burden linked to the administration of public contracts, can easily lead the state to choose "strategic providers" or "intelligent procurement advisors"[49] that end up determining important aspects of the delivery of public services with limited accountability. Under these circumstances, and given distorted market competition and inadequate tendering mechanisms, the private sector's incentives are high-powered only in theoretical terms. In practice, they are unlikely to deliver allocative and productive efficiency where the lack of effective competition renders these large private firms vulnerable to the same or similar x-inefficiencies as public corporations or bureaucracies.[50] Operating in a position of economic strength, relatively shielded from competition (due to high barriers to market entry) and in the knowledge of the state's dependency given its responsibilities as a provider of last resort, the danger is that they begin to resemble 'the separated-at-birth twin to the Soviet [state-owned] "Kombinat" business group' rather than improving public services as 'efficiency-achieving, value-creating innovators.'[51]

In sum, views on the role of markets and on what they are capable of are clearly a contested and challenging part of any decision on the private delivery of public services. For some, as we have seen, the advantages of competitive over integrated structures can clearly justify an 'in principle' preference for private delivery. British policy from the 1980s and 1990s where competitive tendering became compulsory first and strongly encouraged later, has often reflected or leant towards this perspective. But others emphasise that both sides of the argument are conceptually sound and backed up by empirical evidence; that these choices therefore require a balanced assessment, even if this may come at the price of a less tidy and prescriptive policy and commissioning framework.[52] Occasionally, the benefits of privatisation will be clear-cut but, at other times, they require a more cautious approach based on 'a strong sense that the public realm is different from that of the commercial sector'.[53]

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[48] House of Commons Committee of Public Accounts, *Contracting Out Public Services to the Private Sector*, 47th Report of Session 2013-14, 14 March 2014, p. 8, available at: http://www.publications.parliament.uk/pa/cm201314/cmselect/cmpubacc/777/777.pdf?utm_source=rss&utm_medium=rss&utm_campaign=contracting-out-public-services-to-the-private (accessed 2 May 2017).

[49] House of Commons, Committee of Public Accounts, *Strategic Suppliers*, 58th Report of Session 2017–19, available at https://publications.parliament.uk/pa/cm201719/cmselect/cmpubacc/1031/1031.pdf (accessed 29 May 2019).

[50] On the issue whether competition or ownership is the key criterion, see Simon Domberger and Paul Jensen, 'Contracting Out by the Public Sector: Theory, Evidence, Prospects' (1997) 13(4) *Oxford Review of Economic Policy* 67-78, 75 (they argue that competition is 'the key').

[51] Abby Innes, First-best-world economic theory and the second-best-world of public sector outsourcing: the reinvention of the Soviet Kombinat by other means, LEQS Paper No. 134/2018, May 2018, p. 27, available at http://www.lse.ac.uk/european-institute/Assets/Documents/LEQS-Discussion-Papers/LEQSPaper134.pdf (accessed 18 January 2019).

[52] Tony Bovaird, 'The ins and outs of outsourcing and insourcing: what have we learnt from the past 30 years?', (2016) *Public Money and Management* 67-74, 69.

[53] Gerry Stoker, 'Public Value Management: A New Narrative for Networked Governance?' (2006) 36 *The American Review of Public Administration* 41-56, 46.

## Service quality and innovation

Outsourcing is linked not only to cost savings but also to delivering better and more innovative service solutions. It is viewed as a way not only of gaining access to private resources to boost public capacities, but also to ensure that these resources serve to improve service quality because outsourcing encourages clearer planning and specification of these service elements. By allowing multiple and different provider organisations to have a "voice" in how the service might be delivered (and the state to have a choice of who should deliver it), it enhances innovation and experimentation, including in the areas of technology, research and development, knowledge and data, organisational design etc. This involves using contracts as 'smart' or strategic tools to ensure the market delivers the best range of public benefits when providing the services in question.[54]

In this way, outsourcing is seen as an instrument to orient services towards outcomes and away from traditional but potentially ineffective delivery structures.[55] Public contracts may be designed not just to secure short-term service outputs but to deliver a long-term impact on public communities, as is now widely encouraged for example in British public commissioning policies or strategies: contracting authorities are first expected to identify the wider changes they want to see happening in their communities over an extended period of time; and then to develop a path, through their service commissioning and procurement strategies, to see those changes happen.[56] We may think of a publicly funded youth club by way of example. The service output - how many club sessions are delivered to how many attendees etc. – may be relatively straightforward to define and measure but, as such, it tells us nothing about the anticipated impact of its delivery on attendees or the wider community. Focusing the outsourcing on long-term outcomes (impact) on the other hand would include not just a quantitative account of youth club sessions delivered, but also as assessment related to its overarching objectives, e.g. of reducing youth crime or improving social cohesion in the relevant community. This may be harder to specify contractually, not least because it would also require a mechanism of monitoring the progress towards such impact. Assessment and monitoring can be difficult because outcomes are also usually not generated solely through one mechanism (the youth club) but have to do with a broader (and sometimes unobservable) set of public interventions (eg benefit management, policing, etc). However, these difficulties notwithstanding, this approach has the potential advantage of targeting the concrete public good that the state is determined to provide.

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[54] See eg Elisabetta Iossa,Federico Biagi and Paola Valbonesi, 'Pre-commercial procurement, procurement of innovative solutions and innovation partnerships in the EU: rationale and strategy' (2017) 27(8) *Economics of Innovation and New Technology* 730-749. See also Bart Lenderink, Hans Voordijk, Joop Halman and André Dorée, 'Public procurement and innovation: A conceptual framework for analysing project-based procurement strategies for innovation' (undated) available at https://bit.ly/34nmi48 (accessed 13 December 2019).

[55] Tony Bovaird and R. Davis, 'Outcome-based service commissioning and delivery – does it make a difference?' in S. Groeneveld and S. van de Walle (eds.), *New Steering Mechanisms in Public Management* (Emerald, 2011); see also Barber Review, *Delivering better outcomes for citizens: practical steps for unlocking public value* (2017) available at https://www.gov.uk/government/publications/delivering-better-outcomes-for-citizens-practical-steps-for-unlocking-public-value (accessed 4 July 2018); New Economics Foundation, *Commissioning for Outcomes and Co-production*, 2014, available at https://neweconomics.org/2014/06/commissioning-outcomes-co-production (accessed 18 January 2019). Indeed, the first principle in the Good Governance Standard for Public Services prepared by the Independent Commission on Good Governance in Public Services in 2004 enunciated that 'Good governance means focusing on the organisation's purpose and on outcomes for citizens and service users'; available at https://www.jrf.org.uk/sites/default/files/jrf/migrated/files/1898531862.pdf (accessed 4 July 2018).

[56] Toby Blume and Anna Randle*, Social Value: A Commissioning Framework, Pt. 1: Lessons from Lambeth*, Collaborate and Transition Institute (www.collaboratei.com); New Economics Foundation, *Commissioning for Outcomes and Co-production: A Practical Guide for Local Authorities*, 2014 (www.neweconomics.org)

A related benefit can be seen in the growing use of "social value" obligations in public contracts to ensure that their delivery is linked to secondary measures and regulatory objectives that the state considers worth promoting.[57] These target elements that are incidental to the service in question but add important qualities in their own right – delivering a form of dynamic efficiency to ensure that the provision of public services helps support long-term, systemic and innovative policy solutions to a range of political concerns: from equality and non-discrimination rights,[58] environmental obligations and sustainability, to industrial strategy or social and employment policies.

There are clear links to legal debates in the area of public procurement and commissioning on the leveraging of public expenditure to achieve secondary goals including the critical question to what extent these practices can or should be permissible under public procurement law.[59]

In the UK, the introduction of the Public Services (Social Value) Act 2012 has brought an additional legislative dimension to this approach, accentuating both its benefits and some tensions.[60] In its current form, the Act requires public authorities, including local and central government as well as NHS commissioning bodies and housing associations, to consider the 'economic, social and environmental well-being of the relevant area' before they procure major public service contracts.[61] So far, the legislation applies only to public service contracts above the EU procurement thresholds, and it does not (yet) impose an obligation to act upon these considerations.[62] But by directing them to reflect on both the economic and non-economic benefits of the services they commission, it encourages an approach to commissioning and procurement that looks closely at outcomes as well as service processes, where the benefits of how an activity is delivered and who is involved in its delivery, are taken into account alongside the value of what is actually being delivered (the service output). These benefits may be very tangible, such as creating local jobs or training opportunities for disadvantaged social groups or reducing the carbon footprint of the local economy.[63] Others are softer and less immediately measurable, for example the social benefit of generating greater community

[57] See e.g. the discussion by Joshua Pritchard and Rose Lasko-Skinner, *Please Procure Responsibly. The state of public service commissioning* (March 2019) 23-26, available at https://reform.uk/sites/default/files/2019-03/Public%20Service%20Procurement_AW_WEB.pdf (accessed 29 May 2019).

[58] See Christopher McCrudden, *Buying Social Justice: Equality, Government Procurement and Legal Change* (Oxford: OUP, 2007)

[59] Sue Arrowsmith, 'Horizontal Policies in Public Procurement: A Taxonomy' (2010) 10(2) *Journal of Public Procurement* 149-186. For in-depth discussion of the use of procurement to achieve goals of labour regulation, see the contributions to A Sanchez-Graells (ed), *Smart Public Procurement and Labour Standards. Pushing the Discussion after* RegioPost (Hart 2018). For discussion regarding environmental and other social considerations, see Sue Arrowsmith and Peter Kunzlik (eds), *Social and Environmental Policies in EC Procurement Law. New Directives and New Directions* (CUP 2009). See also Albert Sanchez-Graells, 'Truly competitive public procurement as a Europe 2020 lever: what role for the principle of competition in moderating horizontal policies?' (2016) 22(2) *European Public Law* 377-394.

[60] Nina Boeger, 'Reappraising the UK Social Value Legislation' (2017) 37(2) *Public Money and Management* 113-124.

[61] Section 1(3) Public Services (Social Value) Act 2012

[62] Cabinet Office, *Social Value Act Review*, February 2015, p. 13 (www.gov.uk). Note that in 2018, government ministers announced that the Act will be extended to include obligations on central government departments to explicitly evaluate, rather than merely consider, social value, se https://www.gov.uk/government/news/government-announces-major-changes-to-rebuild-trust-after-carillion-25-june-2018 and https://www.thirdsector.co.uk/minister-promises-extend-scope-social-value-act/policy-and-politics/article/1485898 (both accessed 9 December 2019). The consultation on this is currently under consideration, see https://www.gov.uk/government/consultations/social-value-in-government-procurement.

[63] See eg Lucca Ratti and Ester Villa, 'The Protection of Employment in European Procurement Law and the Role of Domestic Implementation' (2018) 4 *Critical Quarterly for Legislation and Law – KritV* 361-375.

cohesion and engagement, local accountability and potentially safer communities a service might deliver when involving local organisations and residents.[64] In the example above relating to a (hypothetical) youth programme, all of these might be considered relevant: the contract and tender might for instance specify terms related to strengthening community cohesion or local employment for young offenders, for example.

All this conveys an understanding of private delivery as a conceptually and empirically tested instrument for improving the overall quality of public services, at least where it is smartly executed. The concern is, on the other hand, that having to parcel up the complexity of a public service and its broader social impact in a tightly specified contract can have the opposite effect of distorting service outcomes and ultimately of reducing their quality. This is hardly an environment that fosters innovation. Instead, it goes some way to explain the unsettling evidence that many commissioners still seem to approach outsourcing predominantly as a means of cutting cost – in terms of short-term cost savings – rather than to improve long-term service quality. Empirical evidence illustrates this for the US[65] and it is a trend also seen in Britain where, notwithstanding the recent social value legislation, public commissioning bodies at all levels (but especially at central government level) are still widely criticised for prioritising price over quality.[66]

Outsourcing raises clear difficulties in the drafting and management of outsourcing contracts when services become, at least partially, non-contractible (also discussed in chapter 3).[67] To keep things contained and manageable, the state might choose to concentrate the contract on those service elements which are relatively simple to deliver and that produce relatively direct effects. So it might fix, in the contract specifications, on a 'quantitative summary'[68] of those activities which it considers will immediately satisfy tangible public needs – considerations such as how many patients are expected to be treated, lessons to be provided, bins to be emptied, roads to be built etc. To do so has the advantage of making the services in question more straightforward to specify and to provide but, by way of drawback, it often results in rather narrow and rigid services design that is not necessarily effective at satisfying, or even identifying, all existing public needs, especially in settings where these are more demanding.

The risk is that this prioritises rather formulaic delivery models that tend to parcel-up services (creating "silos") but cannot cope with more uncertain and complex public needs, especially with qualitative service elements that are too "fuzzy" to measure in rigid, quantitative terms. By way of

[64] London Borough of Croydon, *Inspiring and Creating Social Value in Croydon: A Social Value Toolkit for Commissioners* (www.croydon.gov.uk)

[65] Wendy Netter Epstein, 'Contract Theory and the Failures of Public-Private Contracting' (2013) 34 *Cardozo Law Review* 2211-59, 2240.

[66] E.g. G L Sturgess, *Just Another Paperclip? Rethinking the Market for Complex Public Services - A Report to the Business Services Association*, p. 9, 31 March 2017, available at http://www.bsa-org.com/wp-content/uploads/2017/04/Just-Another-Paperclip-FINAL.pdf (accessed 29 May 2019); House of Commons, Public Administration and Constitutional Affairs Committee, *After Carillion: Public sector outsourcing and contracting*, HC 748, published on 9 July 2018, p. 3. A government-commissioned review of the UK social value legislation for example found that while many authorities are aware of its provisions and open to considering social value, far fewer have put in place strategies or policies to follow through on these considerations or have firmly embedded social value into their commissioning cycles and the structure of their organisation. See Cabinet Office, *Social Value Act Review*, February 2015 (www.gov.uk)

[67] Oliver E. Williamson, 'The Economics of Governance' (2005) 95(2) *American Economic Review* 1-18, 14; Simon Domberger and Paul Jensen, 'Contracting Out by the Public Sector: Theory, Evidence, Prospects' (1997) 13(4) *Oxford Review of Economic Policy* 67-78, 71.

[68] New Economics Foundation, *Commissioning for Outcomes and Co-production*, 2014, pp. 7-8, available at https://neweconomics.org/2014/06/commissioning-outcomes-co-production (accessed 18 January 2019)

example, we may think of the difficulties of setting out a comprehensive *ex ante* definition of what might, or might not, constitute a "good" or "decent" level of social care.[69] It is hardly possible to anticipate all personalised aspects of care services, especially as needs might change over time.[70] It is possible to try instead to use proxies or indicators as a way of measuring their delivery in reasonably quantifiable terms, but it risks overlooking that a wider set of public values e.g. related to trust,[71] morality,[72] community responsibility or a public interest ethic,[73] are clearly relevant to securing public needs are fully met. Cost-effectiveness here remains quintessentially a political issue – what is (qualitatively or quantitatively) "better" always remains fundamentally open to political contestation which means it has to be widely understood and assessed. Only a comprehensive, and more flexible, service definition might be capable of accommodating those wider elements, but it has the drawback of introducing greater complexity and uncertainty at the point of designing the service in question and monitoring (measuring) its delivery.

The danger is that eventually, the public service is narrowed down to those quantitative dimensions that are easy to measure and monitor, and which the state can quite easily contract-out to the private sector. Such a narrow approach to contracting however is unlikely to generate dynamic efficiencies by pursuing opportunities to incorporate secondary regulatory objectives. Instead it risks creating false economies by producing indirect costs for the state elsewhere, as narrow contracts cannot guard against slipping service standards or exploitation e.g. where private providers, by cutting service quality (directly or by squeezing their supply chains), manage to lower their own cost while passing externalities onto the state.[74] This is a theme we will return to in chapter 3.

## Democracy and accountability

A powerful normative concern with outsourcing is that shifting from public to private delivery might give rise to serious 'practical problems and deficiencies in legal accountability and control'.[75] In an in-house structure, (frontline) service providers are subject to direct, hierarchical state control and public legal accountability. Private delivery, on the other hand replaces those structures with indirect forms

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69 Mats Bergman, Sofia Lundberg and Giancarlo Spagnolo, *Public Procurement and Non-contractible Quality: Evidence from Elderly Care*, Umeå Economic Studies 846 (Umeå universitet, 2012), available at: http://sh.diva-portal.org/smash/get/diva2:809601/FULLTEXT02.pdf (accessed 23 January 2019).

70 Oliver E. Williamson, 'The Economics of Governance' (2005) 95(2) *American Economic Review* 1-18, 14.

71 R C Nyhan, 'Changing the Paradigm: trust and its role in public sector organisations' (2000) 30 *American Review of Public Administration* 87-109.

72 M Lee, *Bureaus of Efficiency: reforming local government in the progressive era* (Milwaukee: Marquette University Press, 2008), p. 44.

73 A Ludlow, *Privatising Public Prisons: Labour law and the public procurement process* (Oxford: Hart Publishing, 2015) 82, with references to further literature.

74 Oliver Hart, Andrei Shleifer and Robert Vishny, 'The Proper Scope of Government: Theory and an Application to Prisons' (1997) 112(4) *Quarterly Journal of Economics* 1127-1161, p. 1128.

75 Peter Vincent-Jones, *The New Public Contracting: Regulation Responsiveness, Relationality* (Oxford University Press 2006) vii. For extensive literature, see e.g. M Freedland, 'Public law and private financing: placing PFI in its public law frame' (1998) *Public Law* 288-307; J Boston, 'Inherently Governmental Functions and the Limits of Contracting Out', in *idem* (ed), *The State Under Contract* (Bridget Williams 1995); Jody Freeman and Martha Minow (eds), *Government by Contract: Outsourcing and American Democracy* (Harvard University Press 2009); Rebecca L Keeler, 'Managing Outsourced Administrative Discretion', (2013) 45(3) *State & Local Government Review* 183-188; Stephen Wilks, *The Public Service Industry: A constitutional blasphemy and a democratic perversion*, 2013, available at: http://www.democraticaudit.com/2013/08/11/the-public-service-industry-a-constitutional-blasphemy-and-a-democratic-perversion/ (accessed 21 January 2019); *cf.* Stephen Parker, *Those who argue outsourcing endangers accountability are still fighting the last war*, 2013, available at http://www.democraticaudit.com/2013/09/06/those-who-argue-outsourcing-endangers-accountability-are-still-fighting-the-last-war/ (accessed 21 January 2019).

of public accountability and private governance mechanisms. The worry is that while this may serve to strengthen public capacity and improve efficiency, it potentially sidesteps traditional public law doctrines concerned with the 'substantive legality and procedural regularity of government action' as foundation of the rule of law.[76] Such an impact on democracy and the 'proper role of the state' would be unacceptable.[77] From this perspective, outsourcing therefore is seen as legitimate only where it can be done without undermining these public norms, even if it comes at a price of lower cost-effectiveness. Even where it is less economically efficient to run services in-house than privately, politically it might be a worthwhile price for the state to pay for maintaining a system of public accountability intact.[78]

It should come as no surprise, on the other hand, that economic perspectives tend to not share the same public law concerns. They tend instead to be more positive about the relationship between private delivery and political democracy – and at the same time more critical of public bureaucracy's ability to ensure genuine accountability. From this point of view, conceptually speaking, outsourcing is seen as a neutral mechanism on substantive issues of accountability: having privatised the delivery of public services, the state remains accountable for their provision, regardless of whether it chooses a direct or indirect form of delivery. In other words, private governance merely steps in as an additional control mechanism while the public authority continues to be subjected to usual forms of accountability.[79] Outsourcing tends to improve our understanding of the cost and content of the services in question by requiring their specification in a tender and contract – preventing public authorities for example from "burying" them in public charters or budget documents.[80] It brings a minimum of clarity to the structural division of responsibilities and roles. In short, provided it is effectively managed, private delivery (and governance) incorporates additional tools to strengthen transparency that public administration alone may be less able to supply. In fact, traditional public bureaucracy tends to be scrutinised for having quite the opposite effect: a risk of obfuscating democratic channels of accountability and creating administrative power away from directly legitimated political institutions - making things not more, but less transparent and potentially more expensive. [81]

In empirical terms, then, the question is which of these perspectives has greater practical value, according to the evidence: is outsourcing more likely to lead to a loss of accountability, or is it a neutral or even positive mechanism? To what extent can it broaden out those layers of control (due process) and transparency that public structures might be less able to provide? The evidence is mixed. One

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[76] Jody Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116(5) *Harvard Law Review* 1285-1352, 1302.
[77] Simon Domberger and Paul Jensen, 'Contracting Out by the Public Sector: Theory, Evidence, Prospects' (1997) 13(4) *Oxford Review of Economic Policy* 67-78, 68.
[78] Jody Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116(5) *Harvard Law Review* 1285-1352, 1301. See also Marc Cowling, 'Measuring public value: The economic theory' (2006) Work Foundation Papers, available at https://pdfs.semanticscholar.org/1aaa/e3662d6a1738850c0da6ae1ad296e245b015.pdf (accessed 28 November 2019), p. 31: 'people may value democracy and fairness, even if it means they lose out in a strictly economic sense.'
[79] Simon Domberger and Paul Jensen, 'Contracting Out by the Public Sector: Theory, Evidence, Prospects' (1997) 13(4) *Oxford Review of Economic Policy* 67-78, 76.
[80] I Kirkpatrick *et al.*, 'Un-charted territory? Experiences in the purchaser-provider split in local authority children's services' (1999) 29 *British Journal of Social Work* 707-726.
[81] Classically, John Stuart Mill, *On Liberty* (1859).

study, while not offering much empirical support to back this, insists that 'experience has shown that contracting need not reduce public-sector accountability, only the way in which it manifests itself.'[82] Recent evidence in the UK on the other hand tends to support a more critical view. Here, concerns have been raised for example whether levels of accountability imposed on key providers are sufficient to match their market power because 'the general level of transparency over contractors' cost and profits is limited,'[83] and while 'contracts are a matter of public record, it is usually impossible to find out key details like how much profit is built into each one.'[84] We will return to these issues in chapter 4.

## Conclusion

Decisions to outsource a public service always include highly technical elements (what aspects to privatise, how to structure the tender process and contract documentation etc.) alongside more normative observations (or assumptions) about the role of markets and the state, about public sector capability or the motivations of private economic actors, to name but a few.[85] There is always a possibility or risk that these decisions will be taken 'mechanistically and on ideological grounds rather than because they offered the most appropriate services'.[86] Some may be a political avoidance strategy where, by outsourcing, the 'government can point its finger at the private entity to avoid political backlash' should services slip or fail.[87] However, in this chapter we focused on cost-effectiveness, allocative and productive efficiency (usually understood in terms of long-term savings and improved service outcomes) as by far the most prominent driver for these decisions, especially in a context of political austerity and public cost-cutting pressures. In choosing between public and private delivery, commissioning authorities are looking for 'more efficient service delivery while

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[82] Simon Domberger and Paul Jensen, 'Contracting Out by the Public Sector: Theory, Evidence, Prospects' (1997) 13(4) *Oxford Review of Economic Policy* 67-78, 76, italics added. We note that the authors offer little (if any) evidence in their study for what such experience has looked like.

[83] National Audit Office, *The Role of Major Contractors in the Delivery of Public Services*, available at: https://www.nao.org.uk/wp-content/uploads/2013/11/10296-001-BOOK-ES.pdf, presented to the House of Commons on 12 November 2013, p. 10 (accessed 31 January 2019).

[84] Social Enterprise UK, *The Shadow State: A Report About Outsourcing of Public Services*, 2012, available at https://www.socialenterprise.org.uk/the-shadow-state-a-report-about-outsourcing-of-public-services, 2012, p. 12 (accessed 31 January 2019).

[85] This is, perhaps, particularly clear in the context of the current debate of the legislative proposals aimed at delivering the NHS Long Term Plan, targeting a fundamental reregulation of NHS procurement. See House of Commons, Health and Social Care Committee, *NHS Long-term Plan: legislative proposals*, Fifteenth Report of Session 2017–19, 24 June 2019, available at https://publications.parliament.uk/pa/cm201719/cmselect/cmhealth/2000/2000.pdf (accessed 11 December 2019). For an overview of recent trends in this area, see Marie Sanderson et al, 'New Models of Contracting in the Public Sector: A Review of Alliance Contracting, Prime Contracting and Outcome-based Contracting Literature'(2018) 52(5) *Social Policy and Administration* 1060-1083; Albert Sanchez-Graells, 'Centralisation of procurement and supply chain management in the English NHS: some governance and compliance challenges' (2019) 70(1) *Northern Ireland Legal Quarterly* 53-75.

[86] Tony Bovaird, 'The ins and outs of outsourcing and insourcing: what have we learnt from the past 30 years?', (2016) *Public Money and Management* 67-74, 68.

[87] Wendy Netter Epstein, 'Contract Theory and the Failures of Public-Private Contracting' (2013) 34 *Cardozo Law Review* 2211-59, 2242.

adhering to numerous and sometimes conflicting mandates from higher levels of government' that may relate to a range of quantitative and qualitative service aspects.[88]

We have seen that these decisions are complex and arguments for private delivery often sit very close to their counterarguments. This is messy and contested terrain, both at the normative and contextual level, and in the light of these complexities, the recurrence of outsourcing failures in Britain (and elsewhere) becomes perhaps less surprising. The important point, which we sought to contextualise throughout this chapter, is that notwithstanding these failures, the state's welfare ambitions today mean that outsourcing is not a transient phase but necessary in order to address capacity constraints and to draw on other advantages that it brings. It is essential for the state to integrate private actors into service delivery to strengthen its own capacities, but without undermining politically identified public needs (because the outsourcing relationship is controlled through the contract). Without outsourcing, and given current capability limitations, the state would lack the capability to deliver ambitious welfare programmes to its citizens: there is a partnership of mutual ambition between state and private sector in all mixed economies. Inescapably (at least in the medium-term), therefore, questions arise of how to maximise these benefits of such a partnership while avoiding its failures. We might begin addressing these questions by focusing on the governance instrument at the very heart of the outsourcing process, namely the public contract.

[88] Jody Freeman, 'Extending Public Law Norms Through Privatization' (2003) 116(5) *Harvard Law Review* 1285-1352, 1295.