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Contents

Practical Partnering – Making the Most of Complex Relationships

By Dilys Foster, Serco Government Services, with assistance from Gary L Sturgess, Serco Institute

1 Overview

Over the past two decades, the scale and complexity of public service contracts in the United Kingdom have grown significantly, so that the arm's length relationships that characterised early outsourcing contracts have been progressively replaced by sophisticated arrangements involving major risk transfer and complex service partnerships demanding a significant amount of risk sharing.

Complex partnerships succeed where experienced managers ensure that in addition to professional project management and sound governance, appropriate business relationships are established between the parties to the contract. Interviews with experienced practitioners from both the public and private sectors have led us to the conclusion that there are three key ingredients for achieving successful outcomes in such complex partnership projects: business case; design; and approach.

The business case must accommodate an unequivocal opportunity for mutual gain and it must demonstrate a preparedness for effective project management by both parties. The design must establish appropriate structures and processes that will provide a framework for sound governance and management of the partnership. And the approach must moderate the behaviour of individuals (and organisations) and promote a management culture that will create an environment for effective collaborative working.

Many of these practitioners suggested that people, their behaviour and the culture within which the project is delivered have the greatest

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overall impact on project success. They believe that when a partnering approach is adopted, there is greater openness, and problems are identified earlier and are resolved more quickly by the parties working together. The focus tends to be on solving the problem first and resolving the commercial implications later once the heat is off. Conversely, in failing projects the primary focus is typically on commercial considerations (cost and compliance), there is little effective engagement between the parties at any level, problems are reported formally by contractual letter and there is virtually no scope left for joint problem resolution. Whilst it is easy to suggest that such behaviour may be a symptom of failure rather than the cause, the evidence suggests that where a partnering approach has been adopted at an early stage by the contracting parties and a robust collaborative relationship established, the likelihood of later resolving such difficulties is enhanced. The reality is that complex projects are difficult to manage and however well they are designed and governed there will always be difficult issues to resolve. Where the contractual relationship is likely to span a long period, and many recent large government contracts have a 25 or 30-year duration, a partnering approach could be essential to ensure lasting success.

True partnerships are not created overnight, but are developed over time by people working together cooperatively and building robust, open and trusting relationships. Current policies and processes in Europe fail to reinforce the development of partnerships at the procurement stage. However, outside the competitive phase itself, through the initial engagement period and during negotiation there are opportunities to build coalitions and these opportunities need to be maximised.

Partnerships are expensive to create and maintain and must have real purpose to justify the additional overhead both parties need to invest. The risks are high and the potential rewards must also be high. There is a need to build greater understanding in the area of risk pricing and management if the full potential benefit of this approach to service delivery is to be realised. Where a partnership approach is truly justified it must be in both parties' interests to work very closely together. "We are in this together" is the spirit. Furthermore, where successful collaboration has been achieved it will be very difficult to identify which organisation people engaged in that partnership work for.

1.1 Terminology

In some treatments of partnering and partnerships, these terms are given very specific meanings, based on the assumption that there are ideal structures or models and that collaborative contracting arrangements must conform to these ideals if they expect to secure the maximum benefits from partnering.

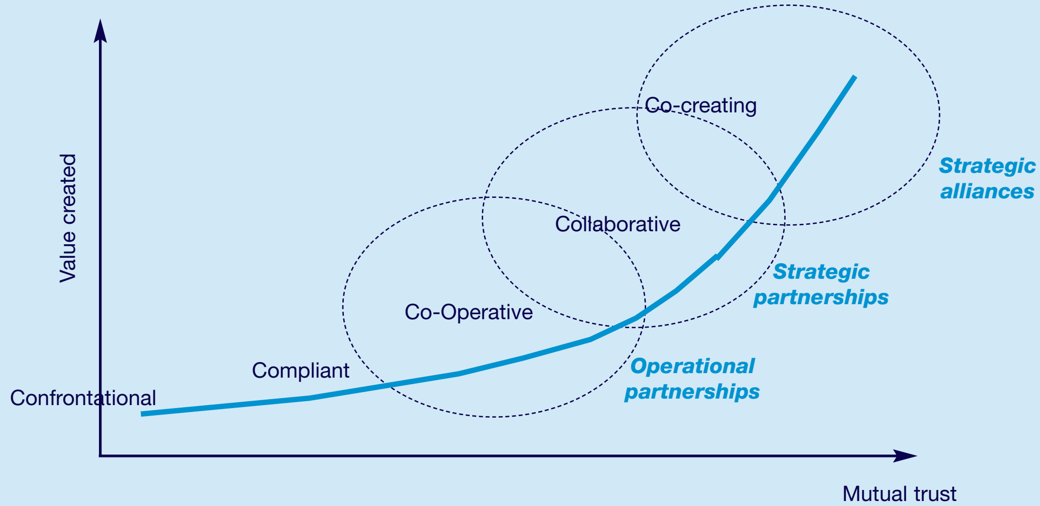
In this issue, we adopt a "toolkit" approach to partnering and collaboration. We take the view that there is a range of different tools that might be applied to develop a *partnering* approach in contracting, and these are capable of being used in a number of different ways to improve the design and delivery of even the most basic service contracts. It is only when these tools are combined in sufficient density, and where there is a reasonably high level of collaboration between two or more different organisations that the relationship is deserving of the term, *partnership*. But even here, we have avoided a prescriptive definition of what the partnership concept implies.

In recent years, the term *alliance* has also been invoked in reference to partnerships that are intimately interconnected, where the alliance partners are selected based on their competencies, where solutions are developed collaboratively and where many of the risks are shared between the parties. To date, the concept of *alliancing* has largely been applied in large-scale construction projects, and for reasons that are outlined below, it is unclear whether this level of interconnection is capable of being sustained in the services sector. While we refer to one innovative application to service contracting, we have refrained from using this term in relation to the delivery of public services under contract.

Tony Lendrum, an Australian academic and thought leader in the field of strategic partnering, uses the term, *operational partnering* to refer to the adoption of a partnering approach in the delivery of conventional service contracts. Based on this analysis, *strategic partnerships* tend to be of high value, associated with the delivery of complex services and adopt more formal partnership contracts. *Strategic alliances* imply a shared endeavour, with a high level of trust and integration between the respective parties. (Tony Lendrum, *The Strategic Partnering Handbook*, 3rd ed., Sydney: McGraw-Hill, 2000)

This issue argues that elements of a partnering approach may add value to any complex, long-term contractual relationship where more than simple compliance is required but that only those contracts in which there is a compelling case for comprehensive partnering will sustain the effort, cost and overhead activity associated with partnering. It also argues that whilst many contractual relationships are referred to as partnerships, are structured as such and have partnership processes written into

Figure 1: Relationship styles



Source Based on work by Tony Lendrum

the governance arrangement, unless people working within the arrangement behave according to a partnering ethos, no real partnership exists and the project is unlikely to deliver its full potential.

2 Background

2.1 Market evolution

The past 10 years have seen a significant increase in the complexity of partnerships formed between public and private organisations, both in the UK and overseas. The drivers for this have been various, but at the heart of the new way of working lies a desire on the part of government to extract more value from the money it is spending on public services.

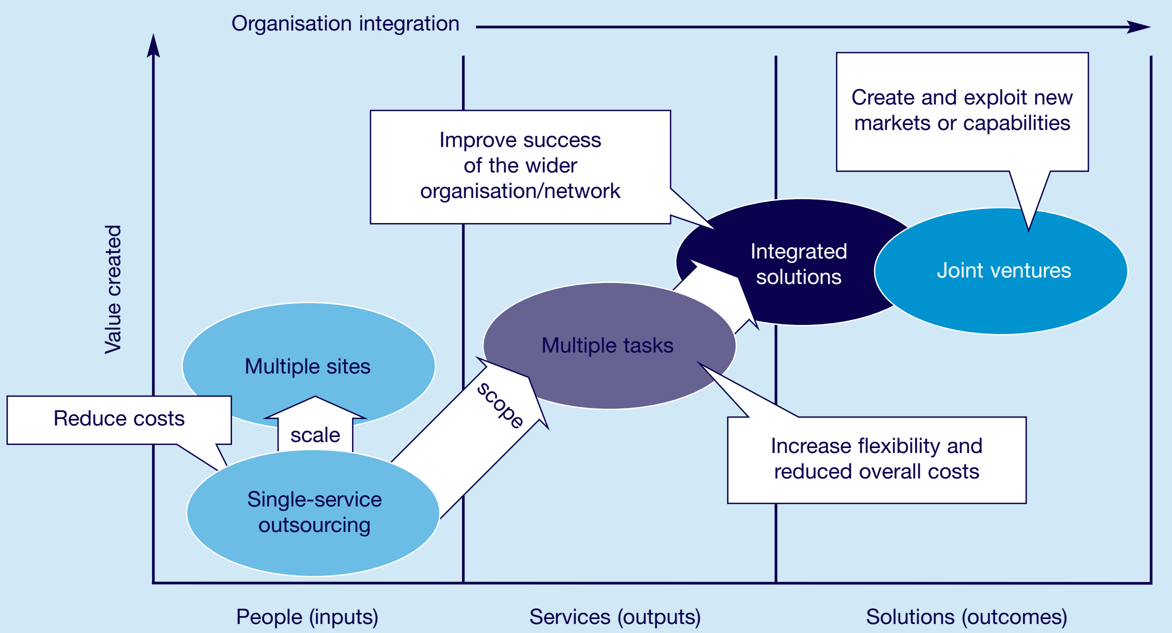
In the UK, as the market for private sector provision has developed, so also has the range of contract arrangements used to define the relationship. In spite of the publicity given to large-scale public private partnerships, the most common arrangements continue to be fixed task, fixed price, fixed duration contracts that are competitively re-tendered on a periodic basis, typically every five to 10 years. Such contracts continue to provide the most straightforward means of providing value for money in many areas of government.

In the beginning, competitive tendering of these services was meant to provide cost savings, with management responsibilities being retained in-house by the public sector. Significant cost savings were initially achieved under these early "manpower substitution" contracts. However, in central government and in local government, repeated competition resulted in undue focus on price, which began to destroy value rather than creating it. With the requirements being closely specified, the predominant discriminator in the procurement was service cost and consequently, successful bidders were obliged to cut margins too finely and services suffered.

These "resource contracting" arrangements are still widely used, but increasingly providers have been asked to assume management responsibilities and the contract has specified the required outputs, or deliverables, rather than inputs defined in terms of manpower and skills. This handover of management responsibility and the change in mode of specification has enabled the private sector to utilise its management capabilities to deliver better value for money solutions whilst still maintaining quality standards. An example of this is the "Best Value" initiative, introduced in UK local government in 1999. Best Value was designed to replace the adversarial relationships that characterised the later stages of the "Compulsory Competitive Tendering" regime, which had been introduced more than a decade before. Among other things, Best Value encourages local authorities to focus on value rather than just price.

Alongside this change in the style of specification has been a move towards task consolidation and increased scale and complexity. The proliferation of short-term, single service, price-driven contracts created an environment where there were frequently a number of different service providers operating on a single site, providing a range of distinct but related services. This restricted the capacity of each service provider to innovate and capture economies of scale and scope. It also created difficulties for the customer who had to manage across numerous interfaces and cope with many small-scale procurements. Some public sector organisations found it difficult to manage such complexity, and increasingly contracts were bundled together into what have

Figure 2: Evolution of the UK market



been referred to as multi-activity, or integrated service contracts. These were usually for a somewhat longer term, they were output specified and they had the dual benefit of delivering enhanced flexibility and a further reduction in costs (achieved in part by training staff to be multi-skilled).

Task contracting is still popular, but as confidence in outsourcing has grown and the government's policy agenda has advanced, the public and private sectors have increasingly sought new ways of working together to add more value.

The past decade has seen a substantial increase in complexity, with a significant increase in the scale and duration of contracts, the bundling of construction, service provision and asset financing under "Private Finance Initiative" (PFI) contracts, major advances in terms of risk transfer, and the experimentation with new structures and processes such as joint ventures, partnerships and alliances.

The movement towards greater risk sharing through collaborative arrangements has taken place in parallel with the pursuit of greater risk transfer, although the latter development has received more attention, both through the PFI and through certain large-scale IT contracts. But over this same period, a great deal of attention has been given to the principles of partnering in the UK construction industry, and in some overseas markets, there has been increasing awareness of and experimentation with alliancing models. In the UK public services sector, particular attention has been paid to the development of strategic partnerships in local government, and there has been widespread experimentation with partnering principles across a wide range of public services (although this has been poorly documented).

In the past, it was customary to speak of outsourced services as “non-core”, but there is a growing realisation that, core or not, it is critical to the success of the commissioning organisation that these services are delivered effectively. Specialist providers are emerging that can not only deliver high quality services, but offer skills in financing and total solution engineering. When aligned with the customer’s business strategy this wider range of services can deliver greater value to the whole enterprise. These integrated solutions are often of significant scale and scope, rely heavily on effective collaboration between the client and supplier and form the basis for many of the public private partnerships discussed in this issue. They are often aimed at delivering not just task *outputs* but service *outcomes*. Most are characterised by complex and lengthy risk reward contracts. This issue of PPP Bulletin focuses on these projects.

2.1.1 Context

By mid-2005, almost 700 PFI/PPP projects had been signed, totalling around £44bn of capital value (*Source*: Partnerships UK Projects Database). This figure does not take into account the long-term requirement to maintain the assets and deliver the associated services, costs which are built into each one of these projects from the outset. Nor does it include the contracts signed over the past few years where the private sector has provided additional investment. The scale and reach of this activity, which affects almost all areas of public procurement demands an approach from both sectors that enables ongoing learning and continuous improvement in the design and delivery of such projects. Significant attention has been given to design of these projects, but it is only now that government is addressing the conditions necessary for successful delivery, a factor which this issue seeks to address.

There is widespread evidence in the UK that complex contracting between the public and private sector is delivering value. The National Audit Office, the Audit Commission, the New Local Government Network, the 4Ps and the Office of the Deputy Prime Minister’s Strategic Partnering Taskforce have each undertaken their own research and all point to an improvement in the delivery of public services and in many cases significant cost savings. It is clear that where a serious attempt has been made to pursue effective joint working, there have been significant benefits.

> The performance of a Local Education Authority (LEA) has been transformed through its relationship with its private sector partner. Inspection reports into the LEA by the Office for Standards in Education (Ofsted) in 2000 and 2002 both identified significant weaknesses in education services. Both inspections rated the authority as “Poor” or “Very Poor” in all categories; all aspects of support and challenge for schools were weak and as a result there was underperformance across the whole borough. In January 2003, a new company was created as a vehicle to take over delivery of all education services on behalf of and in close partnership with the LEA. An Ofsted inspection in 2004 awarded the LEA scores of ”satisfactory” or “highly satisfactory”, representing a significant improvement in performance of the services.

A 2001 report by the Institute for Public Policy Research (IPPR), *Building Better Partnerships* (Gavin Kelly *et al* 2001), made a number of key recommendations for improving public private partnerships (PPPs), many of which have since been addressed. Accountability and governance of PPPs have improved, with more evidence of joint decision making, engagement of local stakeholders and adoption of open book accounting. New powers of prudential borrowing in local government and for some National Health Service (NHS) Trusts have broadened the options for raising capital, and a new code of conduct has been agreed by government, unions and the private sector to promote good employment practice. There is better guidance available for practitioners and new models have been developed that are inherently more flexible. New models include the "Local Improvement Finance Trust" (LIFT) programme in the NHS, which has been employed for the design and delivery of new primary care centres. LIFT has used formal joint ventures as service delivery organisations, collectively owned and managed by the public and private sector stakeholders, who share the risks of asset provision and service delivery.

However, there is also evidence that some complex collaborative projects have failed to achieve expectations. A series of reports conducted throughout the 1990s, culminating in the 1996 Construction Act, encouraged the adoption of partnering principles and brought about a marked improvement in the delivery of projects in the UK construction industry, which historically had been bedevilled by adversarial relationships throughout the supply chain. A recent investigation by the National Audit Office into the management of government construction projects found that, as a result of adopting the principles embodied in this legislation, costs had been reduced, fewer programme delays had been experienced, fewer parties go to law and safety and quality was improved. (National Audit Office, 'Improving Public Services Through Better Construction', HC 364-1 Session 2004-2005, 15 March 2005)

In submitting a recent report of a review of the Construction Act, Sir Michael Latham told the government: "At the heart of all these initiatives...is partnering, collaboration and integrated team working. These approaches are also the core of government policy for the industry and are widely and publicly supported by a growing number of clients both public and private sector". In its revised partnering guide, *Smarter Partnering*, the UK Ministry of Defence (MOD) suggests that "most defence procurement would benefit from the application of…partnering principles".- (Ministry of Defence, 'Smarter Partnering: Additional Practical Guidance about Partnering Arrangements between MOD and its Suppliers', 2002)

In the following sections we explore these partnering principles and consider how they impact on the design of contracts, legal forms and governance structures. We look at how organisations can prepare to partner, what management skills and experience practitioners require, how successful partnerships are designed and how they can be measured and improved.

3 Conditions for success

In spite of the apparent enthusiasm for partnering and partnerships among commissioning organisations and contractors, there is only limited evidence of these principles being applied in practice in complex public service contracts. Why is this? Why is partnering not used more often? The answers can be organised under four broad headings:

(a) purpose;

(b) people;

(c) culture; and

(d) design.

Partnering is hard work and it is expensive. Even at its simplest, it requires more time and effort to be expended on communication between the parties, but as the depth of partnering increases, it demands senior management time, new governance mechanisms and additional resources. Unless it is clear that the benefits outweigh the costs, and unless there is a shared understanding as to the reasons why this time and effort should be expended, then it is unlikely that the parties to a contract will invest in the tools necessary to construct and sustain a successful partnership.

To a large extent, partnering is about relationships between people, and unless the right kind of people with the right kind of skills are engaged in developing, fostering and repairing these relationships, it is unlikely that collaboration between two or more organisations with different cultures and different business models will succeed. These people are thin on the ground in both the public and private sectors, particularly where simple command-and-control management structures have been the norm.

Although involvement of the right people is crucial, it is unlikely that a partnership for the delivery of complex services will survive if it relies solely on interpersonal relationships. Such arrangements are necessarily fragile and they will be severely tested if significant disagreements arise, or if team leaders move on to other assignments. Organisational culture is part of the answer in areas such as institutional patterns of trust and communication. But it is also possible to increase the likelihood of success through good design – in procurement and negotiation processes, in contractual form and in the organisational structures, management practices and governance arrangements through which the service is ultimately delivered.

3.1 Purpose

In the absence of a shared sense of purpose and agreed objectives, the pursuit of a close alliance between two organisations will almost certainly fail, or worse, become a means through which the stronger of the two imposes its will upon the other. In commenting on the difficulty of coordinating the efforts of two or more different organisations, the North American political scientist, Aaron Wildavsky once observed:

> "If we relax the assumption that a common purpose is involved...and admit the possibility (indeed the likelihood) of conflict, then coordination becomes another term for coercion .... Everyone wants coordination – on his own terms. Invocation of coordination does not necessarily provide either a statement of or a solution to the problem, but it may be a way of avoiding both when accurate prescription would be too painful." (Jeffrey L. Pressman and Aaron Wildavsky, Implementation (3rd ed), Berkeley: University of California Press, 1984, pp.133–34.)

Successful partnering demands that both parties understand why they are investing the time and expense in building and maintaining a complex set of structures, processes and relationships.

3.1.1 Pursue optimal interconnection

In service contracting, there is almost always a case for adopting some partnering principles such as trust and communication, but full-scale partnerships should not be pursued where the anticipated costs outweigh the expected benefits, or where the level of integration involved is unnecessary for achieving successful value for money outcomes from the service in question.

In the organisational literature, this has been discussed in terms of the level of coupling. Tight coupling is essential in a continuous processing plant where objects must move continuously from one stage of production to another, but this level of interdependence is not usually so important in the service sector where deviation from standard processes will not have such disastrous effects. The tighter the coupling between two or more different organisations, the more participants that will be involved, leading to greater organisational complexity, an increased likelihood of failure and higher costs of coordination.

After studying the public transit system in the Bay Area of San Francisco, Donald Chisholm proposed what might be called an "Optimal Coordination Rule": No more coordinative machinery should be used than is absolutely necessary to achieve a satisfactory level of interdependence for that particular system. (Donald Chisholm, *Coordination without Hierarchy: Informal Structures in Multiorganizational Systems*, Berkeley: University of California Press, 1989.)

This is not an argument against using partnership models in the design of public service networks. But it is an argument for optimising the intensity of the partnership based on the network in question. Introducing an unnecessary level of complexity into a contractual relationship will increase rather than decrease the risk of failure.

3.1.2 Create a shared sense of purpose

Because it is such hard work, the parties need a compelling reason for adopting a collaborative approach that will bind them together throughout the life of the project. Both parties need to arrive at the conclusion that partnering is the only sensible answer and that the burdens of following this path are outweighed by the benefits.

The origins of the alliancing model are to be found in the North Sea oil industry, where the potential benefits of collaboration in terms of the early delivery of complex infrastructure were immense. Because the potential upside was so large and quantifiable in monetary terms, there was plenty of scope for reaching agreement on rules for sharing the gains. Conversely, the potential downsides were huge and it was recognised that the only way that this risk could be managed effectively was through establishing an alliance that incorporated a shared sense of purpose and by developing a contractual and governance structure which reinforced the common ground.

Research into alliancing models seems to suggest that they work best with construction projects which have a defined lifespan and a focused set of objectives. Moreover, they deliver better value for money where the project is complex, the risk of delivery and the opportunities for value enhancement are high, where time is a major constraint and/or where there is a demand for a significant amount of certainty around the overall cost.

It is unclear whether there is the same scope for value for money improvement out of alliancing models in the public services sector: the potential benefits (and risks) may be just as great as in construction projects, but they are not always clearly defined and they cannot be reduced to simple monetary values capable of easily being divided between the parties. As a result, the challenges associated with developing a common sense of purpose in the ongoing delivery of public services are much greater, which may be why they are better suited to looser forms of partnership.

The Local Government Strategic Partnering Taskforce of the Office of the Deputy Prime Minster (ODPM) monitored a series of multi-authority partnerships as part of its 2002 Strategic Service

Partnership pathfinder programme. More than one of these partnerships fell at the last hurdle, after incurring cost for the authorities themselves and their potential private sector partners, because the authorities concerned could not agree on the design of the model. The Taskforce concluded that there was no shared sense of crisis that would have encouraged the partners to cooperate more closely to find a collective solution.

3.1.3 Create a win-win situation

Where the parties together are not confronted by a significant risk, or where they are not able to identify substantial benefits that can be achieved by working collaboratively, then they will see themselves as playing a "zero-sum game", in which any success by one of the parties will be seen as having been made at the expense of the other.

For a partnership to be sustainable over the long term, both parties must believe that the arrangement is a positive-sum game, so that any benefits obtained by one side are not necessarily secured at the expense of the other. In the public sector, this may involve a significant effort in documenting the overall benefits and communicating them to a sceptical public which is conditioned by the media to see only zero-sum games.

But more than that, in most situations, the parties must also believe that the benefits are being distributed "fairly". There are two dimensions to the concept of fairness in this environment, which are, to some extent, in conflict: benefits must be roughly proportionate to the risks and there must be a sense that they are being shared fairly between the parties.

Too many partnerships fail because the understanding of the risk/reward relationship is poor and not debated early in the process. The anticipated risks and the expected returns need to be well understood by both parties. An aggressive procurement process which results in the private sector partner assuming risks that are impossible to manage or are inadequately compensated, will not lead to a contractual relationship that will be sustainable over the long term. Unrealistic performance measures that result in steep financial penalties for the private contractor will also undermine the viability of a long-term partnership.

On the other hand, an agreement which delivers huge windfall gains for the private contractor will be difficult for the public sector partner to defend. These risks can to some extent be overcome through periodic review clauses (a device used in the London Underground PPPs), or through profit-sharing arrangements (such as exist in the contract for the management of the National Physical Laboratory).

A deal between a large public sector organisation and the private sector stands on the brink of collapse. It was set up honestly and with a sound business model, but it made unrealistic assumptions about how much third party revenue could be generated. Circumstances changed and the potential for growth all but disappeared. Without the assumed third party growth, the commercial model did not stack up. The private sector partner is not able to deliver the service at a profit and it now has little or no flexibility to provide the added value that it promised. The public sector partner feels aggrieved that contractual promises are not being delivered. Neither partner is obtaining what they hoped to gain and the arrangement is likely to end in divorce, a situation that might have been avoided if there had been greater openness in the early stages of the deal, and the underlying assumptions of the business case had been realistically discussed.

3.1.4 *Clarify objectives*

Clear objectives sharpen the focus of any project, but they are essential in complex projects where significant change is required and/or a number of organisations are involved in delivery. Defining and communicating a vision early in the definition of a project will help keep those objectives clear and assist in developing an effective strategy and a sound financial case, and in allocating appropriate resources for the project.

These objectives should be translated into a timetable and a clear set of performance measures that define success and a satisfactory rate of achievement. This will provide the focus around which the partners can design their processes and controls in order to work together effectively.

> In 1997, Westminster City Council began a project to improve its performance in dealing with customers. The vision for this new customer services initiative was "to improve significantly the quality of our customers' experience when they contact the Council and to reduce, over time, the cost per customer contact". The Change Manager for Westminster Council at the time commented that "having a sharp vision helped to focus the development of the programme and assess more accurately what needed to change. Building the outline business case underscored the need to collaborate to deliver the required outcomes and in 2001, the Council established a long-term partnership with Vertex Ltd to realise the vision". (Office of the Deputy Prime Minister website.)

3.1.5 *Create realistic expectations*

Some partnerships are undermined at the very beginning through unrealistic expectations on the part of the commissioning organisation. The procurement processes introduced by UK Treasury as part of the Private Finance Initiative have been remarkably successful in managing unrealistic expectations, but major procurements are still proceeding where the client is subject to what Treasury has described as "optimism bias" – those involved in the procurement develop a set of unrealistic expectations that lead them to overestimate the outcomes and to underestimate the risks.

The business case should be an honest assessment based on realistic assumptions and reliable data. It must not be a mechanism for generating an internal justification for the project. Building such a case may often involve significant development work and analysis to link the business plan to the top-level strategy of the organisation. Critically, it will often require active engagement with the supplier community to ensure assumptions about the technical solution and risk transfer are sound. This does not imply a "one size fits all" solution imposed on all parties at the competitive stage, but rather the creation of realistic approaches through which reasonable upper and lower parameters can be established.

Affordability is a key part of establishing any business case and continues to be a difficult issue in complex projects, especially where private finance involved. Projects are still being cancelled late into the procurement timetable because the public sector comparator turns out to be unrealistic. But even where a procurement proceeds to financial close, unrealistic expectations generated during preparation of the business case, combined with an aggressively competitive procurement process and opportunistic bidding on the part of one or more contractors, can result in contracts that are undeliverable from the outset. Greater transparency in the estimation of affordability would help all parties to understand the underlying assumptions made and facilitate more effective challenge at project review.

Of course, contractors can also be guilty of unrealistic expectations, particularly in new markets where there is only limited understanding of the service in question, where the service itself is inherently complex, and where the external environment is changing. Since the ultimate risk for service failure rests with the client agency, it is not in the interest of either party for winning contractors to be placed in a situation where they are destined to lose (a market failure known to economists as “the winner’s curse”). It follows that those involved in commissioning a procurement and those involved in actually conducting it, must ensure that the services that have been specified, and the risks that will be transferred, are manageable at the price that has been proposed. Of course, in a changing environment, the maintenance of realistic expectations requires ongoing adaptation of the performance requirements.

> During an interview, a client-side contract monitor confided to one of the authors: “Some of these performance indicators really do not make sense, and I hate raising non-performance penalties against them. These requirements are out of date and force the service provider to focus on delivering something that we don’t really need them to do anymore. There are other things they could be doing that would be really valuable to us, but they are not in the contract and we have to enforce the contract.”

As unfortunate as this sounds, there are still numerous examples of contracts being enforced that are out of date and no longer appropriate, in spite of the attempts to get them changed. In the example above, whilst the parties sometimes refer to the contract as a partnership, their behaviour belies the name. One solution to this dilemma lies in planning for a full review of the performance regime part way through the life of the contract.

3.2 People

In some of the current literature on partnership management, the terms “project” and “partnership” are used interchangeably. There are two distinct and parallel objectives in the construction and maintenance of a public service partnership – delivering the project outcomes and building the relationships necessary to sustain the collaborative arrangements. These are, of course, complementary and mutually dependent roles, but they require different skills and (usually) different kinds of people.

3.2.1 Find the right people

The task-focused people who make ideal project managers are of a different nature from the people-oriented people who make good relationship managers. People who are good at partnering tend to be cooperative by nature. They enjoy establishing and grooming relationships. They tend to focus on the big picture and would rather get everyone round the table to make important decisions than rely on each member of the team doing their own job. When serious problems occur, partnering people will wish to understand the root cause, but they will be much less interested in apportioning blame. They would rather concentrate on channelling the creative energy that is generated in a crisis into jointly resolving the problem and learning from it.

The people who make effective partnership leaders tend to be gregarious by nature. They breeze in and out of people’s offices, stop them on the stairs for a chat and ask after the health of a new baby in the same breath as they question the status of the project plan. They are natural networkers and relationship managers, being genuinely interested in the wellbeing of their colleagues. They tend to disregard organisational boundaries and promote social interaction outside the office environment.

These people invest a huge amount of energy into relationships and they are likely to introduce colleagues as "friends" when meeting third parties, blurring the boundaries between business and social contact. And they will be genuinely distressed if such relationships break down. When interviewed on this question, one operations manager said quite simply, "our customers are our colleagues". It is the depth of these relationships that creates the value in partnering.

Provided that these individuals operate within a transparent framework, there is value in having them focus on maximising each other's success. An effective project team will have a balance of people with technical, commercial and people skills. The team will need to be assessed to determine each individual's strengths and their affinity for partnering, to ensure there are people with a track record of success in designing and building partnerships. The selection of leaders for partnership projects is one of the most critical decisions of the design phase, so individuals must demonstrate a high performance signature in an assessment of partnering competence.

> One project director described a PFI project where the construction partner made a serious mistake in building work, putting the project back by four to six weeks at a cost of £1m. It was clearly their fault, but instead of penalising them, the project director gathered the consortium together, explained the problem and asked everyone to work together to come up with a plan that would put the project back on schedule and recover the loss. The team found innovative ways to reduce their costs in other areas, devised a new method for the construction and changed their plans in order to save time. As a result all the partners still made their profit margins and the programme was delivered only two weeks behind schedule. This minimised the impact to all, including the construction partner. To do this, the project director was both motivated to resolve the problem and empowered to take a proactive approach.
>
> The interests of the project appear to have taken precedence over those of the senior partner's parent company. The senior partner and possibly others might reasonably have sought reparation from the partner who had bungled. The project director argued differently. She explained that they had been constantly changing details in the design specification, forcing the constructor to update their plans regularly and amend the construction timetable. "We had agreed to work in partnership and I was determined to stick to that. I had built strong relationships with my peers from the partner organisations and I knew that whilst the constructor had made a mistake, it was certainly an honest one. We had approved the plans and agreed to the construction method, so perhaps we should have spotted the error. Anyway we had two options: litigation or pragmatism. I made the decision to share the satisfaction of putting the project back on track rather than share the blame for it going wrong. This way too, we have all learned from what went wrong and I believe we will be able to plan better in the future. We also have a relationship with our partners that has been fire-tested and we are stronger and more competitive as a consortium, ready for the next opportunity."

The PFI model provides a powerful incentive for project teams to deliver against a timetable, but it does not encourage this type of partnering within the consortium. In fact, quite the reverse. The strict contractualism of PFI, and the way in which risk is flowed down, tends to provoke legal responses to this kind of dilemma, rather than promoting an appetite for risk sharing. Of course every project is different, but the example above highlights the importance of appointing project directors who can see the bigger picture, and engage and motivate their partners to do the right thing for the project.

Partnerships for Health (PfH), is a joint venture between Partnerships UK and the Department of Health, set up to deliver improved primary healthcare facilities through LIFT (Local Improvement Finance Trust) companies. When recruiting new staff, the CEO of PfH specifically looked for people with a mix of corporate and business experience and a background that incorporated both the public and private sectors. Furthermore, whilst strong influencers were required, candidates for roles in PfH needed to demonstrate an ability to see both sides of the argument. The CEO was certain that "some people are incapable of seeing another person's point of view". No matter how strong such individuals might be in their field of expertise, they are a liability when trying to build collaborative relationships. "In the negotiation phase all LIFT arrangements need a deal-closer. These people have to be able to empathise in order to find the right common ground for compromise, an essential ingredient of win-win negotiation."

3.2.2 Engage the right people early in the process

Given the importance of contract design to the ongoing success of a partnership, it is essential that the right people are engaged during the preparation of the bid and at contract negotiation stage. In a recent issue of the *Harvard Business Review*, Danny Ertel has pointed out that "the very person everyone thinks is central to the deal – the negotiator – is often the one who undermines the partnership's ability to succeed". Deal makers see the contract as the conclusion; partnership makers see the agreement as just the beginning. Among his correctives, he includes the appointment of implementation-minded negotiators who will treat the alignment of interests as a shared responsibility. (Danny Ertel, "Getting Past Yes: Negotiating as if Implementation Mattered", *Harvard Business Review*, November 2004, pp.60–68.)

The same is true of those involved in designing the service solution during the preparation of the actual bid. It is fundamental to the success of a subsequent partnership that relationships are being built throughout the procurement process. Aggressive behaviour on the part of the procurement team or the various bid teams can undermine trust between the parties and make subsequent collaboration virtually impossible. Of course, it is at this early stage that project objectives are being defined and expectations are being created, and in an effective partnership, these will have been treated as shared concerns when the contract was first being commissioned.

3.2.3 Develop the right skills

Given the growing importance of public private partnerships, which all depend on partnering skills to one degree or another, public sector agencies need to develop the competencies required to manage these new delivery networks. This concept of network management is pursued in an important new book published in North America, entitled *Governing by Network*. The authors remind us that government has traditionally been constructed on hierarchical lines, with authority imposed from the top down. The new, networked organisations which are emerging in governments right across the world, demand a very different set of skills, both in network design and network management.

While their concept of network government is somewhat broader than that of service partnerships, many of their insights are directly relevant. On the question of capacity, the authors explain: "Managing network government requires a different kind of capacity than managing public employees. Good network procurement capacity required the participation of individuals with broad experience and the ability to see how varied configurations produce different outcomes and how different partners produce differing results". (Stephen Goldsmith and William D. Eggers, *Governing by Network*, Washington, DC: Brookings Institution Press, 2004, p.49)

Many complex PPP projects, such as the procurement of new hospitals, are undertaken by commissioning bodies that have no experience of large-scale procurement or of working in partnership with the private sector for delivery. For many of the individuals working in those project teams, this will be their first experience of procuring such a large asset and unless they subsequently move to a different authority to work on another procurement, it will often be their last.

Some of these deficiencies can be met by turning to experienced advisers elsewhere in government or in the private sector, although care needs to be taken to use these resources as a source of advice, rather than an excuse for abdicating responsibility. In particular, if the commissioning department or agency is proposing to embrace the partnering tools referred to throughout this issue, then great care needs to be exercised in the selection of advisers.

3.3 Culture

Contrary to what is often imagined, the business community relies heavily on behavioural norms in managing contractual relationships. In a ground-breaking study undertaken in the early 1960s, Stewart Macaulay conducted research with 43 Wisconsin manufacturers, investigating the way in which they actually managed their contractual relationships day to day. He found that their conduct was heavily influenced by cultural factors which operated over and above the formal contract. The lawyers Macaulay interviewed complained that businessmen wanted to "keep it simple and avoid red tape"; the businessmen reported that they preferred to "rely on a man's word", even when the transaction involved substantial risk. One purchasing agent told Macaulay, "You don't read legalistic contract clauses at each other if you ever want to business again. One doesn't run to lawyers if he wants to stay in business because one must behave decently". (Stewart Macaulay, "Non-Contractual Relations in Business: A Preliminary Study", *American Sociological Review* 28 (1963), pp.55–69 at p.61)

3.3.1 Understand that culture matters

Among those involved in commercial negotiations, interpersonal behaviour and organisational culture are often treated as soft factors which are difficult to capture, but they lie at the heart of long-term partnerships. Increasingly, this is being recognised within government. In a recent report on successful delivery of major defence projects in the UK, the National Audit Office concluded, "Successful working relationships are characterised by soft factors such as team working, trust and honesty. When [the Ministry of Defence] and its industry partners on a project display these behaviours they are more likely to develop a common understanding of the task, the progress being made and give early warning of problems". (National Audit Office, "Driving the Successful Delivery of Major Defence Projects…" 20 May 2005, HC 30 Session 2005–2006, p.7.)

One implication of this is that a partnership culture cannot be created simply by going through the procurement process. Those involved in commissioning public services from the private sector must have regard to the cultural setting in the supplier community. In the case of new markets, where central government agencies are sometimes bringing companies together and creating a new supplier community, public sector commissioners will have a significant amount of influence over the shape of that market culture.

The UK prisons sector provides a striking example: throughout the 1990s, the Home Office and the Prison Service brought together suppliers from a number of different sectors to create a new market, and through a series of wise decisions, created an industry culture which is both socially responsible and highly responsive to the government's policy agenda. However, it is not difficult to identify industry sectors where a partnership culture of this kind does not exist. Until the 1990s, the UK civil engineering sector was characterised by a culture of commercial hostility, leading to the Latham Report (1994) and the Egan Report (1998), which drew upon partnering principles and provided a sound basis for cultural change within that industry.

Of course, those involved in conducting a procurement should be concerned with selecting a supplier that has a culture of collaboration. Some (but not all) private sector companies have experience of working in a partnering environment. The scale and complexity of many service contracts have encouraged the provider community to collaborate in joint ventures, partnerships and networks so as to become more competitive. Through this experience, these companies have been able to understand more clearly what is involved in partnering and they have developed helpful approaches and mechanisms. They have also been able to develop individuals with the management style and skills necessary for collaboration of this kind.

On the other hand, the public sector has a very formal organisational culture and is somewhat more inclined to adopt an hierarchical, command-and-control style of management. Public sector managers have much less experience with managing in a networked environment and thus government has fewer of the people and processes required for successful partnering. This is exacerbated by the tradition of having public servants frequently transfer between positions, and the tendency in government to under value the kind of "non-core" skills that are essential for a good relationship manager.

The procurement process matters, but contrary to what some advisers have suggested, it is not possible to "procure partnering". Partnerships cannot be procured; they must be built over time through the development of mutual trust and understanding. Signing a contract will not deliver a partnership. This can only be done when each party adopts an approach that will facilitate the development of effective collaboration. In theory, a partnering approach could be adopted at any time throughout the life of a contract, but experience suggests that the earlier such an approach is employed, the greater the potential impact on service outcomes.

3.3.2 Build a culture of cooperation and respect

The culture of an organisation is the sum total of the values and beliefs of the people in that organisation, although it is maintained through traditions and rituals that are larger than the individuals themselves. The perpetuation of an organisational culture demands adherence to implicit rules and expectations of behaviour so that without formal specification, employees understand what is expected of them. Organisational culture is the responsibility of senior management and it is one of the tools through which managers can have the greatest impact on individual behaviour.

The same applies to partnerships between two or more different organisations. Establishing the right culture is critical for success: the leaders of the partnership are able to ensure that the various parties do "the right thing" by making "the wrong thing" unacceptable. Investment up front in creating a healthy partnering culture also enables those who create the partnership to institutionalise the behaviours and practices that enabled it to succeed in the early stages. This means that the relationship is not as vulnerable to the risk of losing individual leaders as the partnership matures. One of the ways in which some partnerships have institutionalised these cultural norms is through the creation of behavioural charters (on which, *see* below).

Key features in the cultures of successful partnerships are shared values, mutual respect, openness and a willingness to share important information across organisational boundaries, a no-blame approach to resolving problems and the celebration of success. There is some evidence that giving the partnership its own identity (for example, by giving it its own name) can create a sense of shared identity and provide a common focus for people who come from various different organisations. Where partnering is embraced, it is sometimes difficult to tell which company an individual has come from.

When individuals from organisations with very different cultures come together, there is the potential for misunderstanding and conflict. Where such stresses exist, firm leadership is required to sustain focus on achieving strategic outcomes, but change will often be embraced and welcomed if it comes with the opportunity to improve morale. Difficulties usually arise where the cultural differences arise from fundamental differences in people's values. This is perhaps less likely in organisations engaged in public service delivery because of the strong norms that have been established over many years in relation to these services, but where there is no common ground, behavioural change may prove to be difficult.

3.3.3 Build trust

Trust is fundamental to complex and long-term contracts (particularly service contracts) precisely because the parties cannot specify all of their rights and obligations in advance, in the way that they can with simple, standardised and short-term contracts. In a contract with some degree of complexity, it is impossible for the parties to imagine all of the conditions under which they will be required to work. In the case of 25 or 30-year contracts, such as those being signed under the Private Finance Initiative, it is absolutely certain that the political, policy and economic environment will have changed significantly by the time these agreements have run their course.

It is for this reason that the language of partnership has come to be used: long-term service contracts demand cooperative behaviour over an extended period of time, which means that they tend to look more like business partnerships than just supply contracts. And like a business partnership, over time the informal accommodations between the respective parties will acquire as much significance, if not more, than the formal agreement. It is fundamental to the success of such an arrangement that the parties have trust in one another.

We can think of trust as a kind of social capital, so that the time and effort spent in building mutual trust between partners is an investment that will bring returns in the form of reduced transaction costs. If the commissioning agency trusts its suppliers (to be both honest and capable), then it can allow them to monitor and report on their own performance, with only periodic external auditing. This avoids the need for a duplication of performance measurement and reduces the costs of contracting. It follows that trust is central to successful partnering and early investment in building trust and the ongoing maintenance thereof can result in significant savings over the life of the contract. It also follows that companies that are trustworthy will have lower transaction costs and, other things being equal, will more often be selected for complex and long-term partnerships.

Trustworthiness is built through the consistent delivery of promises; if it does not do "what it says on the tin", then the customer will not buy it again. People who build successful partnerships will be both trusting and trustworthy, although they will expect others to be so too. Interpersonal and inter-organisational trust is built first by extending trust: social research suggests that trusting people are more likely to elicit cooperative responses from others, although relationships of trust are most likely to survive over the long term where both parties understand that such behaviour must be reciprocal. Of course, this involves an element of personal risk for the individuals concerned.

> One project manager working on a roads project with a local authority back in 1995 took the decision to adopt a new approach. He spoke to his opposite number on the client side and expressed the desire to work together cooperatively, avoiding written correspondence and resolving issues face to face proactively. He was told by his line manager: "if this approach fails you are out of a job". As it turned out, the project was completed several weeks early and to a high level of quality, so that after 12 months, the only rectification order was the removal of a cone from a ditch. Not only did this approach make for a much more pleasant working environment, but critically it represented a real financial benefit for both parties and enabled the contractor to remain on the tender list for future work with the authority.

The level of integration in this example does not warrant us referring to it as a partnership, but this is an example where the project manager was able to employ some of the tools of partnering to reinforce a contractual relationship. What this example does demonstrate is the importance of leadership: both managers were at risk of looking foolish if things went wrong. The conventional wisdom at the time was that the contractor and client would seek to exploit each other and neither could be trusted to do the right thing by the other.

> When asked to identify the key factor that underpins their relationship with their client, managers in one service delivery partnership did not hesitate to name trust as the vital ingredient. "Our customer hears what we say, sees what we do and then we show them the results via the management information system. We say it, we do it and we prove it. Plus, if we make a mistake we tell them, and after two years of working together that now works both ways. We have no secrets. Our people behave as if they are part of the client organisation."

3.3.4 Communicate effectively

Effective communication plays an important part in building trusting relationships. Contract managers report that openness and honesty in communication between the parties, a willingness to compromise and a convention of "no surprises" are essential to a successful partnership. Reference has already been made to the importance of shared outcomes, but the process of actually coming to a common understanding of the issues is itself important in the development of successful long-term partnerships. In some forms of service partnerships, this may involve joint research into the problems that the partnership is designed to address.

Communication channels should be established as early as possible, and the best relationships do not confine these early conversations to the resolution of specific problems. They also include discussion about the culture and politics of the contracting organisations, the way in which decisions are made, what motivates (and de-motivates) key stakeholders, and their limitations and aspirations for the future.

Many of these partnerships are designed to operate for a very long time and they deserve a solid foundation. If organisations discuss win-win negotiation strategies, each party will learn what winning feels like for the other, both at day one and throughout the life of the arrangement. Some contract managers have suggested that a useful guide is to strive to understand the other organisation so that its interests might be represented to a third party. Compromise in the design phase means finding a way that both parties can win in the long-term, and this should always be the objective.

> During the procurement phase of its partnership for support services, Lincolnshire County Council provided office accommodation on its own site for the bidders. The rationale for this was simple – it enabled the bidding teams to engage with the client community during the bidding process, to reassure the client staff that their ideas and concerns were being listened to and to begin to build partnering relationships through the procurement phase.

3.3.5 *Reinforce good behaviour*

People who are engaged in successful partnership delivery often say that the key to success lies in the personal relationships they have developed. A typical comment from this kind of manager is: "Nobody gets it right all the time, but I know whatever happens, the team will work out a solution that we can all live with. I trust my colleagues on both sides to do the right thing". Practitioners often use the word "behaviour", and when asked how one creates an environment that facilitates the construction of the right relationships between the right people and encourages the right kind of behaviour, they often respond by referring to cultural issues.

To those with a technical or commercial background, this heavy reliance on personal behaviour seems like an uncertain foundation upon which to construct a robust business relationship. And yet if soft factors of this kind are central to the success of sustainable partnerships, then consideration must be given as to the conditions under which positive behaviour will be developed and reinforced.

It is not enough for project managers to identify "relationship with supplier/client" as a risk and record it in the risk register. Project teams must actually mitigate the risk by investing in building cooperation or actively seeking improvements in interpersonal behaviours.

Some organisations have sought to reinforce partnering behaviour by introducing a "behavioural charter", describing what is expected of each member of the team, what kind of conduct is acceptable and what is not. Marion Luckhurst, Procurement Director for BAe Systems Tactical Systems Division recommended writing all of this down on a card and carrying it around with you, as some organisations do with their corporate values statement:

> "This approach enables you to challenge poor behaviour and use the card to back you up – rather like showing a yellow card in football. After all, the point is that you have all agreed how you want to work, the card is there to remind you. We have found, unsurprisingly, that when things are going well, everyone behaves beautifully. The real test is when things are not going so well. Can everyone remain cooperative and focused on outcomes then? The behaviour charter really does help, because it reminds us that we are all in it together, we can back each other up, and help put things right. In my view the real power of partnering is the synergy you derive from getting everyone on the same page and working for the benefit of the project, not for themselves or their parent company alone."

The card is a useful addition to the armoury, but it is not enough. There must be frequent and robust debates about behaviour. This is crucial at the start of the relationship but it must be continued: people and organisations often behave differently when they are under stress and when things get tough (as they always do), unexpected behaviour may damage the partnership.

3.4 Design

Of course, no matter how well intentioned and how people-oriented they are, individuals must operate within an institutional framework. For this reason, those who are concerned with the intelligent and effective application of partnering principles must have regard to the design of the contractual and governance arrangements – how the contract is structured to incentivise the desired outcomes, what the delivery vehicle looks like and how the governance of this organisation is managed by the partners. Successful partnerships have review mechanisms that enable flexibility, monitoring regimes that add value, payment mechanisms that avoid perverse incentives and encourage innovation, escalation mechanisms that enable swift resolution of disputes, governance structures that facilitate the delivery of the shared objectives, partnership management structures and processes that enable optimal operational delivery and effective joint decision making. Partnering is not an excuse for reducing the depth and quality of process, nor is it an alternative to good contracting.

It also needs to be understood that it is possible to employ partnering principles throughout the life of a contract, and to take a standard service contracting arrangement and to redesign it so that it enables the parties to pursue much broader ends.

An established service contract with the UK Ministry of Defence (MOD) had achieved its key objectives and was working well. The desire for further cost and performance improvements resulted in the MOD and its private sector partner considering a more collaborative relationship and they subsequently negotiated an Interim Partnering Agreement (IPA), which set demanding targets. A Joint Management Team was formed to provide governance and strategic direction. The IPA enabled the parties to share efficiency savings and gave the private sector partner the confidence to invest in refurbishing infrastructure in order to achieve enhanced performance. This would not have been possible under the original agreement.

During the negotiation phase while the parties were working out the detail of their IPA, the teams discussed what a successful future might look like. They wrote joint statements about the services that would be delivered at various stages in the future and discussed how these would be achieved. Both parties identified a shared approach to risk management as being essential to robust collaboration. They developed a communications strategy that engaged all the stakeholders of the service.

3.4.1 Find the right partner

In some cases, a partnership may grow out of a pre-existing contractual relationship, although it is more likely that the commissioning agency will be faced with the challenge of choosing an appropriate partner in the course of the procurement process. This point seems so obvious that it might be thought that it is unworthy of specific mention. And yet in far too many traditional procurements, government customers appear to be content to select whichever supplier offers the lowest price, without regard to their reputation for compliance. When it comes to complex, long-term service contracts, the failure to pay attention to the potential suppliers' experience in working cooperatively with customers can be disastrous.

One of the characteristics of the new alliancing models is that customers select their design and construction partners based on their competencies, including their ability to engage in collaborative relationships, and then work together on developing the solution. While there are very few working models, it is possible that this approach might also have application in the public service sector. At the time of writing, the Tokyo Metropolitan Government was undertaking a PPP procurement to find a partner for a major hospital redevelopment. As this model was explained to potential bidders, the successful party would be expected to work alongside the hospital administration to undertake business process re-engineering, to develop and implement the strategy for procuring a new hospital complex, and to manage supplier relationships on an ongoing basis. What these models have in common is the emphasis on the selection of the right partner with the technical and commercial skills, as well as a track record of successfully engaging in complex partnering arrangements.

Of course, where a true partnership or alliance is being built, then both parties will be faced with the challenge of finding the right kind of partner, and both organisations will be engaged in undertaking a “due diligence” audit of the other. For some public sector agencies, the fact that they are also being subjected to scrutiny by potential suppliers will come as something of a surprise. This courtship process is much more challenging than traditional procurements, since the due diligence investigation must address a range of cultural factors in addition to technical and commercial ones, and it will need to take into account not merely the strengths of each organisation standing on its own, but the way in which the two organisations might work together. Questions about the compatibility of strategies and objectives will be central in determining whether goal alignment is truly possible.

Given that private sector suppliers are resource constrained and that the best of them are obliged to make early decisions as to which projects they will bid for, an intelligent customer will signal its understanding of and commitment to a partnering approach very early in the process of commissioning and procuring a new service. Publication of the RFP (Request for Proposal) or the OJEU (Official Journal of the European Union) Notice should not be the beginning of the engagement. The best project leaders find ways of enabling their organisations to engage prior to the formal commencement of the procurement process to build relationships with potential partners, to share ideas and develop outline solutions. It follows that in the procurement of complex public services, early engagement with potential suppliers is of value, not only in facilitating due diligence, but in creating a market with sufficient depth.

3.4.2 Build a suitable performance regime

One of the most elemental aspects of any contract is the performance regime, the conditions which the contractor is obliged to meet in order to be paid. With complex public services, it is often difficult to specify these obligations in advance with great precision, which means that over-engineering of the performance regime, with large numbers of key performance indicators (KPIs), is unlikely to deliver the best outcomes.

This is not to say that the contractual performance measures are unimportant. But they must be designed with the particular service in mind and the current state of knowledge about the linkages between inputs, outputs and outcomes. Where the customer has an imperfect understanding of these linkages, either for reasons of complexity, or because the service in question has evolved over many years, then there is a strong argument for relying on the partnering approach, at least until the service is better understood.

In situations of uncertainty, performance regimes driven by harsh penalties tend to create a focus on penalty avoidance rather than service improvement. Some of those interviewed for this issue suggested that such mechanisms act as disincentives for innovation and can have the effect of inhibiting risk-taking, leading to a reduction in value for money. This is not to say that financial penalties ought not to be invoked, but it is possible to construct performance regimes which reinforce rather than undermine the partnering elements of a contract.

> Serco has a contract with a Local Education Authority where any penalties paid to the authority and the bonuses received by Serco under the performance management regime are re-invested into the development of the service. Whilst this does not impact the operation of the performance regime itself, it does remove any perverse incentives on the part of the client to extract penalties and does benefit the service overall. More importantly, it takes a potentially divisive aspect of the contracting regime and turns it into a force for greater unity.

Another way in which those designing the performance regime can reinforce the partnership is by placing greater emphasis on rewards rather than relying exclusively on penalties. Performance regimes where the service provider can only ever lose are demotivating, and this can be overcome with rather simple design changes so that the regime also provides for bonuses where service levels are exceptional. This is consistent with research into operant conditioning by the behavioural psychologist, B.F. Skinner, and experts on child-rearing, who have found that positive reinforcement is a more powerful motivator than negative reinforcement. Furthermore, a performance regime that is penalty based also focuses on finding fault and failure, whereas a reward based regime focuses on problem solving and success which is attitudinally suited for a partnership.

The approach taken by the customer to the actual monitoring of the contract can also serve to reinforce (or undermine) a partnering approach. Where trust has been established between the parties, then it may be possible to have the supplier undertake a great deal of self-monitoring, with periodic audits to meet the demands of probity. If the objective of a performance regime is to ensure the quantity and quality of service provided to the public, rather than scoring points at the contractor's expense, then this end will be better served through the early identification of problems and the rapid application of remedial measures. Feedback should be used to generate improvement, rather than simply driving the payment mechanism.

Particularly where the services in question are complex, this feedback is essential for the design of the next generation of contractual performance measures. Where, in the early stages of a newly contracted service, the contractor will be heavily dependent on the customer's understanding of the service, as time passes, the contractor becomes the principal repository of this knowledge, and if the service is to be re-engineered and the performance regime improved, communication between the parties is essential.

But partnering principles can also be used to enhance the performance regime, to encourage the contractor to deliver well beyond what is strictly required under the formal agreement. For most public service companies, the risk of damage to reputation will provide one of the most powerful motivators for service improvement. In other cases, it is possible for the customer to harness the service culture of front-line professionals employed by the contractor. In fact, it is not unusual for contractors to deliver well beyond the strict performance requirements of the contract. Why would a contractor do more than it is legally required to do? Sometimes it is because staff develop a strong sense of commitment to the end-user, so that they are motivated by a sense of professional pride. In other cases, it is because the company can see benefits in terms of its reputation with the customer or with the public at large.

Consideration needs to be given to the design of the contractual framework and, indeed, to the design of the market overall, in order to take advantage of these cultural and reputational drivers of service delivery. For example, it is much easier to harness these reputational incentives where the contractor is engaged in numerous interactions with the customer at different points in time, compared to a single once-for-all transaction. It might also be possible to reinforce the contractor's identification with the end-user through the design of the performance regime.

Through a contract for environmental services with a Local Authority, Serco's profit is put at risk against the results of independent customer satisfaction surveys, completed by members of the public. Failure to please the public, who are the recipients of Serco's range of environmental services, will result in a direct financial penalty. This requires Serco's staff to pay a great deal more attention to those aspects of environmental cleanliness that are important to the public at large.

Performance regimes are there to ensure service outcomes and they can be used creatively to drive innovation and to deliver service improvement. Service providers will usually wish to retain a profitable business relationship over a long period, and most will be pro-active in seeking opportunities for innovation and service improvement throughout the contract period, without any additional incentives to do so where they believe that this will help them retain and potentially grow their business. Where contracts are to last for an extended period, however, parties need to find other ways to provide motivation for continuous improvement. Benchmarking and market testing can help, but more imaginative means may be found that draw on the combined capability of the partners working together.

The Joint Service Command and Staff College (JSCSC) was built under a 25-year PFI arrangement. Since the college began operation, performance measurement has evolved beyond its initial focus on specific contractual terms. Monthly performance review meetings are now used in a broader, more constructive way, to analyse performance trends and consider ways to improve current approaches and outcomes. Because this is a PFI contract, amendment of the KPIs is difficult, but performance methodology statements can be rewritten and Serco has been updating these statements to distil the corporate knowledge and reflect lessons learned during the first three years of operation.

Over and above this, it is possible to use informal agreements or memoranda of understanding to create a high level commitment to a partnering approach. At JSCSC, there is a joint commitment by the partnering organisations to maintain a world class academic facility, and when it comes to disagreements over how this should be achieved, the parties have agreed to compromise in the interests of the institution as a whole. In the words of one of the leaders of the partnership, they have agreed to "give way graciously for the good of the wider partnership". This approach to continuous improvement would be difficult to mandate in a formal contract, but can be built into a partnering agreement (a non-legally binding informal document that parties sign up to as part of the partnership negotiations).

3.4.3 Build in flexibility

Robustness and flexibility are not mutually exclusive. Contracts provide the framework for managing service delivery and where the environment is complex, they need to be designed for flexibility as well as to encapsulate service requirements and payment mechanisms. The contracts designed for complex partnerships often run into several volumes, and where standardised terms and conditions can be used appropriately, this is certainly to be encouraged.

However, as Stewart Macaulay discovered, service level agreements frequently end up in the drawer, especially after the first few years either because the services are being delivered satisfactorily and there is no need to refer to the detail of the arrangement, or because service requirements have changed so much as to render the original agreement meaningless.

In both these situations, it might be argued that value is not being achieved. If money is to be spent on drawing up detailed contracts, then it would be better if they were designed so that they reflect the reality of how contractual relationships are managed in practice. And they might be written so that they served as a tool for the ongoing management of the relationship rather than just as a fall-back position when things go wrong.

One way of doing this might be to provide that service levels are continuously renegotiated and the contracts underpinning them are regularly updated and re-baselined. Not only does this ensure that service specifications match user requirements as closely as possible, it also provides a basis for application of a mechanism to assess and improve ongoing value for money, a factor which is of critical importance in maintaining the legitimacy of any long-term contractual relationship.

> Serco won a contract with the MOD, through a competitive process, to deliver support services. The competition was run on the basis of delivering a suite of core services, against an outline service level agreement (SLA). The process included a "post contract verification phase" during which far more detailed service level agreements were evaluated jointly with the customer and then finally agreed. Rather than leave it at that, these SLAs are now jointly reviewed on a regular basis and updated as required, so that they always reflect closely the actual services required. This would be difficult to achieve efficiently if the parties did not approach the activity cooperatively.

3.4.4 Choose the best structure

If we apply Donald Chisholm's "Optimal Coordination Rule" to contract design, then our choice of the governance arrangements will be heavily influenced by the desire to keep transaction costs to a minimum. In fact, it is somewhat more complex than this, since as soon as we begin to build formal governance structures at partnership level, then we also have to worry about the costs of collective decision making and the costs of controlling managers and staff from two or more different organisations.

It follows that considerable thought needs to be invested in the design of the contractual and organisational structures, to ensure that they are ideally suited to the nature of the service in question and the structures and the cultures of the parties to the arrangements.

A useful overview of the design and appropriate use of partnership structures is provided in "Rethinking Service Delivery", a paper prepared by the Strategic Partnering Taskforce of the Office of the Deputy Prime Minister (ODPM) in the UK and available on-line on the ODPM website. Most structures are variations of two key options:

(a) service delivery contracts between service provider and service commissioner, potentially with an overarching partnering agreement, where ownership of the delivery vehicle lies with one or other party, and

(b) formal joint ventures where ownership of the delivery vehicle is shared.

There may be any number of direct contracts between parties, and where multiple parties are commissioning a project jointly, the structure can become complex. Projects where private finance is to be used are usually based upon a new delivery vehicle that may have been established specifically for the purpose (a "special purpose vehicle") and which is owned by those members of the private sector consortium responsible for delivery that are bearing most of the risk.

Option (a) is the most common, however an enhanced sense of shared responsibility for project outcomes may be generated by choosing a vehicle that has shared ownership. There are advantages to this approach in that it encourages the partners to become genuine stakeholders in the success of the business. The Local Improvement Finance Trust (LIFT) has made use of this model in the NHS, both at the national level and through local LIFT companies, all of which are formal joint venture companies. Brian Johns, the chief executive of the national company, Partnerships for Health, is convinced that creating an entity where the partners have invested equity into the service company encourages a very real sense of joint purpose and a commitment to achieving successful outcomes. In return for investing risk capital, the partners have real influence at service company board level. Brian Johns: "If things go wrong we are all going to lose our money, so everyone is motivated to get things right".

Care is needed if a customer–supplier joint venture is chosen as a vehicle for service delivery, as service levels still need to be negotiated and agreements drawn up between this service company and its customers. Furthermore, there is a potential conflict of interest for the directors appointed to manage the joint venture company if they are also employees of either of the shareholding organisations.

> Liverpool Direct Ltd is a joint venture between Liverpool City Council and BT and operates as a minority interest local authority company. The majority of staff are council employees who have been seconded to the joint venture company (JVC). The main driver for the creation of the partnership was to deliver organisational transformation, focused initially on customer contact, but broadening to cover other council support services. The vehicle is also expected to trade externally to generate third party revenues. There is a service delivery contract between the JVC and the council, which contains challenging performance targets. Incentive mechanisms have been very carefully drawn up to minimise the potential for conflict of interest for the director of the JVC who is also an employee of the council. Use of a joint venture company has created a sense of shared purpose and a vehicle for real risk and reward sharing. This could have been achieved by other means, but this structure satisfied Liverpool's desire to retain staff as council employees and at the same time to transfer operational risk.

The National Audit Office (NAO) and Partnerships UK (PUK) may wish to take a lead role in encouraging government departments to pilot new commercial models and new ways of working that have the potential to improve value for money and the quality of operational delivery. Speaking at the 2004 conference, *Delivering Public Sector Innovation*, Jeremy Colman, then Assistant Auditor General for the National Audit Office said that opportunities for innovation were not being maximised because of an overly conservative approach: "Departments should encourage a culture of responsible risk taking and reward individuals who achieve good results through adopting an innovative approach". A shared approach to risk management built into the partnership design at an early stage may provide such a mechanism. Partnering is about give and take, but the public purse is often limited in its true ability to give because of the fear of liability and public accountability. It is important to find ways of creating some headroom that will enable a genuine feeling of risk sharing.

The development of new solutions in an iterative and incremental way, might be the way forward for some projects, especially where the commissioner and potential partners have distinct and complementary skills. The governance of such projects consistent with European Union (EU) procurement rules will require development, but an additional benefit may be an overall reduction in risk as the project is delivered in discrete stages, with a go/no-go decision at each stage. The Gateway Process developed by the Office of Government Commerce (OGC) might be adapted for use with a phased procurement.

> South Gloucestershire Council worked with its partner Unisys, using an incremental approach. This enabled a framework agreement to be signed on the basis of one clearly defined initial project and various options to develop further discrete packages of work. Following successful completion of each stage of the implementation, the two organisations were able to work together according to an agreed process to design and implement the next stage. One clear advantage of this approach was that the knowledge of the two teams could be effectively combined when it added the most value, avoiding costly re-design post contract award. Furthermore, obviously business priorities change over time, and the incremental approach provides a very flexible framework for designing and implementing a process of continuous service improvement.

3.4.5 Build good governance arrangements

The design of governance structures will be project specific, as each partnership exists under different circumstances and has different management arrangements over which governance is to be applied. However, in the design of such structures, genuine stakeholders in the project must be encouraged to take an active and sustained interest in ensuring the direction of the partnership and the delivery of the required outcomes. This means that governing bodies need to be established with participants who are empowered to make important decisions and ensure they are implemented. And the governing processes need to ensure that these individuals meet frequently enough to maintain the momentum of the arrangement. Membership of governing bodies needs to be kept tight or they will struggle to make decisions and thus cease to be effective.

It is important to remember that the relationships developed between the individuals who sit on these governing bodies will be key to the overall health of the partnership. There are many such bodies that have never held a meeting, on the basis that the partnership is doing fine and there are no issues to resolve. This approach may seem practical, but it misses a vital opportunity for the individuals to get to know and trust each other when things are going well, in preparation for when issues do arise later.

Partnerships for Health advises all its LIFT companies to set up a “shadow board” at least six months before the negotiations are completed and appoint an independent chair. The purpose of this shadow board is to provide independent facilitation of the deal at the critical last stages of negotiation. Brian Johns argues that those LIFT companies that took this step have been able to complete the deals more effectively through providing both facilitation and focus to the negotiations and preventing negotiators from becoming entrenched in their positions.

4 When partnerships go wrong

What happens when a partnership goes wrong, when the numbers do not add up or the contractual framework creates perverse incentives? Even the best project teams encounter problems that are not of their own making. In circumstances where large sums of money are involved, or where there is risk to reputation or of political fallout, these problems may become very difficult to solve. Where such circumstances persist, both sides can become uncooperative and even adversarial, and positions become entrenched. The focus starts to drift away from delivering what the customer wants, to delivering what the contract demands.

Good practice dictates that a dispute resolution process is agreed at the outset of the partnership. This should articulate when and how to escalate the dispute, who should be involved and at what stage the outcome will become binding on the parties.

Conventionally, when difficulties are encountered, the first stage of escalation is to involve more senior management. This can be problematic with partnership projects because these types of projects require the involvement of people with specific skills and attributes. Frequently in the public sector and not infrequently in the private sector, the people in more senior roles have not had sufficient direct experience of partnering to be effective in a dispute resolution capacity. Where intervention by senior management does not produce results, assistance from outside the partnership may be required.

The manner in which external assistance is provided will depend on the nature of the problem, but may include formal mediation, individual consultations with stakeholders, professional advice and guidance to senior managers or joint workshops for the partners at all levels. Whatever the means, the solutions arrived at through facilitation must be owned by the stakeholders.

In a dispute involving a conventional contract, the facilitation process involves looking at the situation from both perspectives, client and supplier, and aims to find an equitable way forward. The key difference with a partnership contract is that the parties in dispute should both be sitting at the same side of the table. Resolution has to focus on the best interests of the partnership and its objectives. In the case of public private partnerships, the governance structures should distinguish between the public sector as a partner and the public sector as a customer and disputes within the partnership should clearly distinguish those two roles.

Facilitation must be an honest attempt by a third party who is impartial and is perceived by the parties to have, as his/her sole interest, the restoration of failing outcomes for the partnership. The facilitator's function is to understand in detail the circumstances of both the parties and use this understanding to broker a return to honest and open endeavour. The solution will be focused on delivering the planned outcomes of the original partnering agreement and will be arrived at through a thorough assessment across the success factors already discussed.

A good facilitator will be able to take the heat out of the argument and provide encouragement to teams who will often have become demoralised and demotivated by the time he or she is called in. A successful result will involve restoring meaningful communication and bringing about a cooperative mindset that should lead to a renewed focus on outcomes, allowing the teams to solve the problems themselves.

5 Where next for partnerships?

With sound preparation, good design and a collaborative approach by all the parties, complex partnerships between the public and private sectors have the potential to deliver more innovation, greater value and more public service reform than conventional contracts. Contrary to the perception that is sometimes conveyed in the media, PPPs have continued to evolve, and there is strong evidence that they are still doing so, as government seeks to address new political, policy and commercial needs and as providers continue to innovate.

It seems likely that some new PPP models, building on programmes such as LIFT and Building Schools for the Future (BSF), will be structured as businesses, able to trade widely and provided with incentives to do so successfully. Over time, such trading will assist in creating new markets in the delivery of public services, where competitive forces will determine the price and quality of services delivered. This will complement the wider market already being created through the commercial exploitation of the physical and intellectual property of UK government and universities. If the market continues to develop along its current path and the political climate does not change dramatically, the principal role of the state in these markets will change from being overwhelmingly that of provider to that of commissioner and regulator.

This broadening of the commercialisation agenda will require closer relationships between the partners, sharing risk and reward equitably and leveraging far more of each other's capabilities. There is already some evidence of a desire to develop closer relationships between client and supplier, and some government departments have been very active in letting partnership contracts for complex programmes. This is certainly a big step in the right direction, but the execution has sometimes failed to deliver the outcomes as, in most cases, there is still too much emphasis on managing process, rather than encouraging innovation and diversity in solutions.

PFI will continue to be used as a tool for the long-term financing of assets, but it too will evolve. There is clear evidence that the strict contractualism and the emphasis on risk transfer associated with PFI contracts, makes it difficult for managers to engage in effective partnering. The financial penalties for failure tend to be so great that companies within the consortia have little incentive to cooperate for the good of the overall programme, and they are encouraged to protect their own interests. Whilst these contracts have been successful in transferring significant risk from the customer to the contractor, it is clear that this is more difficult to achieve in projects that are complex or highly innovative (such as some technology-based contracts).

In the interests of long-term customer satisfaction, improved contractual and governance arrangements are required to enable the requirements of the end-user to be taken into account over the life of the contract. Many PFI contracts have been primarily concerned with the interests of the client and the asset owner, and this can make it more difficult for the service provider to accommodate the interests of the end-user if these are not compatible with those of the asset owner. For example, it can be expensive and bureaucratic to obtain the permission to make a small change to the building, such as moving a washbasin or closing off a doorway, changes which might benefit end-users. It is likely that more flexible contractual solutions will be found as agreements mature and the partners gain experience and it is likely that this will result in yet another generation of evolution in the development of the PFI model.

If it is used in the right circumstances, a partnering approach can add immediate value to participating organisations. This being the case, there is clearly a need to provide greater emphasis on the development of a partnering approach early in any project. There are no real barriers to the development of effective dialogue and joint working prior to the commencement of a formal procurement process. The EU procurement rules then provide for a "competitive dialogue", a framework for engagement between potential collaborating organisations. New models for incremental partnering are being developed in local government, led by local authorities and supported by the ODPM. These are designed to promote joint working throughout the period of project definition, partner selection and procurement process and have the potential to provide significant benefits:

- early adoption of partnering approach, maximising the opportunity to create value;
- reduction in cost by accelerating the time to preferred partner and less duplication of effort;
- incentive for both parties to deliver ongoing value;
- reduction in risk to both parties through phased roll-out, with comprehensive review at agreed stages;
- reduction in complexity through the potential for disaggregation of complex programmes into deliverable projects which may be let separately
- lowers barriers to entry.

One Local Authority has announced its intention to set up a joint enterprise with a private sector partner to manage the delivery of all its public services. What will remain of the authority will be the elected members of the council and a small team of executives who will execute the council's policies and commission and regulate the provision of services through the joint vehicle. This may point the way to reform elsewhere in government departments and agencies and over time, it may also provide a means to reform of employment models for public sector employees.

Better coordination is required, with better leadership from the centre. There is a real need for better sharing of knowledge and best practice. Given the recognised lack of expertise within government, there may be justification for the creation of an independent body dedicated to the development of partnership practice, provision of partnering facilitation and training for partnership managers. The government needs to embed expertise centrally to reduce procurement timescales and close deals more efficiently, and then provide ongoing support to projects post-closure to ensure value continues to be generated. The new Supporting Operational Partnerships (SOPs) initiative by Partnerships UK, aimed at extracting more value from operational PPPs is a welcome acknowledgement that a shift is needed from the current focus on deal-making to provide more support for operational delivery.

6 Conclusions

Over the past two decades, the number of large, complex public service contracts in the UK has grown significantly. Associated with this has been the change from the arm's length contractual relationships that characterised early outsourcing to more sophisticated arrangements involving major risk transfer and complex service partnerships. It seems clear from reviews of some of these service partnerships that partnering has much to offer as a way forward for certain contract situations, particularly those that are inherently complex, contain high levels of risk and/or involve long-term service commitments. There are a few examples of where this approach has delivered excellent benefits and others where achievement has outperformed the alternatives even if their full potential has not been realised.

In the UK, there appears to be the political will to extend the use of partnering as evidenced by the support from the Office of the Deputy Prime Minister, the Ministry of Defence, the Department for Education and Skills, and a number of local authorities.

In spite of the demonstrable benefits and the apparent enthusiasm for partnering and partnerships among commissioning organisations and contractors, partnering is still not being used as widely as might be expected. If partnering is going to play a more significant role in the delivery of public services and play its part in delivering improved and better value services, then current understanding and practice need to be moved on to overcome the hurdles that stand in the way.

The way forward can be summarised under the four broad headings discussed in Section 3 above: purpose, people, culture and design.

- Partnering is not a panacea. It is hard work and it is expensive. It can add real value in certain situations, but it incurs an overhead in terms of cost and effort that needs to be justified by benefits over and above those achievable from conventional contractual arrangements. Even at its simplest, it requires more time and effort to be expended on communication between the parties, but as the depth of partnering increases, it demands senior management time, new governance mechanisms and additional resources. The risks are high and the potential rewards must also be high. Unless it is clear that the benefits outweigh the costs, and unless there is a shared understanding as to the reasons why this time and effort should be expended, then it is unlikely that the partnership will survive.

- Partnering is about relationships between people, and unless the right kind of people with the right kind of skills are engaged in developing, fostering and repairing the required relationships, then it is unlikely that the partnership will establish. Partnering requires the involvement of individuals who have not only the specialist experience and skills but also have an appropriate management style. “We are in this together” is the spirit. Where a successful partnership has been achieved it may be very difficult to identify which organisation people engaged in that partnership work for. These individuals are difficult to find and may not fit easily into traditional management structures and career paths, particularly where simple command-and-control management structures have been the norm.

- Although involvement of the right kind of people is crucial, it is unlikely that a partnership for the delivery of complex services will survive if it relies solely on interpersonal relationships. Such arrangements are necessarily fragile and they need to be backed by institutional patterns of trust and communication. True partnerships are not created overnight, but are developed over time by people working together cooperatively and building robust, open and trusting relationships. With successful partnerships, the culture needs to be one of mutual support and problem solving, not of blame and focus on the commercial consequences. Current policies and processes in Europe fail to reinforce the development of partnerships at the procurement stage. However, outside the competitive phase itself, through the initial engagement period and during negotiation there are opportunities to build the trust and problem solving culture that is required.

- The likelihood of partnerships succeeding can be substantially improved through good design – in procurement and negotiation processes, in contractual form and in the organisational structures, management practices and governance arrangements through which the service is ultimately delivered. Successful partnerships need partnership management structures and processes that enable optimal operational delivery and effective joint decision making, review mechanisms that enable flexibility, monitoring regimes that add value, payment mechanisms that avoid perverse incentives and encourage innovation, escalation mechanisms that enable swift resolution of disputes and governance structures that facilitate the delivery of the shared objectives. Governance structures tend to be complex and require careful design that must reflect the reality of shared responsibilities that create stress for the accountability and reporting responsibilities of directors and public servants.

Investment by all parties in developing a better understanding of these four areas and in developing the necessary people, skills and knowledge to deliver them will enable the partnership approach to become more widely used and effective in the delivery of public services.

Glossary

BSF	Building Schools for the Future
CCT	Compulsory Competitive Tendering
HMT	Her Majesty's Treasury
IPPR	Institute for Public Policy Research
JV	Joint Venture
JVC	Joint Venture Company
KPI	Key Performance Indicator
LIFT	Local Improvement Finance Trust
MOD	Ministry of Defence
NAO	National Audit Office
NHS	National Health Service
NLGN	New Local Government Network
ODPM	Office of the Deputy Prime Minister
PfH	Partnerships for Health
PFI	Private Finance Initiative
PPP	Public Private Partnership
PSC	Public Sector Comparator
PUK	Partnerships UK Limited
SLA	Service Level Agreement
SPT	ODPM Strategic Partnering Taskforce
VFM	Value for Money

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