Effects of privatization and competitive tendering on local government - a comparative study

Preliminary project description

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Introduction
Since the last regional and local elections in the fall of 1995, the interest in Norway for using market-like mechanisms in local government has increased notably. This represents a marked change in political climate that can partly be traced back to the progress made by a rightwing liberal party (Fremskrittspartiet) at the local elections in 1995. Their progress also seems to reflect more basic and general long range changes in public opinion, triggered by the downfall of the Berlin Mauer and the Soviet Empire. But perhaps the most important factor now at play is increased public poverty at the regional and local level. The lack of money will become acute in 1999, according to reports from local government officials. Local politicians are even threatening to leave their positions in protest. In this situation increasing numbers of politicians and administrators argue that privatization and competitive tendering will ameliorate the economic crisis. This question will probably become one of the most heated topics before the next local and regional elections in 1999. The biggest trade union for local government employees in the country, Norsk kommuneforbund, has already declared that the struggle against privatization and competitive tendering will be their first priority in the year to come.

Much attention in the domestic and international research on privatization and competitive tendering has been focused on the economic effects: did local government save money, and in case how much?

In this study, however, attention will be turned in another direction. I want to look at the effects of introducing market-like mechanisms in local government on local government itself. I suppose that these and other types of changes in working conditions, in environmental pressures etc. stimulate adjustments or major transformations in organizational processes, structures, and cultures. These adjustments and transformations are important to study because they in their turn effect distribution of attention and priorities within local government. The big question is if organizational changes in the wake of privatization and competitive tendering strengthen or weaken the ability of local government to be what it is meant to be: a democratic institution for making and implementing collective and authoritative political decisions and for providing collective goods to its local population. In Norway, local government plays at least three important roles: (1) as political arena, (2) as service producer, and (3) as agent for the national government. The legitimacy of local government depends on its ability to fill these roles. More specifically its legitimacy is heavily dependant on its ability to make some basic values become real: political participation (democracy), local autonomy, local identity and attachment, justice and equality, and effectiveness and efficiency. The ranking of these values is not stable. They are given different weight over time and by different groups in society. For instance today, effectiveness and efficiency are generally given much higher priority than local autonomy and democracy (Rose and Skare 1996, Pettersen and Rose 1997, Torsteinsen 1998). How then will the ability of local government to fulfil its roles in society, and to realize the basic values, not only one or two, but all of them, be effected by organizational changes in the wake of privatization and competitive tendering? Are these changes neutral in their effects, or will they for instance systematically favour effectiveness and efficiency at the expense of democracy? How will the accompanying rhetoric of the market and idolization of the firm effect local government identities and cultures? What about the long term consequences?

One important development that can be expected in the wake of marketization of local government is the establishment of autonomous or semi-autonomous service-producing units. Some of these units will work clearly within the limits of local government while others will be organized as municipal limited companies. In addition, of course, we have regular private
firms working for local government. They are, at least in principle, totally independent. How will this development influence the ability of local government to govern? Will there be a change from hierarchical to contractual management? How will this change influence the position and status of local councillors? Will they become more removed from the daily work of local government, concentrating on strategic issues? Or will a more distant position lead to loss of political interest and even bigger problems with recruitment than today? How will the relationship between local councillors and local bureaucrats develop on this background? These and other questions need to be asked when privatization and competitive tendering is on the local agenda. Even if effectiveness and efficiency in local service production are important, legitimacy in local government has to do with more than that.

The paper is a preliminary project description, outlining a comparative empirical study in four or five different countries. My objective is to receive feedback from foreign colleagues and to get in touch with someone who might be interested in co-operating on the project.

The Research Problem
The purpose of the planned research is to find out (1) what changes take place in local government structures, processes, and cultures when privatization and competitive tendering are being introduced, and (2) what are the effects on local government’s ability to fulfil its ultimate mission in society and to gain legitimacy? The problem can be visualized by the model in figure 1.

![Model](image)

Figure 1

One first step in the elaboration of the model is to clarify the concepts or variables being used.

2.1 Privatization and competitive tendering
Privatization and competitive tendering were introduced in UK during the eighties by the new right movement and the Thatcher administration and gradually spread to the rest of Western Europe. While spreading the ideas became less ideological and more pragmatic and adapted to other political contexts. All the same, the use of markets mechanisms in public sector is still a controversial issue, stirring much heated debate, at least in Norway and other Nordic countries. Therefore, even the concepts themselves are carriers of controversy.

One of our ministers recently complained that “for some reason or the other those who prefer privatization don’t want to use the word privatization” (KRD-Nytt no. 2/98, p. 4). This example illustrates how important it is to clarify the concepts we are using.

In the international literature Savas is one of the first scholars who tried to write about privatization in more academic terms. In his book Privatizing the Public Sector (1982) he identified three roles in the service provision process: the arranging, the producing, and the financing roles. For the time being, let me then define privatization as the process whereby private actors take over one or more of the three roles from public sector. At the local level privatization is very much a question of opening up production to private actors.
actors can be both voluntary non-profit organizations and for-profit firms. The controversy of privatization, however, is mainly over the last type of actors, especially when their operation within the "soft" sectors is on the agenda. Many feel that making more or less dependant people like for instance the elderly, the mentally handicapped, and the children an object of commercial interests, is immoral.

Historically, care and education were the inventions and tasks of the church and other non-profit organizations (civic society, the third sector). Gradually, often in the wake of democratization, public authorities took over more and more of these tasks, defining them as a public responsibility. But even as recent as during the years 1946-86, Norwegian health care for instance, went through a process of further deprivatization. As much as one third of Norwegian health care (measured by working expenses) was still privately owned in 1986 (Hofoss 1987). The privatization we are witnessing today is not as much a process of reprivatization as a process of commercialization. Public services are not primarily brought back to the third sector, but are instead taken over by profit-oriented businesses. The historical process can be illustrated as in figure 2.

Figure 2

To sum up, privatization in Norwegian local government today means:

- Mixed public-private partnership in service provision, i.e. the arranging and the financing roles are still a public responsibility, while the producing role is contracted out to private actors.
- Commercialization, i.e. the private actors are profit-oriented businesses.

Privatization does not necessarily include competition. It is still rather usual for local authorities to give orders to private companies without competitive tendering or to grant private actors monopoly (for instance to doctors) for delivering public services within its territory. Therefore, when discussing the use of market mechanisms in local service production, it is useful to introduce competitive tendering as a supplementary concept to privatization. Competitive tendering emphasizes competition between two or more actors as the most important mechanism for producing better and cheaper services. Whether the producer is privately or publicly owned is of less importance. By combining the two concepts privatization and competitive tendering we can now identify four different forms of management regimes (or situations). Figure 3 may illustrates this (Jonsson 1991).

<table>
<thead>
<tr>
<th>Competition</th>
<th>Private management</th>
<th>Public management</th>
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<tbody>
<tr>
<td>Non-competition</td>
<td>A</td>
<td>B</td>
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<td></td>
<td>C</td>
<td>D</td>
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Figure 3

In the public debate conclusions about efficiency are often drawn on the basis of comparisons between A and D. A better and probably more fair way to judge the effects of private vs.
public management is to compare A and B, and C and D. On the other hand, if we want to study the effects of competition, we can do that by comparing A and C, and B and D. In any way, my main interest is not to evaluate efficiency, but to use the model to identify and compare general management regimes.

In square A we find the traditional free market model where firms have to compete with each other on the basis of price, quality and impression. The competition is about attracting customers and is ultimately a struggle for survival. In this process firms are disciplined to pay attention to the customer’s needs and preferences.

Square D shows the traditional public sector regime. Politicians try to satisfy their voters and administrators seek to satisfy their politicians. But since there is no price mechanism regulating demand, voters will (always) expect and ask for more supply of public services. Politicians expect the administration to do more for less while the administration wants to continue as before, or preferably do more for (much) more.

Square C illustrates a monopoly or oligopoly regime. Here we can classify the rather widespread practice of local government turning to specific private actors for services, investments etc. without any form of competition.

In square B local government has integrated competitive elements in its management practice, for instance by introducing a purchaser-provider or a citizen choice model. Local government institutions like for instance schools, kindergarten and community nursing have to compete with private actors for the assignment to deliver public services.

Sometimes it is difficult to know exactly how to classify a practice. When for instance a commune or a county wants to out-source some of its activity it could do that (1) by leaving it completely to the market, or (2) by establishing its own company. The first case definitely belongs to square A, whereas case 2 is less obvious. Establishing a municipal limited company could be seen as a square B practice. But at the same time, even though the company remains 100% publicly owned, it becomes an actor of the market regime, judicially speaking. This means it is no longer under the authority of the local government law (Kommuneloven). The members of its board will instead be held both individually and collectively responsible to the limited companies act (Aksjeloven), irrespective of what a local council might decide.

Besides outsourcing, communes and counties can buy production of public services from private companies. This means using competitive tendering and contracting out as public management practices. If we were to classify these practices according to our model, they would fit into both square A and B, dependant on where in the process we were. The danger is of course that the segment of the market directed towards producing public services might deteriorate into a monopoly (or oligopoly) regime, i.e. square C. This has happened or is about to happen in some local communities where market mechanisms have been in function for some time (Bogen og Nyen 1998). Maybe then the traditional public management regime (square D) has to be reintroduced to break a private monopoly? In that case we have to deal with a circular process.

This little exercise has hopefully illustrated that lumping the two concepts privatization and competitive tendering together, removes important nuances. Although some participants in the public debate argue that the concept competitive tendering is used to “steal” privatization in through the back door, experience does not support such an outright conclusion. In Thatcheristic Britain, for instance, 85% of the local government contracts set up after competitive tendering was introduced, went to municipal actors, whereas in social-democratic Sweden a majority of the contracts were won by private companies (Bogen og Nyen 1998).
2.2 Changes in local government

This is a rather broad variable that could be operationalized in different directions. Empirically we are talking about for instance purchaser-provider models, splitting the municipal organization in two. Within the provider part of the organization we also typically witness the establishment of business centers (resultatenheter). We are further talking about the use of contracts to manage private producers of public service. In addition, we find citizen choice models where the resource flow and ultimately the survival of both public and private service producers are being made dependant on where the citizens prefer to use their service checks.

In the more general and theoretical perspective the institutional environment of communes and counties seems to have become more demanding and complicated. Local government is met with tougher demands as to efficiency, service quantity and service quality, responsiveness etc. At the same time political and ideological environments have become more critical, in some cases even hostile, to public activity in general. Market liberalism has swept through most of Europe and seems for the moment to have little if any competition. In addition, the financial pressure on public sector has been considerable for several years, and the introduction of the EMU has and will certainly not make it any less. Up till now Norway has benefited from high oil prices, but recently they have fallen to an all time low. Therefore, Norwegian public sector is no longer in any better financial position than its Western European colleagues.

With more demanding and complicated institutional environments communes and counties seem to respond by developing more complex organizations. This observation is in line with both general theoretical reasoning (Scott and Meyer 1994) and empirical findings (Jacobsson 1994). If increased market orientation is triggering the same kind of organizational response, how could we then specify complexity?

First of all, local government seems to open up for greater institutional autonomy (Grønlie og Selle 1998). Departments, institutions and activities can be given different degrees of autonomy, ranging from traditional decentralization to complete outsourcing. In the last case a commune could for instance turn a hospital into a public limited company. This development opens up for a wide range of alternative organizational forms where the degree of attachment to the mother organization could differ very much. How far this could go before the idea of organizational unity breaks down is uncertain. The idea of unity is important because it helps create a common identity. Once that is lost the challenges to integrate the organization becomes higher. Competing identities will develop within the different more or less autonomous units and this could easily harm the overall objectives of local government. Increased autonomy will probably reduce the insight of the local councillors and the general public and possibly also of the municipal CEO. On the other hand, autonomy could mobilize institutional responsibility, innovation, and efficiency, reducing the need for detailed hands-on management from the top. Important questions can be raised in this connection. Are processes of increasing autonomy reversible, if results are poor? What if they are not? What about the role of the local councillors? Is it legitimate to limit or deny their access to information and decisions inside autonomous municipal units? If so, is it in accordance with our democratic ideals?

All in all, increased autonomy seems to create more complex local government organizations. In the longer time perspective, what could happen is the gradual transformation of local government into public corporations.
Another indicator of increased organizational complexity is the introduction of *contractual management* on a broad scale, side by side with the traditional hierarchical model. The use of contracts is certainly not new in local government, but the more widespread use of private producers of public services has lead to a marked increase in this practice. Communes and counties have little experience in managing the “soft” human-oriented services, i.e. education, health care, and social welfare through contracts. Important aspects may easily be lost out when contracts are set up and signed. How can they be brought back in, without creating unacceptable financial, judicial, practical, and human problems. The use of contracts may quite possibly lead to *less flexibility* in local government. Within a hierarchical organization changes and adjustment can be done continuously. With a contract running, things are more fixed for a given period of time. If changes and adjustments are wanted or needed, negotiations have to be initiated and the contract has to be revised. This will take time and it could influence costs. If there is a disagreement it is up to “the principle” (local government) to prove that “the agent” (the contracting partner) is wrong or not doing his job according to the contract. This could take more time and even include a lawsuit. The point I am trying to make here is that the popular conception of hierarchy as bad and inflexible and markets as good and flexible is not always correct. Within local government we will not know what is true before we gain more experience. Today experience seems to be rather ambiguous on this point.

Contractual management will also influence the kind of *competence* that is needed in local government. There will probably be an increase in the demand for judicial and economic expertise. There is also reason to expect that when these professions become more important in the organization their position and status will be enhanced and their influence will increase. How will the established, more operative professions, i.e. teachers, nurses and engineers react to this challenge? What relations will develop between the new professions on the one hand, and the political and administrative leadership on the other? Will they strengthen or challenge the executive level or what? How will this in turn effect the position and the influence of the local council and the local councillors?

One last question that could be raised is if this practice will eventually be used *within* local government itself. Will local government try to manage those of its institutions that have been granted autonomy in this way in the future? In other words, will contractual management gradually grow at the expense of hierarchical management?

The third and last indicator of growing complexity in the wake of marketization in local government is increased *formalization*. It is natural to assume that competitive tendering, contracting out (or in), and control of contracting conditions will lead to more detailed specifications, more rules and more paper. When contracting management substitutes hierarchical management what actually happens is that the flow of verbal and informal information, orders etc. is replaced by written and formal communication. Every change and adjustment is in principle a change in contracting conditions and therefore has to be dealt with formally. On the other hand, the *internal* processes of management are probably less bureaucratic and formalized in a private business than in public administration (Gabrielsen 1986). Therefore, when a private firm runs, for instance an elderly home on behalf of a commune, this might be done in a more flexible and less formal manner than in comparable public run institutions. More delegation to the institutional level and shorter lines of internal communication might explain this. The problem is the *interface* between local government and private business. It is the regulation of this relation through contracts that creates increased formalization.
Summing up, I have argued that the changes in local government in the wake of marketization can be associated with increased organizational complexity. I have tried to specify this increase in complexity by pointing at certain indicators: growing institutional and operative autonomy, and more widespread use of contractual management. As a result formalization has grown and flexibility has become less. Also, a new management profession is challenging both the established operative professions and the traditional political-bureaucratic management.

2.3 Effects on democracy, effectiveness etc.
How will changes in local government, triggered by marketization, effect its ability to function properly as political democratic arena, service provider, and agent for the national government? My basic assumption is that the legitimacy of local government depends on the degree to which it attends to these functions. By legitimacy I mean the willingness of people to accept the decisions made by public institutions. If local government is democratic, effective, efficient, equitable and just, etc. it will more easily gain the respect, confidence and support of its inhabitants, thereby building a reservoir of legitimacy. If it is not, the reservoir will gradually drain away, and when its is empty problems will accumulate.

It is not necessarily so that a commune or a county will reach high (or low) scores on all criteria of legitimacy. One could for instance imagine a commune with a high score on democracy and a low score on efficiency, or vice versa. The effect on the legitimacy of local government therefore, depends on (1) the total score on the different criteria, and (2) the weight attached to the different criteria by the public opinion at the time. Recent studies within local government show that efficiency and effectiveness are given high scores now, whereas autonomy and democracy receive low scores (Rose og Skare 1996, Rose og Pettersen 1997, Torsteinsen 1998).

In Norway there seems to be a rather widespread opinion that democracy and efficiency are somehow partly incompatible. This could be labeled a structural hypothesis. The solution according to this line of thinking is to identify and implement better organization models, securing a kind of optimization or satisficing. An alternative perspective could be called the cultural hypothesis. Here the answer is to be found in the civic culture of the local or regional community. Communes and counties with the “right” kind of culture will score high on all accounts, while those with the “wrong” culture will get low scores all over (Putnam 1993). If this is true, changes in organizational structures will be of minor importance. Effects on performance will be neutralized by the culture. In relation to the problem I am studying the structural hypothesis would be verified if we identify positive or negative effects on different performance (legitimacy) criteria. If instead the performance is approximately the same for all criteria, irrespective of changes in local government, this could be seen as a verification of the cultural hypothesis.

The effects of privatization and competitive tendering have almost exclusively been studied in relation to efficiency. It is perhaps not so strange if we consider that much of the driving force behind this marketization is financial pressure. It is also understandable when seen on the background that efficiency and effectiveness now are the most important factors for boosting local government legitimacy. In other words, it is local government as service provider that covers “the front page” of society right now. Although this is true, the focus of public opinion changes from time to time. Today efficiency and effectiveness are important, tomorrow democracy may be headline number one. This implicates that although the other
criteria of legitimacy are not at the forefront right now, they are not forgotten or insignificant. If any of them should be seriously threatened, people would probably protest and mobilize to protect them. In a study like this it is therefore necessary to evaluate the effects of local government changes on a broad scale, not only in relation to one set of criteria.

3. Theoretical perspective

Today the market seems to enjoy high and increasing legitimacy all over the world, also in Norway. With the downfall of the Berlin Wall in 1989 and the dissolution of Soviet Union in 1991 ideological competition has more or less disappeared. Compared to the strong support of state interventionism in most Western Europe after the Second World War, this represents literally speaking a political U-turn. But just as the majority 3-4 decades earlier trusted government almost without reservation, the situation now is that many people nourish perhaps unrealistic hopes and expectations as to what can be accomplished through the market. At the same time, today’s faith in the “goodness” of the market seems to be far more sober and pragmatic than the almost religious zeal that we could observe in some circles during the eighties. What remains though is that market liberalism has put it definite stamp on people and institutions in our society. It has introduced a normative and cognitive “regime” that is different from the state oriented “regime” that dominated the first 30 years after the war. As a consequence, local (and central) government is now operating within institutional environments that are much more positive to the market and much more sceptical to politics and the public sector than before. These environments influence conceptions of what is legitimate and what is not. Therefore, it is both possible and probable that local government now try to find solutions to their problems within these new normative and cognitive frames. When the market and the private firm are the models it is not hard to understand why privatization and competitive tendering are becoming more and more popular.

Anyone familiar with neoinstitutionalism within organization theory will already have recognized its influence on the perspective I have been trying to outline here (Røvik 1998, Scott 1995, Scott and Meyer 1994, Powell and DiMaggio 1991). Neoinstitutionalism offers a useful general perspective on the processes that we are observing. It sheds light on (1) why privatization and competitive tendering are becoming more and more popular, and (2) why local government changes its structures and procedures the way it does. But when it comes to evaluating the effects and instrumentality of organizational changes in local government, neoinstitutionalism is not specifically relevant or useful, except perhaps for studying symbolic effects. Therefore, I would like to see if Williamson’s transaction cost theory (1985) could fill this gap. The main focus of this theory is on what model is most rational in an economic sense, hierarchy or market. The criteria is the minimalization of transaction cost. I would like to widen this perspective to find out what is most rational according to the criteria of legitimacy, i.e. democracy, effectiveness etc. In other words, what makes local government function best as political-democratic arena, service provider, and as national agent? Hierarchy or market? If for instance hierarchy is best for the national agent function, and the market for the service provider function, what is best for the political-democratic function? A mixture?

4. How to conduct the survey?

In order to collect the necessary data I am planning to conduct a comparative survey in three or four countries besides Norway. The other countries are Sweden, Denmark, and UK. In
addition I would like to include one country on the continent. To make the study truly comparative I have to establish contact and co-operation with interested and dedicated colleagues from the respective countries. The number of communes to be included in the study could vary, but as I see it now it should for practical reasons be limited to two from each country. This will make it possible to study each case more in depth.

First step in this process will be to make a literary survey in order to develop the theoretical framework further and to plough deeper into empirical work that has already been done. After that the survey communes have to be selected, relations established, and whatever written material there is available has to be collected. Documents, position papers etc. will hopefully prove useful to map the formal organization and changes in it, proposals, reasoning and philosophies connected with this process etc. I have already started collecting documentary material form some Norwegian communes. Next step will be to set up an interview guide and maybe a questionnaire. Primarily these instruments should help me to uncover the effects of organizational change in or on local government, or rather the subjective conceptions of the effects among some of the participants. I also expect to find out something about the informal organization through these methods.

5. Conclusion

Norwegian local government now seems to be entering or has already entered a period of rapid and radical transition. The post-war “regime” characterized by widespread trust in politics and political authorities, is now being challenged by a growing support for the market “regime”. Traditional preferences for public solutions are giving way for increasing demands for private alternatives. We are witnessing an important and maybe historical transition in the public sector. What the effects will be, in the short and especially in the longer time perspective, we don’t know.

On this background it is not difficult to understand the heat in the public debate over privatization and competitive tendering in local government. First, we have the clash of interest between employees and employers. Local government employees are of course worried about what will happen to them and ultimately afraid to loose their jobs. Second, we are witnessing a cultural collision between the traditional professionalism within teaching and nursing and social welfare on the one hand, and the more business-like, efficiency-oriented management of the top executive staff on the other. It is service quality and equity against efficiency. This brings us over to a third point, the controversy over what emphasis to give to the different roles and values of local government. Opponents of the marketization, both within and outside local government argue that privatization and competition will make democracy suffer. The importance of local government as a political-democratic arena for collective debate and decision-making will be reduced. Supporters on their side argue that besides increased efficiency and effectiveness local government will become more responsive and more flexible. The argument seems to imply that the market is more democratic that representative democracy itself. Government has grown to much and must leave the citizens more to themselves.

In this study I will try to address some of these problems. By focusing on changes in local government and the effects of these changes I hopefully will be able to accomplish that.
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