

The Role of Transaction Costs in Contracting Non-Governmental Organisations to Scale Up HIV Prevention Services in India

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Abstract

Background: Transaction cost economics predicts that as scale increases, transaction costs are minimised by internalising transactions to form firm-like or bureaucratic governance structures. In contrast, in India, where an estimated 5 million people are living with HIV/AIDS, HIV prevention services for vulnerable groups are being scaled up by contracting with NGOs. Using a qualitative case study approach, this paper compares the transaction costs and governance of contracting with NGOs in two states in India in the context of scaling up.

Methods: The state AIDS programmes of Tamil Nadu (TN) and Andhra Pradesh (AP) were selected according to HIV prevalence and number of government funded contracts. To obtain the NGO perspective, case study NGOs (17) were chosen, stratified by state, age, capacity, and target group. Information was collected through document review and semi-structured interviews on: contract design and negotiation; monitoring mechanisms; actions to ensure contract enforcement; asset specificity; and scaling up. Interviewees included the state AIDS programme director, NGO staff, and those responsible for design and management of the contracts. Factors affecting transaction costs and governance were identified, classified according to institutional environment, organisational, service and transaction characteristics and compared.

Results: Two contracting models were identified: direct contracting; and contracting a management agency to manage recruitment, monitoring and evaluation and technical support. Preliminary findings suggest the management agency's closer "control" reduces opportunity costs of leakage and poor quality.

Conclusion: The findings support more hierarchical governance that reduce the opportunity costs of poorly managed transactions in spite of their higher financial costs.

1. BACKGROUND

The governance of health service contracts is likely to have an important influence on their costs and effectiveness. Transaction cost economics (TCE) explores how governance arrangements are a result of the costs of friction in the contracting process (Williamson 1983). Although a departure from the neoclassical analysis of costs and efficiency, TCE uses the same analytical perspective of the utility maximising objectives of parties to a transaction. The resultant framework predicts that different organisational structures and strategies evolve in an attempt to minimise transaction costs. These, in turn, are shaped by institutional factors alongside organisational and service characteristics.

Government contracting for health services is increasing throughout the developing world as a mechanism to increase efficiency and coverage (Oliveira-Cruz, Hanson et al. 2003). The rationale for the contracting out of HIV prevention services in India arises in part from the size of the problem:

“It has been acknowledged by NACO (National AIDS Control Organisation) that NGOs (Non-Governmental Organisations) ... are necessary and complementary actors on this stage, as this is beyond the realm of either the Union or State Governments to consider tackling this problem alone”, National AIDS Control Programme (NACP) Country Scenario Update (December 1995, p34) cited in (National AIDS Control Organisation Undated).

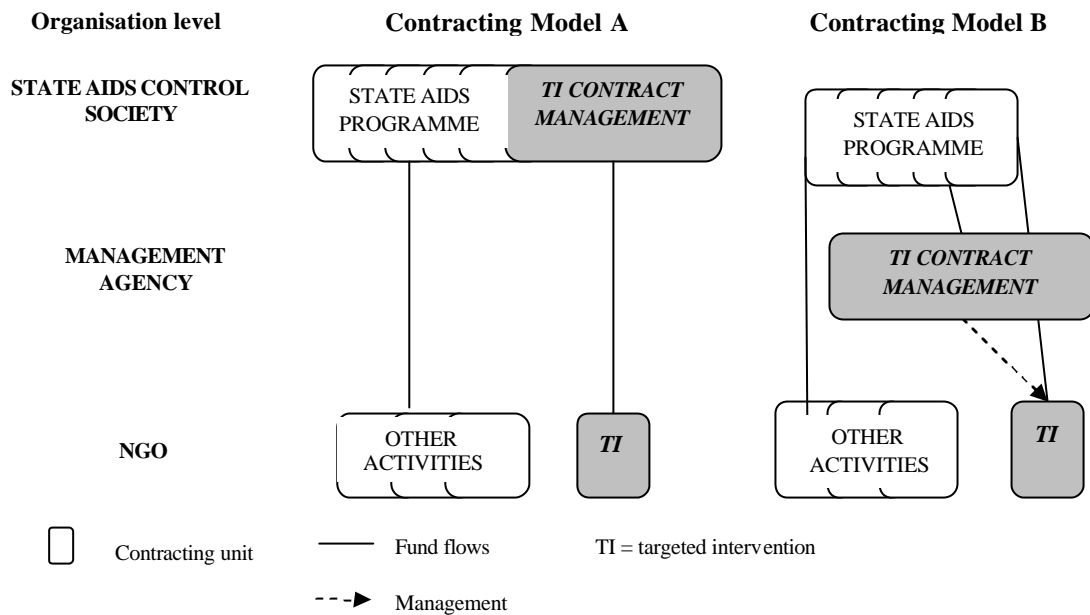
In addition, it forms part of the Government of India's (GOI) and donor community's move towards New Public Management initiatives in the health sector: moving away from the bureaucratic models of activity and expenditure control inherited from a colonial era (Bennett and Muraleedharan 2000). Delivery by the government health system implies internalisation of decision-making. This is a transaction cost minimising solution to governance of exchange where: bounded rationality makes contract specification difficult; and relational contracting is undermined by the combination of asset specificity and guile. However, in India, the extent of central control in the health sector slowed decision-making and action (Bennett and Muraleedharan 2000) and often resulted in policy that did not meet need or system failings observed at the field level (Das Gupta, Khaleghian et al. 2003; Varatharajan 2003). In spite of a concern regarding the limited capacity of government to manage contracts (Bennett and Mills 1998), evaluations of such initiatives in Cambodia, Bangladesh and Central America have shown positive results in terms of improved equity, efficiency and transparency

(Abramson 2000; Abramson 2001; Bhushan, Keller et al. 2002; Jack 2003; Soeters and Griffiths 2003; Loevinsohn Undated). In their analysis of contracting with Non-Governmental Organisations (NGOs) for HIV/AIDS services in Brazil and Guatemala, Barnett et al (2001) found increased security, the improved accountability, speed and coordination as the four main reasons for contracting with NGOs within in the national HIV/AIDS strategy (Barnett, Connor et al. 2001).

Targeted interventions (TIs) are perceived as the most effective strategy for halting the spread of the HIV/AIDS epidemic in its nascent stage (World Bank 1997). The GOI has chosen to scale up these HIV prevention efforts by contracting out services to NGOs, where little activity existed before (Bennett and Muraleedharan 2000). NGOs are seen as particularly appropriate for accessing high risk groups who are most likely to be marginalised and least able to access to public health services. The central government has decentralised the HIV/AIDS programme to the state, and in some cases municipal level, and implementation to corresponding State or Municipal AIDS Control Societies (SACS/ MACS). The SACS are then responsible for contracting NGOs to implement the TIs according to a set of guidelines issued by NACO (National AIDS Control Organisation 2004). However, the combination of the SACS' autonomy and varying donor support in each state has led to the evolution of two contracting models for HIV prevention services: A. direct contracting by the SACS; and B. employment of an intermediary to recruit, manage, monitor, evaluate and provide technical support to the NGOs (see Figure 1) on behalf of the SACS.

Scaling up, from the SACS perspective, entails increasing coverage of the target group either through expansion of target group coverage by the NGO or replicating interventions in new geographical areas. As each intervention is dependent on close ties with a particular community, it is perceived to have certain geographical limits. Consequently, to reach the next community(ies), the SACS need to increase the number of interventions by recruiting new NGOs or contracting an existing contractual partner to establish an additional intervention(s). The NACP is currently contracting with over 800 NGOs. In spite of these large numbers and the variations in contracting models, there has been no analysis of the contracting models to identify the most effective mechanism for managing the NGO contracts. To address this information gap, this paper examines the different governance arrangements and their transaction costs put in place to contract NGOs and scale up targeted HIV prevention interventions in three GOI supported programmes in Southern India.

Figure 1: Contractual units within the organizational structure for delivery of targeted interventions (TI) in India.



2. THEORETICAL FRAMEWORK

TCE and the broader framework of New Institutional Economics in which it sits, have been used to explore the impact of New Public Management innovations in the health sector (Grindle and Hilderbrand 1995; Frant 1996; Ashton 1998; Goddard and Mannion 1998; Isham and Kahkonen 1999; Jan 2000; Mills, Bennett et al. 2000; Palmer 2000; Palmer and Mills 2000; Allen 2002). Formally, transaction costs are defined as the costs of negotiating, establishing, safeguarding and enforcing contractual agreements (Williamson 1983). The nature of the transaction costs will influence how the production of the good or service is organised and governed. Transaction costs and the resulting forms of organisation are a function of certain properties underlying the transaction(s) (Shelanski and Klein 1995) and the institutional environmentⁱ in which production or service provision takes place. Assuming profit-maximisation, different organisational structures are established to minimise the transaction costs (Williamson 1983). Where transactions are costless we would expect to see governance by the market and discrete spot contracts (as assumed in the neoclassical model). As the cost of transactions rises, incentives to remove the transactions from the market are created and a move towards the internal organisation of transactions results in the hierarchical

ⁱ The *institutional environment* is the broader set of institutions (rules of the game) within which people and organisations develop and implement *institutional arrangements*.

forms of organisation i.e. the firm (Coase 1937; Alchian and Demsetz 1972). At the extreme the centralisation of organisation results in bureaucracy.

Transaction costs and associated governance are shaped by the presence or not of bounded rationality; opportunism and asset specificity, see Table 1. Drawing on this framework, Allen shows how the UK’s National Health Service could have identified a priori that the introduction of comprehensive contracting was not feasible, due to asymmetries of information, a lack of trust between payers and providers and the asset specificity of resources associated with health service delivery (Allen 2002). A better understanding of the transactions might have led to improved and more appropriate contracting or governance arrangements. A similar analysis in New Zealand shows that transaction costs are not homogenous across all health services but vary according to the type of service provided (Ashton 1998). The implication is that the methods used for governing transactions should also vary across these services i.e. one size does not fit all. Finally, Palmer (2003) documents how regional governments’ dependence on private primary care providers in areas of poor health care is a form of asset specificity that has led to relational contracting in South Africa (Palmer and Mills 2003).

Table 1: The transaction cost implications of the interaction between behavioural characteristics and asset specificity^

Behavioural Assumption		Asset specificity	Transaction cost implications
Bounded rationality	Opportunism		
0	+	+	Comprehensive contracting
+	0	+	Relational contracting
+	+	0	Spot contracts
+	+	+	Bureaucracy

^ Adapted from (Williamson 1983)

In addition to the 3 basic tenets above, uncertainty of the transaction outcome, frequency of the transaction and the institutional environment serve to further influence the transaction costs (Williamson 1983; Williamson 1996; Ashton 1998; Palmer 2000; Allen 2002). Uncertainty has a similar affect on the transaction as bounded rationality. Transactions that recur frequently are associated with higher transaction costs as the number of transactions is necessarily higher. The institutional environment can be defined as a combination of the degree to which competition is present (Williamson 1983; Palmer and Mills 2000), the nature of the regulatory framework (Williamson 2000), as well as the presence of cultural norms,

codes and conventions that shape behaviour (North 1990) and therefore the extent of opportunism.

Applying this framework to the case of HIV prevention in India, there are two key factors likely to affect the transaction costs and governance of contracts at increased scale of activity. Firstly, as scale increases, in the form of numbers of contracts, monitoring becomes more difficult due to the increased volume of activity. This compounds problems of bounded rationality and opens up possibilities for opportunistic behaviour. Second, more contracts imply more asset specific investments along with their associated opportunity costs. In addition, the monitoring of HIV prevention interventions is unusually problematic. The impacts of any specific HIV intervention are difficult to capture given the dynamics of the target populations and their sexual partners and the presence of other general population interventions. In theory, these complexities are likely to lead to what Williamson terms “serious contractual difficulties” (Williamson 1987). This paper hypothesises that the SACS need mechanisms that move towards more hierarchical forms of control to cope with the complexities of contracting with large numbers of NGOs for HIV prevention services. To explore this hypothesis, a qualitative analysis is used to compare the transaction costs and governance of NGO contracts in Andhra Pradesh (AP) and Tamil Nadu (TN).

3. METHODS

3.1 Sampling

Two Indian states, Andhra Pradesh and Tamil Nadu, were selected according to HIV prevalence (1% or higher), number of targeted interventions funded by the government (greater than 50) and agreement to participate (see Table 2). The GOI programmes in these states include the Tamil Nadu State AIDS Control Society (TNSACS); the Chennai Corporation AIDS Prevention and Control Society (CAPACS) (also in Tamil Nadu); and the Andhra Pradesh State AIDS Control Society (APSACS). TNSACS and CAPACS contract directly with the NGOs, managing the relationship from within the organisation. APSACS employs an intermediary to manage the NGO contracts.

For each programme, a case study approach was used to collect data on the transaction costs of contracting from the NGO perspective. Commercial sex worker (CSW) interventions were

selected to control for production technology and to strengthen comparative analyses. For CAPACS, TNSACS and APSACS, 2, 4 and 9 CSW interventions, respectively, were selected from a mapping of interventions carried out for this research. Where possible, NGOs were selected in consultation with the funding agency to represent a range of intervention history, levels of capacity and experience and location. At CAPACS, the only 2 CSW interventions functioning at the time of our census were selected. At TNSACS, selection criteria failed due to the inaccessibility of the NGOs and led to interviews at those NGOs available and willing to participate. In addition, to see how transaction costs varied across interventions for other target groups, 3 non CSW targeted interventions were included in the analysis (see Table 2).

Table 2: Description of the State AIDS Control Societies' Targeted Interventions Programmes in Andhra Pradesh and Tamil Nadu and the NGO Case Studies, 2002

	Andhra Pradesh	Tamil Nadu
Programmes	Merging of DFID & APSACS ⁷ programmes (2001)	TNSACS ⁸ ; CAPACS ⁹ ; USAID APAC ¹⁰
Method of contracting	Intermediary carries out contract management, technical support and monitoring and evaluation on behalf of APSACS	Direct contracting with NGOs
Number of Targeted Interventions (TIs)	101	TNSACS-65, CAPACS-7, APAC-31
Of which sex worker targeted interventions*:	18	TNSACS-21 CAPACS-2 APAC-6
Bi-lateral donor	DFID ²	USAID
No. of case studies	11	TNSACS – 5 CAPACS – 2
Of which:		
Number of sex worker targeted interventions*:	9	TNSACS – 4 CAPACS - 2
Average Age of NGO, years (range)	18 (5-89)	19 (6-38)
Average years experience with HIV (range)	5 (3-14)	7 (4-12)
Average annual expenditure of NGO, Rs* (range)	2,420,160 (224,800-105,372,462)	3,862,403 (700,000-45,784,404)
Average no. of staff* in NGO (range)	26 (10-477)	43 (8-176)
Number of NGOs with FRCA** certificates	10	5

¹United States Agency for International Development; ²Department of International Development (UK); ³Canadian International Development Agency; ⁴National AIDS Control Programme, phase 2; ⁵Andhra Pradesh State AIDS Control Society; ⁶Tamil Nadu State AIDS Control Society; ⁷Chennai Corporation AIDS Prevention and Control Society; ⁸USAID funded AIDS Prevention and Control project (not included in analysis). *N=5 for Tamil Nadu; ** FCRA = certificate which allows NGO to receive foreign funds

3.2 Data Collection

Data collection methods included both semi-structured interviews and document review. Interviews were carried out with the funding and contract management agency staff, intervention staff and a set of key informants (KI). Information was collected on the process of designing and negotiating the contract, the nature of monitoring mechanisms for the contract and actions taken to ensure the contract is enforced during the implementation period. Asset specific investments, i.e. those that are associated with an opportunity cost when allocated to use outside the services under contract, were also noted. In addition, information was sought to establish if these institutional relationships would suffice for the expansion of activities and to understand what changes would be needed to enable scaling up.

The time period covered by the material extends from approximately June 2001 to April 2003. Interviews were carried out between December 2002 and May 2003 by the author in the presence of one research assistant, following an interview guide (see appendix 1). Where permission was granted, interviews were taped. Otherwise notes were taken by both the author and research assistant and cross-checked for consistency.

3.3 Analytical approach

The interviews were transcribed and/or notes collated. Transcripts and documents were analysed by the author. First, the different institutional environments and contracting processes were documented. Key themes, related to the transaction costs of contracting with NGOs, were then identified using a transaction cost economics theoretical framework (i.e. asset specificity, bounded rationality, uncertainty, opportunism and the institutional environment) and the interview data (see appendix 2). The qualitative data were then manually classified according to those themes and comparisons made across the models.

The following section first describes the contracting processes under review and the contextual factors that constrain the ability to implement effective contracts. It then goes on to analyse the transaction cost of the two models by characterising them according to the level of asset specificity and their ability to address issues of bounded rationality and opportunism within their local contexts.

4. RESULTS

4.1 The SACS/ NGO contracting process as guided by the National AIDS Control Programme

NGOs are recruited to SACS programmes through an advertisement in the local newspaper. The NGOs submit proposals and are short-listed on the basis of certain criteria, an on-site appraisal and evaluation by a team of experts. Once a shortlist has been drawn up, the Technical Advisory Committee (TAC), consisting of technical advisors of the State AIDS Control Societies and the NGO members of the Executive Committee of the State AIDS Control Societies make the final NGO selection (National AIDS Control Organisation 2004).

The TI contracts are legal documents signed by the SACS and NGO Project Directors. The contract commits the NGO to implementing the intervention according to their project proposal and on condition of following the financial management guidelines. Nothing is stated in the contracts as to what penalties would be imposed if there were a breach of contract, nor what entails a contract breach. Given the relatively new nature of the HIV/AIDS problem and the low level of awareness even within the NGO community, technical and managerial capacity was weak at the outset of the SACS programmes (National AIDS Control Organisation Undated). Investment in capacity development, in the form of training, monitoring and experience sharing, is thus a core part of the NGO programme.

Also addressing gaps in technical capacity, the intervention design is largely shaped by guidelines issued by NACO. The SACS have closely adhered to these structures, in spite of directives from NACO stating that these are to be used with flexibility (Lenton, Hawkins et al. 2003). As well as addressing capacity weaknesses, the prescriptive approach leads to uniformity and so simplifies the appraisal of proposals and monitoring of the interventions. Due to the inherent difficulties of measuring HIV intervention impact, the NACP focuses on quantitative monitoring indicators which reflect the outputs of the interventions corresponding to the TI project components: condom promotion; behaviour change communication; STI treatment/ referral; and creating an enabling environment for the intervention. The monitoring system, otherwise, comprises financial reporting, submission of monthly and quarterly reports, a twice yearly visit from a team of experts who complete a standard reporting format and the submission of an end of year report. In addition, the NGOs attend

experience sharing workshops. All the TI programmes have undergone third party evaluations between 2002 and 2003 (Dalal Mott MacDonald Pvt Ltd 2002; Sexual Health Resource Centre 2003)

Grants are released directly to the SACS/MACS by NACO according to approved annual action plans. The SACS/MACS in turn remit quarterly expenditure statements to NACO. The contracts are renewed on annual basis subject to meeting monitoring requirements and submission of a proposal.

4.2 Contracting NGOs in Tamil Nadu: direct contracting

The Tamil Nadu NGO sector has been working on the issue of HIV/AIDS longer than any state. The first AIDS case identified in Chennai in 1986 and a core group of NGOs took up both advocacy and programme activities in the late eighties through their existing links with key vulnerable groups. TNSACS was also the first of the SACS, established in 1996 and increased the number of NGOs in the state programme from 17 in 1994-5 to over 100 in 1997/8 (Seshadri 2003). Having been documented as a model of best practice in terms of ability to spend and scaling up the number of NGO contracts (Ramasundaram, Allaudin et al. 2001; Seshadri 2003), the TNSACS programme model was exported around the country. The scale of the programme has not been sustained. Since 1999, it has been funding between 40 and 65 NGOs, each of them delivering a single TI for this funding agency. CAPACS was established in 2001. NGO contracting activities commenced in 2002, with the transfer of all Chennai based, TNSACS funded NGOs to the CAPACS programme.

Once an NGO has been recruited and commenced implementation, claiming the funding instalments require the submission of monthly reports for the NACO monitoring system and a report from a monitoring team, consisting of volunteer experts from other NGOs. Contract renewal takes place annually with the submission of a proposal for the following year reviewed by a technical advisory committee.

TNSACS has provided 8 different training sessions, attended by 137 NGOs since the start of the current funding phase. These are complemented by the experience sharing workshops, although these tend to be sporadic (NGO16). There is no uniformity of participation in training or workshops across the NGOs. An NGO advisor, with support from clerical staff, is

responsible for receiving and processing the monitoring and financial reports. Although a post is assigned for a monitoring and evaluation officer, this post is to date vacant. The SACS are therefore dependent on the staff of a core group of capable NGOs for carrying out both capacity development and monitoring for the NGO programme. In the event that malpractice is perceived to have occurred, government officials will be sent to the NGOs to investigate (TNSACS). If the malpractice is proved to have occurred the contract is stopped and the NGO is blacklisted.

4.3 Contracting with NGOs in Andhra Pradesh: the management agency approach

The state of Andhra Pradesh has been receiving support for its HIV prevention activities from a number of different sources since 1998. Prior to this, there was little HIV prevention work and limited capacity at all levels. In 2001, it was decided that all DFID (Department of International Development, UK) bilateral support to the programme should be channelled through the SACS and the management of all NGO-SACS contracts streamlined and contracted out to one agency, the Technical Resource Unit (TRU). Hindu Latex Limited (HLL) were awarded the contract through a competitive tender and are paid a pre-agreed fixed annual overhead for the management of the TRU over three years. The TRU is governed by a project steering committee which meets on a regular basis and comprises representatives from the TRU, HLL, APSACS, the state Government, DFID and NACO. DFID, however, has followed a hands off approach and distanced itself from the governance of the programme (KIs 1, 5). The number of NGO contracts rose from 23 in 1999 to 101 in 2002, all, except one, delivering a single intervention for APSACS.

The TRU employs a team of full-time experts outside standard government employment conditions, implying higher salaries and the freedom to hire and fire personnel. The TRU can also recruit agencies to provide further technical support for research, planning and development of educational materials, subject to the approval of APSACS, allowing the programme to draw in extra expertise in a timely manner. As well as providing flexibility, the TRU is a third party to the transaction and therefore able to lobby APSACS on behalf of the NGOs, if necessary, while also increasing transparency in NGO recruitment decisions.

The TRU is intrinsically involved in the contract design and renewal process. Once recruited the NGOs are invited to participate in proposal development workshops and trained in

carrying out needs assessment surveys. The proposals are subsequently revised in consultation with the TRU. Contract renewal is a consultative process and again the TRU provides direction in activities, target setting and budgeting. Written guidelines in financial management have also been provided to the NGOs to support the contracting process.

The TRU has provided a higher quantity of training sessions with greater uniformity across the NGOs than in Tamil Nadu. In 2001/02 alone they trained 57 batches of NGO staff, covering 13 technical areas. Monitoring visits are also used as a capacity development exercises. The technical team at the TRU processes the NGO reports and provides monitoring and supervision through visits to the NGOs as well as drawing in monitoring expertise from outside where necessary. If malpractice comes to light in Andhra Pradesh, APSACS requests an investigation which is carried out by the TRU. During the investigation the project is suspended and does not receive funds. Most of the investigations are initiated as a result of anonymous letters or phone calls to APSACS (TRU).

4.4 Contextual factors constraining the ability to implement effective contracting models

It is important to note at this point that a number of national level factors impinge on the ability of the SACS to contract effectively with NGOs. Firstly, contracting out takes place in an environment in which there is already significant distrust between NGOs, corruption is well known (Bennett and Mills 1998; Transparency International 2002; Das Gupta, Khaleghian et al. 2003). In the SACS programmes, the distrust is manifest in both the reports of opportunism in the interviews for this study (see Table 3), as well as an imbalance in the contractual relationship. The NGOs do not feel they have many rights within the contract, although the contractual document is signed by both parties (NGOs 9,14,18; TNSACS). Secondly, as noted above, the monitoring of the impact of HIV prevention interventions is problematic. This is compounded by: a. by the limited ability of external evaluators to access marginalised groups such as CSWs, access to whom maybe dependent on the NGOs themselves; and b. limited capacity in HIV/AIDS programming, financial management and reporting.

Table 3: Level and impact of funding delays and corruption on the implementation

	Level of problem	Impact on implementation
Corruption	<ul style="list-style-type: none"> • Mis-direction of funds (NGO 6) • Under-appointment and under-payment of staff for whom full salaries are claimed (KI ; TRU; NGOs 9,10) • Mis-reporting of activities (NGOs 6,9,10); mis-use of STI drug and travel allowances (NGO 10; TRU) • Staff and target group exploitation (NGO 9; TRU) • Bribing of government officials and TRU staff (TNSACS; KIs 1,3,4; NGOs 8,10,14,16,17) 	<ul style="list-style-type: none"> • Effective reductions in expenditure on activities • Monitoring does not reflect reality and therefore inability to identify gaps in services • Activity levels lower than reported and funded • Encourages NGOs to mis-report in order to demonstrate they have met targets • Larger budgets awarded to those NGOs willing to pay bribes rather than those with greatest need
Funding delays	<ul style="list-style-type: none"> • Funding delay of approximately 11 days per NGO (Sexual Health Resource Centre 2003) • 3 case studies experienced delays on 7 different expected releases over 4 years, ranging from a few days to 8 months • NGOs not reporting delays in quantitative form complained that were always delays (NGOs 6, 14, 9, 12) 	<ul style="list-style-type: none"> • Without being able to plan for the funds NGOs borrow or spend from their reserves (NGOs 5,8,9,10,14,16), • NGO budgets are squeezed (NGOs 5,9,19), • Cannot pay salaries (NGOs 11,15,17,18; KI 2) • Lay off staff or close the project (NGO 17). • Heighten the level of distrust between NGOs and the government.

Thirdly, the funds released by NACO to the SACS rarely meet the budget that they have approved and funds are regularly delayed (KI 5; APSACS), see Table 3. The cause of these delays relates to both the expenditure ceiling of the GOI's 10th Expenditure Plan and capacity limitations at NACO (KI5). Funding delays are further exacerbated by inadequate resources, financial, human and technical, at the NGO and SACS. Finally, NACO guidelines recommend administrative approval should be given for 3 years. In practice the contracts are renewed on an annual basis (NGOs 6,13,14,17; KI 2). This serves to increase uncertainty and, coupled with the persistent funding delays, limits the ability to plan over the longer term.

4.5 The transaction cost characteristics of contracting with NGOs at the state level

To re-state: transaction costs are defined as the costs of negotiating, establishing, safeguarding and enforcing contractual agreements. This includes the direct inputs to the process as well as the opportunity costs of poorly managed transactions such as poor quality and opportunism. The NGOs, the SACS staff and the literature all relate that the contract management needs of the NGO programme are beyond the capacity at the SACS themselves (Seshadri 2003). APSACS has introduced another managerial layer by contracting out the management of the NGO contracts and argues that the TRU is better placed to invest the appropriate time and resources (APSACS). As a result, APSACS could be seen to be increasing the transaction costs of delivering HIV prevention activities. However, these costs

need to be weighed against counterfactual costs of the management of the contracts through APSACS alone. As this counterfactual does not exist, this paper uses a comparison of the two contracting models in Andhra Pradesh and Tamil Nadu to shed light on the transaction costs of recruiting a management agency.

Where asset specificity is present, barriers to entry and exit in the contract are created and so the problems of bounded rationality and opportunism are exacerbated. As stated above, the investment in partnership with the NGOs, the capacity development and the establishing of NGO-target community links are all asset specific investments in the HIV prevention service contract. The development of funder-NGO partnerships and capacity are both associated with opportunity costs if the contract is terminated. Therefore the funder has an interest in maintaining these contracts. On the NGO side, if the NGO loses the contract, there is a real possibility of seeking funding elsewhere given the current momentum in HIV programme funding in India. On the other hand, there are also opportunity costs of losing the contract, associated with: losing the status of implementing a government supported project; seeking funding elsewhere; and funding gaps that may mean they lose the trust of the communities that they work with.

The investment in training, contact time with the NGOs and the development of partnerships with the NGOs varies across the programmes. In spite of this, the dependence on the NGOs is evident in both states. In Andhra Pradesh, it has led to falling competitiveness in the NGO sector: the second round of NGO recruitment did not involve re-advertisement but a return to the original short list of NGO applicants; and, more recently, under the TRU, when a need for re-focusing some of the less successful interventions was realised, rather than terminate contracts and re-advertise, the existing NGO partners had their projects re-designed. TNSACS presented a real concern that the NGOs might seek funding from other sources:

“If they (NGOs) have FCRA certificate (registered to receive foreign funds) they will go elsewhere” (TNSACS)

With the funding agencies tied into the contractual relationship, they require mechanisms to ensure that NGOs deliver according to plan. Informational problems are inherent in the system. The theory predicts that these will be the underlying causes of contractual difficulties. The ability of the contracting programme to deal with these informational

problems is likely to be key to its success. In spite of the central guidelines, how the systems meet this challenge varies considerably across the two states.

The monitoring system in Tamil Nadu is seen as particularly weak (Dalal Mott MacDonald Pvt Ltd 2002). Document review of monitoring records at TNSACS for this research found it impossible to track activity and financial reports: there were inconsistent sets of data across NGOs; and complete sets of reports were not available for the majority of NGOs. Quality of the interventions is also unknown (Comptroller and Auditor General of India 2004). External evaluations for Tamil Nadu did not capture quality and NGOs report that queries from TNSACS focus on the financial rather than the technical (NGOs 6,8). Other problems in the system include: lack of feedback from the monitoring teams to the NGOs (NGOs 6,8,19); insufficient resources for NGO supervision (KIs 6, 7); mis-reporting of outputs and activities (TNSACS; NGO 6); and potential bias in the monitoring team who are all staff from “competitor” NGOs (NGOs 6, 8). In addition, one key informant criticised TNSACS for simplifying its financial monitoring system. Although, the former system had caused delays, it had screened out misspending of up to £1 million over three years. One NGO had strong feelings about TNSACS monitoring:

“There is no monitoring system” (NGO 6).

The Tamil Nadu contractual relationships appear to be characterised by autonomy and distance between the NGOs and the SACS. In contrast, in Andhra Pradesh, the NGOs perceive the monitoring in the APSACS programme as a strength and a vital part of the contracting system (NGOs 2,9), placing importance on its capacity building aspects (NGOs 8,18,19), in spite of the quantitative emphasis (NGOs 9,10,12) and the time required (NGOs 2,15).

“the monitoring system is best; it allows us to make rectifications... it may be time consuming but it will improve and support our work” (NGO 18)

The NGOs also place importance on their relationship with the TRU and APSACS:

“transparency is there;anything we will discuss; Ours (relationship) is informal – we are friends” (NGO 2)

“APSACS is a good donor.... providing to the NGOs funds and guidance and training”
(NGO 5)

In Andhra Pradesh it appears that the TRU, as a third party, is able to make NGO recruitment and evaluation more transparent (KI 5). It is also better able to overcome opportunistic behaviour:

“Can’t give (external evaluators) bribes – the NGOs don’t know them” (NGO 8)

“There is very little corruption in the TRU programme..... (In other government funded programmes) those people they directly ask for money” (NGO 2)

Facilitating the identification of opportunistic behaviour are the experience sharing workshops where NGO staff exploitation was uncovered. By mid 2003, the TRU had completed investigations on 9 NGOs and five projects had been terminated, whereas TNSACS had blacklisted only one since 1996. In addition, the TRU has had and used its flexibility to remove staff suspected of being involved in bribery.

The key features influencing the transaction costs of the different models are summarised in Table 4. In TNSACS the high costs of funding delays and contractual frequency led to the streamlining of financial and other monitoring requirements. From these shifts and the apparent NGO autonomy, this analysis suggests that contract model A, implemented by TNSACS and CAPACS, operates within a relational type governance structure. However, it appears that this structure’s ability to implement the current programme size is limited with the number of NGO contracts falling during the current phase of the programme. Observations suggest that TNSACS had simply too many projects to carry out the intensive monitoring required (NGO 6; KI 2). Funding delays persist, problems with meeting monitoring requirements are evident and capacity development has not been adequately realised (NGO 6, 16, 14). Added to this, the relational contract continues to be undermined by opportunism.

Table 4: Transaction cost characteristics of contracting for HIV prevention services in India

	General contracting model	Contracting model A (TNSACS/CAPACS)	Contracting model B (APSACS)
Asset specificity	Associated with investments in capacity development, NGO links with community, NGO-funding agency partnership	Dependency on core of technically competent NGOs; limited and varied inputs to training for NGOs	Uniform capacity development; supervision, consultative intervention design and monitoring process strengthens NGO/TRU relations
Bounded rationality	Inability to measure impact; Emphasis on quantitative indicators of output/ process	Monitoring system is weak; Simplified financial reporting procedures; External evaluation for all NGOs completing 3 years of funding; Issues of technical quality not addressed.	Monitoring and supervision by team ensures TRU knowledge of programme implementation
Opportunism	Traditional barrier of distrust between NGO and government; Corruption a feature of working life in India	Opportunism persists at NGO & SACS level; simplification of financial procedures leads to further exploitation; only 1 NGO intervention stopped.	Opportunism persists but identified and penalised – 5 NGOs have had interventions terminated

By providing for greater operational independence and flexibility in recruiting technical expertise, the management agency model is able to deliver more TIs and scale up the number of contracts faster (Soni and Jani 2001). APSACS used the management agency mechanism to implement the scale up of its TI programme. The TRU plays a directive role in project design and budgeting. All NGOs receive training in both technical and managerial aspects of the programme. Capacity development inputs have led to strong ties between NGOs and with the management agency, accountability and clarity in the intervention methods. A technical team strengthens the NGO links with the management agency in a way that the single NGO advisor at TNSACS is not able to achieve. In this way, the TRU and APSACS have considerable control over the design and implementation of the individual projects (KI 1). As a result, in spite of contracting out the management of the contracts, the governance tends to the hierarchical.

The use of a management agency appears to be transaction cost reducing and better able to cope with scale. However, the question remains whether this is a result of absolute funding levels or governance and the minimising of transaction costs. Financial costs in the Andhra Pradesh programme are necessarily increased due to the addition of a management agency. Overall TNSACS TI expenditure fell from Rs 55 million in 1999/2000 to 26.5 Rs million in

2002/03. At the same time, their budget rose from Rs 40 million to Rs64 million, implying that the problems do not lie in resource constraints. The findings presented here also suggest that the extra costs involved in recruiting a management agency have helped to offset the opportunity costs of weak monitoring systems, poor technical and financial reporting capacity, NGO distrust of government (and vice versa) and opportunism, even increasing the ability to spend and scale up.

4.6 The importance of political will and leadership on the success of the contracting model

The institutional environment also influences the transaction costs and effectiveness of the governance structures. Political will, or lack of it, have been vital in shaping the programmes in Andhra Pradesh and Tamil Nadu. Political influence has both constrained and facilitated the TI programmes. At CAPACS, decision-making was constrained by political influence in the budgeting setting process (NGOs 13,14). In contrast, in Andhra Pradesh, the Chief Minister took a keen interest in the APSACS programme. It is the only Indian state which provides its own funds to the SACS and as part of efforts to improve governance requires regular monitoring reports to be submitted to the state government.

The political will in Andhra Pradesh has also resulted in the continuity of SACS Project Directors. The former Project Director (PD) at APSACS was in post for a period of 2 years. The time allowed for learning and innovation: he appointed technical project officers to work with the NGO advisor and worked with DFID to merge the TI programme and recruit the TRU. The current APSACS PD has been in post for over 2 years, also allowing for learning and a sense of ownership (KI 5). In contrast, both TNSACS and CAPACS are beleaguered by frequent changes in leadership. TNSACS PDs have stayed in post for periods of 6 to 12 months. At CAPACS, during a single year there were four changes of PD. This limits the ability of the SACS/MACS to reach full capacity (CAPACS; NGOs 13,14).

The history of project directorship at TNSACS has also demonstrated the importance of leadership and its changes. The first TNSACS PD developed the “best practice” SACS by ensuring the clean up of corrupt systems, instituting transparent financial and activity monitoring systems and so facilitating fund absorption (NGOs 6,14; KI 1) (Ramasundaram, Allaudin et al. 2001). The NGOs showed a great deal of respect for TNSACS during the

period of this directorship. They expressed disappointment in the subsequent leaders and their frequent changes, stating that programme quality had declined considerably (KI 1; NGOs 6,14,16).

Empty or inadequately filled staff posts, partially resulting from weak leadership, also delay programme activities and reduce technical capacity. TNSACS and CAPACS have suffered from empty staff posts and mixed quality of the personnel. At TNSACS, the NGOs describe mixed experiences with the NGO advisors (NGOs 6,14,16), who are crucial to the smooth functioning of the programme. In particular they expressed a complete loss in faith in the current post holder with allegations of corruption. At CAPACS, the post of NGO advisor had yet to be filled: although an appointment was made during this time, the individual only remained in post for a few months. Similarly, although the TRU are better technically resourced and have managed to fill critical TI management posts, a large under-spend in the first year of activity can be partially attributed to the 6 month absence of a Team Leader (TRU).

Political will and SACS commitment is required to build up the requisite technical, financial and management skills to ensure effective monitoring and to develop strong relationships within the NGO programme. Whereas strong leadership in Andhra Pradesh has led to a commitment to the programme and an investment in both capacity development and the facilitating of NGO partnerships, the apparent lack of leadership of the NGO programme has contributed to weakness in the contractual governance and continued distrust within the Tamil Nadu programmes at the time of the study.

5. DISCUSSION

Two models for contracting out HIV prevention services in India are described here. The model descriptions are based on a combination of document review and interviews with key personnel and supported by the author's observations of the contracting process. The documentation sourced was mixed in quality. There were conflicting figures given in different documents and it was often difficult to discern the reality. Where there was doubt, figures that are reported to NACO were used. Many of the NGOs perceived that we came from their funding agencies, in spite of explanations that we were not, and their answers could have been shaped by this perception. Interviews were conducted in English with interviewees

who had at least a Master's level degree, which are carried out in English. However, the differences between Indian English and British English complicated the explanation of some issues, possibly leading to mis-understandings. Finally, not all interviews were taped. It is recognised that there can be flaws in note taking, although the notes of the interviewer and the research assistant present were cross-checked for any divergence.

Evidence from both states demonstrates how comprehensive contracting has not been feasible given the combination of bounded rationality and opportunism. In Tamil Nadu, by reducing the demands on the monitoring system to reduce delays and depending on a core of technically competent NGOs to help roll out the programme, a more relational style contract evolved. This could not be sustained with the level of technical resources and commitment available at the funding agency. In the long run, funding delays, lack of feedback in the monitoring and evaluation system and inadequate investment in capacity development resulted. Without major change in the contracting system and renewed commitment in the form of resources, the success of this relational contracting is determined by the extent to which opportunistic behaviour of both parties continues.

Andhra Pradesh contracted out NGO contract management to a third party to overcome SACS constraints. Through the direction of intervention design, capacity development, investing in NGO partnerships and direct supervision, a more hierarchical approach to governance of the contracts has evolved. Transaction costs are also affected by the institutional environment and contract design. The analysis shows how the contracts and associated capacity development can be undermined by limitations in leadership. In addition, the annual renewal of the contract limits the ability to plan. Re-designing the financial procedures to enable longer term planning, while retaining an incentive to perform, might reduce transaction costs and improve quality of the interventions.

Under NACP the SACS have contracted with over 800 NGOs, using a highly prescriptive approach. In nearly all cases, each of these NGOs implements one intervention. The study here shows the importance of strong relationships between the NGOs and their funder or the management agency in minimising transaction costs. Consequently, increasing the number of interventions an NGO implements has potential for increasing returns to the transaction costs. Where two or more interventions are funded by the same agency, technical and managerial skills and the investment in partnership building can be shared across the interventions.

Indeed, visits to India after the completion of the data collection suggest that the SACS are now exploring the possibility of increasing the number of interventions implemented by existing contracted NGOs as well as contracting further NGOs.

As investment in HIV prevention continues and the SACS programmes evolve, the contracting models have important lessons for the next phase of the NACP as well as to other South Asian countries, where similar NGO contracting programmes are being supported by the World Bank (e.g. Bangladesh and Pakistan). The transaction cost framework has allowed the identification of key costs associated with the governance of HIV prevention services through NGO contracts in India. The analysis highlights the importance of governance systems that reduce opportunity costs arising from poorly managed transactions, in spite of higher financial costs, as inability to address capacity development, monitoring and evaluation and building relationships are likely to result in poor quality and leakage. It is unlikely that the SACS on its own, with its broader responsibilities and limited autonomy can meet these needs. An independent contract management agency offers more technical resources and the greater flexibility and transparency needed to establish a greater degree of control and so facilitate these processes. As Allen found in the NHS, comprehensive contracting is too complex and costly to implement in practice (Allen 2002). The results presented here indicate that a contract that involves more hierarchical style relationships is required, in particular where opportunism is evident. The major challenge still remains as to how to sustain these relationships as the volume of contracts increases further.

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