

Contracting and Behavioural Practices in State Owned Enterprises in Uganda

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ABSTRACT

Public procurement regulations in Uganda were initiated among other objectives; to ensure accountability, transparency and value for money in all public procurement activities. Despite the presence and application of these regulations, State Owned Enterprises have continued to face challenges in contracting for works, goods and services. Evidence shows that most procurement contracts are never fulfilled because of mal practices and high transaction costs. This study sought to examine whether contracting impacted behavioural practices in procurement performance of Uganda's State Owned Enterprises.

The study mainly employed quantitative research methods, in the process of research instrument design, data collection, analysis and presentation. The study sample consisted of 160 employees picked from 20 State Owned Enterprises in Kampala and Entebbe districts of Uganda. Data was collected through a self-administered questionnaire, sorted and analyzed using both descriptive and inferential statistics.

Results reveal a positive and significant relationship exists between contracting and behavioural practices ($r = .353^{**}$, $p < .01$). Further, the regression model indicates that contracting significantly predicts Behavioural practices in State Owned Enterprises ($\text{Beta} = .763$, $\text{Sig.} = .000$).

For improved performance, State Owned Enterprises should clearly set their contract objectives to guide all those involved in the contracting process. There should be key deliverables in those objectives, which should be communicated to the relevant stakeholders.

Further, staff on the contracting team should be selected on merit. This is very important in order to avoid biased selection of contracting teams – even when some of these people do not have the required experience and expertise. This is very important because service providers can exploit such a team to their benefit once they realize that the team is weak and vulnerable.

Keywords: Contracting, Behavioural practices, Corruption, Public procurement, Uganda

INTRODUCTION

Contracting is a key aspect in the public procurement process and broadly covers issues related to Contract objectives, ability to contract and contract procedures. When State owned Enterprises (SOEs) contract, a number of transaction costs are incurred. These transaction costs include search and information costs, bargaining costs and negotiation/contracting costs (Nort, 1999; Zylberztain, 2003; European Investment Bank, 2007). However, unethical behaviour is evidenced among the procurement practitioners as SOEs carry out procurement contracts. A number of, these include absence of trust among contracting parties and opportunistic behaviour (FMA Act, 2007). According to Nj (2007) opportunism negatively affects contract execution because parties suspect themselves. Issues of trust can be significantly more important in procurement, because contracts involve a higher degree of interdependency between companies and that trust promotes efficiency, productivity and effectiveness (Morgan and Hunt, 1994; La Londe 2002; Handfield, 2002).

Measuring performance of SOEs has been increasingly recognized as a critical factor in gaining competitive advantage (Simchi- Levi et al, 2000). Earlier studies utilized several different performance measures including cost, customer responsiveness, and time (Arntzen et al, 1995). In this framework, two types of performance measures have been adopted as the necessary components of SOEs' procurement performance measurement system: i.e.; Efficiency and Effectiveness (Kulatuga et al, 2007). Particularly, procurement performance of the SOEs will be measured in terms of material price cost, user involvement, operational costs, state of inventory levels, supplier delivery reliability, adequacy of personnel, policies and procedures, information systems, user involvement (Weele, 2000; Kumar, 2000).

Public procurement regulations in Uganda were initiated among others with the objective of achieving accountability, transparency and value for money in all public procurement activities. Despite the presence and application of these regulations, State Owned Enterprises (SOEs) and other PDEs have continued to face challenges in contracting for works, goods and services. Evidence shows that most procurement contracts are never fulfilled because of mal practices and high transaction costs (PPDAA, IGG & USAID, 2006). The existing law and the structure of the public procurement process do not also enable SOEs to get the best price for goods and services so as to compete favourably with the private firms. Consequently, SOEs register high contracting costs which in turn negatively impacts procurement performance. So there was a need to empirically find out whether contracting impacted behavioural practices in procurement performance of Uganda's SOEs. Findings of this study will make a contribution in helping updating literature on the subject matter. Public procurement managers in the state owned enterprises, other public entities, suppliers to clearly identify the non-value adding processes that lead to increased procurement transaction costs. The study also provides practical recommendations to the public procurement practitioners on how to efficiently and effectively manage the procurement contracting process so as improve procurement performance of SOEs. Further, the study provides practical recommendations on how to manage the public procurement process and specifically the contracting process and suggests that the PPDA Act should be revised to cater needs of the SOEs as a special case.

LITERATURE REVIEW

State Owned Enterprises in Uganda

According to Okecho (1995), Uganda's SOEs were involved in wide range of activities that spanned from manufacturing, printing, linting, mining and food processing among others. For example the Uganda development corporation had over 40 subsidiaries in the manufacturing sector and many more companies in other fields of production. The National Textile Board was responsible for the textile industry; the Coffee Marketing Board was responsible for coffee processing and sales etc.

In all the SOEs, the government played a great role in management because there was absence of indigenous capital and entrepreneurship among the citizens.

Table 1: Ownership of SOEs before PERD

TYPE OF OWNERSHIP	NUMBER	JOINT VENTURE	MANAGEMENT CONTRACT	OWNERSHIP ISSUES
Government's direct holding	86	9	8	6
Government indirect majority	44	-	-	8
Government direct/indirect majority	8	1	1	3
Government indirect minority	3	1	-	2
Government indirect minority	5	1	-	2
Total	146	12	9	21

Adopted from Okecho (1995)

Contracting

According to the PPDA (Act, 2003) a "contract" means an agreement between a procuring and disposing entity and a provider, resulting from the application of the appropriate and approved procurement or disposal procedures and proceedings as the case may be, concluded in pursuance of a bid award decision of a Contracts Committee or any other appropriate authority.

Contracts specify the terms and arrangements for carrying out economic exchange. The term contract "refers to a formal written arrangement between two or more competent parties, which creates obligations, whereby one party becomes bound to another to do or omit to do certain acts that are the subject of that contract" (Blomqvist et al, 2005).

Contracting and behavioural practices

Prior the divestiture of most the SOEs in Uganda, there was evidence of mismanagement of the procurement contracts in terms of bribery, deception and bounded rationality (Cecchini, 1992; Investors guide to Uganda 2004; Martin et al, 1997). This unethical behaviour led to poor performance of these SOEs which later forced the government to privatize most of them and suggest new procurement reforms.

A number of behavioral aspects manifest during the procurement process and these are in form of procurement malpractices. In this study, emphasis will be put on opportunistic behaviour and trust.

Majority of research on opportunistic behaviour and trust in inter-organizational relationships is based on these widely accepted bases of trust: integrity, accountability, ability, benevolence and confidentiality (Greenberg et al, 2008). Ertel (2004) for example demonstrates the importance of integrity and benevolence by recommending that procurement contract negotiators should focus on ethical issues during negotiations rather than trying to make the “best” deal. This is because bad behaviour and absence of trust leads to the demise of procurement contracts (Khalfan, 2003).

There is also misrepresentation of facts in order to influence a procurement process or the execution of a contract by both SOEs and their respective providers. This includes collusive practices among bidders (prior to or after bid submission) designed to establish bid prices at artificial, non-competitive levels and to deprive the procuring and disposal entities of the benefits of free and open competition (Rogge, 2003). In procurement contracting, shared information and trust between and among partners is an essential element for successful contract implementation. Information sharing (IS) sometimes requires a release of strategic information which is heavily dependent on trust (Bowersox et al., 2000). Such a requirement (releasing and sharing information) is a challenging task, which requires a high degree of trust between the contracting parties. “Issues of trust can be significantly more important in procurement, because contracts involve a higher degree of interdependency between companies” (La Londe 2002). Morgan and Hunt (1994) argued that trust produces outcomes that promote efficiency, productivity and effectiveness. It is reported that the biggest stumbling block to a success of strategic alliance formation is the lack of trust and commitment (Sherman, 1992), and subsequently the trust is perceived as a cornerstone of the better performance (Spekman, 1988).

Opportunistic behaviour mostly manifests itself in two forms (Masten, 1996). The first form of opportunism usually entails one party using certain “loopholes” within a contract in such a way that does not actually breach the terms of the contract, but takes advantage of terms in the contract that are ill defined or difficult to enforce (Irene, 2005). According to Nj (2005) Such behaviour, is a moral hazard and negatively impacts contract execution (Masten, 1996). “The second form of opportunism arises when one party who perceives himself in a stronger position may renegotiate the terms in such a way that holds the other party “ransom” (Irene, 2005; Masten, 1996; Williamson, 1985).

During contracting, sensitive information may be offered to some providers by the SOE. This puts other providers in a vulnerable position leading to bounded rationality. Bounded rationality prevents

a contract from being complete, since contracting parties are not able to foresee all future events (Greenberg, 2008). Where bounded rationality exists amongst the contracting parties, greater uncertainty increases the fear of opportunistic behaviour and lack of trust undermines the ability of parties to write more efficient contracts (Bello and Lohtia, 1995; Williamson, 1991).

Opportunistic behaviour and lack of trust among parties is therefore costly. To the extent that parties can try to devise contracts that reduce the probability or costs of conflicts, the gains available to redistribute between them rise tremendously (Jeuland and Shugan, 1983).

RESEARCH METHODS

This study mainly employed quantitative research methods, in the process of research instrument design, data collection, analysis and presentation. Limited use of qualitative methods is envisaged mainly in literature and document review.

Sample design and Size

The unit of analysis is the SOE. From a population of 34 SOEs, 20 SOEs that were listed in PPDA Audit compliance report 2009 were selected. For each SOE, 8 respondents were proportionately selected using the following sampling methods; firstly, the entity was stratified into 4 strata (i.e. user department, procurement and disposal Unit, contracts committee, and contracts management committee). Stratified sampling was employed here in order to obtain a representative sample (Sarantakos, 2005) of the procurement system. Secondly, 2 respondents per strata were selected using purposive sampling to add up to 8 respondents. 2 respondents per strata were selected because these were directly involved in the procurement activities of the SOEs directly. This procedure was applied to all the selected SOEs, hence generating a total sample size of 160 as indicated in the table 1 below.

Table 2: Composition of the sample size

Strata	Number of respondents per SOE
User department	2
Procurement & disposal unit	2
Contracts committee	2
Contract management committee	2
Total	8
Total number of respondents	160 (i.e. 8 x 20)

Data collection and analysis methods

Data was collected through a self-administered questionnaire. These data were later sorted to remove incomplete questionnaire and inconsistent responses. The data were then entered in SPSS for analysis. The data were analyzed using both descriptive and inferential statistics as seen in next section.

FINDINGS

Gender of the respondents

Data were collected and analyzed in order to inform this study about the gender of respondents as seen in table 3.

Table 3: Gender of respondents

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	77	64.2	65.8	65.8
	Female	40	33.3	34.2	100.0
	Total	117	97.5	100.0	
Missing	System	3	2.5		
Total		120	100.0		

Results in table 3 reveal that most respondents were male (Freq=77, Percentage=64%). Only 40 respondents (Percentage=33%) were female.

The Relationships among the Variables

Using the Pearson (r) correlation coefficient, the nature and the direction of the relationships between the study variables was established. The results of the correlation analysis are shown in table 4 below:

Table 4: The relationship among variables

Variable	Contracting	Behavioural Practices
Contracting	1	.353**
Behavioural Practices	.353**	1

** Correlation is very significant at the 0.01 level (2-tailed).

Results in table 4 show that a positive and significant relationship exists between contracting and behavioural practices ($r = .353^{**}$, $p < .01$). It was observed from the results that contracting was

positively related to Trust. These results imply that contracting should be built on trust and that opportunistic behaviour should be avoided. Organizations with poor behavioural practices are less likely to have good contracting practices.

Regression Model

Regression analysis was used to model the strength of the independent variable in predicting the dependent variable. Table 5 presents the regression model.

Table 5: Regression model

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.201	.132		.453	.011
Contracting	.352	.021	.763	1.523	.000

Dependent Variable: Behavioural practices

Regression results in table 5 reveal that contracting predicts Behavioural practices in SOEs (Beta=.763). The model is significant (Sig. =.000).

DISCUSSION OF FINDINGS

Findings indicated that there was a positive and significant relationship between contracting and behavioural practices. Unethical practices can deprive the SOEs great value money since those involved in the contracting process have their own agenda different from that of the SOEs (Cecchini, 1992; Investors guide to Uganda 2004; Martin et al., 1997). To be more specific it was found that, contracting was positively related to Trust than opportunistic behaviour. Trust was observed to affect procurement of the SOEs this is because trust was the key determining factor as far as behavioural practices were concerned. Which would actually mean that when the SOEs are contracting, trust plays a great role in the overall execution of procurement contracts. And it has been suggested by some scholars that trust and shared information between and among partners is an essential element for successful contract implementation (Bowersox et al, 2000).

Therefore as earlier mentioned, contracting should be built on trust and that opportunistic behaviour should be avoided because if one party in contract is suspicious of the other, there is likelihood that reliable information that may be instrumental during the contracting process will not be released.

Acts like deceit, cynicism and flattery which together combined lead to opportunistic behaviour should be avoided at all costs by those involved in the contracting processes of SOEs because this can cost the SOEs a great deal of money. An example is NSSF which flouted the set criteria of procurement contracts. The SOE went ahead to award a contract to company to supply it with cars without even advertising yet this was high value procurement (Daily monitor, 2010). Even if this could have been done in “good faith” it has been questioned by the public and relevant authorities and currently those who were involved in flouting this process are being prosecuted in the courts of Law.

The above is consistent with the literature that before the SOEs were privatized, there existed improper management of the procurement contracts in terms of bribery and deception (Cecchini, 1992; Investors guide to Uganda 2004;, Martin et al, 1997).

Such unethical behaviour can be disastrous to any company if it is not curbed in the fastest time possible. Perhaps it is for this reason that some of these SOEs were privatized.

From the literature, opportunistic behaviour and trust is based on the widely accepted bases of trust: integrity, accountability, ability, benevolence and confidentiality (Greenberg et al, 2008) which were found to be key issues in as far as behavioural practices were concerned in this in this study. Ertel (2004) suggests that procurement contract negotiators should focus on ethical issues during negotiations and not try to make the “best” deal. This is because bad behaviour and specifically absence of trust leads to the demise of procurement contracts (Khalfan, 2003) which will in turn negatively affect procurement performance of the SOEs.

This is in line with the findings of Jeuland and Shugan (1983) who pointed out that opportunistic behaviour and lack of trust among parties is costly to the extent that parties will do anything to safeguard their interests and that such behaviour is a moral hazard and negatively impacts execution of procurement contracts (Irene, 2005).

However Cuganesan (2007) asserts that it is difficult to put trust in contracts and that there is a challenge in what should be indicated in the contracts as key performance indicators in relation to trust.

CONCLUSION AND RECOMMENDATIONS

SOEs should clearly set their contract objectives. Clear objectives will guide all those involved in the contracting process to pay attention to key deliverables because this is what objectives aim at achieving. These objectives should be communicated to the relevant stakeholders especially the

providers that an SOE intends to contract with. If a member on the contracting team intends to stray from these set objectives, such a character should be removed from the contracting team immediately to avoid future costs that may occur.

Those who appear on the contracting team should be selected on merit. There were instances where some SOEs selectively selected a contracting team that was not based on merit and some of these people did not have required experience and expertise. Providers can exploit such a team to their benefit putting the SOE in vulnerable situation. People with the required abilities and capabilities should be selected depending on the nature of procurement contract.

Areas of further research

Due to the scope, further research can be conducted in the following areas.

- i. The impact of the current procurement regulations on procurement performance of State Owned Enterprises in Uganda.
- ii. Behavioural practices and contract execution in public entities of Uganda- the case of Local government.

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