

New publications

The commodity boom and incomplete contracts

Cecilia Perla

In the context of increasing commodity prices, particularly in the oil and gas sector, the management of contracts that cannot be fully specified ('incomplete contracts') has taken on increasing importance. What happens when the outlook is uncertain, or when the strength of bargaining positions changes dramatically?

Cecilia Perla reviews the basics of contract theory and describes how the rise in oil and gas profits has unleashed a wave of recent renegotiations. Conventional wisdom suggests that contracts require terms and specifications for penalties in order to avoid opportunism (culminating in 'the hold up problem') as well as incentives to encourage initial investment. Different contract types provide unique advantages. 'Tax and royalty contracts' are more likely to split up front risks and encourage investment while being more prone to ex-post conflicts, for example when the value of the commodity changes significantly. In contrast, 'production sharing agreements' tend to be a more risky initial investment but less likely to create conflict during the latter stages of the life of a contract.

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Contrary to traditional notions of contract theory, the paper describes how underspecification may be a strategic choice to avoid the pitfalls associated with rigid adherence to a rules-based system. The article concludes by highlighting the elusiveness of the 'ideal' contract and offers some practical guidance for improving the management of incomplete contracts. Read her paper [here](#).

"OPI's mission is to contribute to public sector performance by providing international comparative evidence about what works best in different settings and why."



The role of trust in health care settings: does trust matter?

Sachiko Ozawa

Trust, the expectations of performance among parties in a relationship is a major determinant of outcomes in a variety of situations. In a setting which is heavily dependent on relational modes of governance and where information is largely asymmetric, trust can play a pivotal role to facilitate cooperation. In a new paper, Sachiko Ozawa reviews the concepts underpinning the connections between trust and healthcare arrangements and identifies mechanisms through which trust is fostered in healthcare. She argues that financing systems can impact on levels of trust as different types of arrangements can alter the incentives to supply or withhold information and care. Similarly, she describes how the functioning of health insurance systems depends on the expectations on the part of both the insurer and insured party. Therefore, by improving levels of trust, it may be possible to enhance the effectiveness of such schemes. The paper concludes by highlighting emerging research on the development of norms and customs as well as reputations. Read her paper [here](#).

Literature reviews on ‘public service motivation’

Martin Karlsson, Jerrett Myers

OPI has been commissioned by the General Medical Council to undertake a [pilot study](#) on the way the NHS reforms have impacted levels of motivation among clinicians at University College London Hospitals Foundation Trust. The amount of time worked in excess of contracted hours (‘donated labour’) will be recorded and analysed as it relates to worker motivation and the type and timing of various reforms.

Two reviews of the concept of ‘public service motivation’ have been completed. The first paper by [Martin Karlsson](#) looks at the theory and evidence behind public service motivation from an economist’s perspective. It begins by reviewing the implications arising from principal-agent theory, pointing out that inefficiencies can result from situations where information is imperfect about either the ability of the agent or the outcome of the project, or if the principal is limited in her ability to punish or reward the agent. As a result, incentive schemes such as performance-related pay have been devised to motivate better performance. The article points out that simple models of performance related pay may not be practical in a public sector setting due to problems arising from multiple principals, and measurement and attribution difficulties in lieu of conflicting goals and the absence of precise and reliable performance data.



An alternative source of motivation may arise from an employee feeling a 'warm glow' or caring about the outcomes of an organisation, and may be facilitated by job seekers selecting public service as a vocation, or from the organisational design in the public sector. Where public service motivation is a result of an employee's concern for outcomes, residual claimancy appears to be important. Levels of 'donated' labour tend to be less prevalent in a private setting as compared to the public and non-profit sectors and this may be because private sector managers face strong pressures to ensure that the results of additional worker effort result in higher profits. If a staff member knows that 'donating' labour is likely to result in the hiring of fewer staff, he may be less likely to 'donate' it in the first instance.

The paper concludes with a word of caution for those devising incentive schemes. If public sector employees are motivated by intrinsic concerns (as a result of either self-selection or the type of activities found in the public sector) they may be less responsive to extrinsic rewards. If the residual claimancy problem exists, it may undermine the altruistic dividend of 'donated labour'.

However, the roles of the purchaser (or principal) may result in motivating a certain type of behaviour and the outside option of workers needs to be considered as it can alter payoffs (and preferred incentives) for performance. Read his paper [here](#).

In the second paper, [Jerrett Myers](#) reviews the conceptual basis underpinning public service motivation, its attributes and results. While contractual arrangements creating 'high-powered' incentives can affect the way employees perform tasks, there is considerable evidence that non-financial motivations for performance including the development of relationships, professional rewards and altruism are pervasive. He points out that despite the increasing interest in public service motivation among both researchers and public managers, there is limited empirical data in several key areas. As values underlying motivations tend to have considerable stability over time, identifying personal and psychological characteristics that can reliably predict levels of public service motivation is one area that could yield interesting results. There is also a limited amount of evidence on the way that prospective employees select work based on missions and financial considerations. While there is an acknowledgement that under certain circumstances financial incentives can crowd out intrinsic motivations, the evidence about which mechanisms are driving this result are also rather limited. Read his paper [here](#).



Projects update

How public health sector innovations travel

Unlike the private sector, the sources of innovation in the delivery of public services and their diffusion has received little systematic attention. As a result, there is little evidence for why and how service innovations were adopted and adapted, where and why they succeeded and, as importantly, failed, what incentives motivated them, what intermediaries were involved in their diffusion and what barriers impeded their spread.

OPI is working with the India Development Foundation to analyse some 450 projects submitted to the Global Development Network in a competition for innovative health projects in order to determine the patterns of innovation and diffusion. The projects are being classified by type of innovation, geographical location, sources of funding and whether they are truly innovative, copies or adaptations from innovations elsewhere.

The results are in no way representative. However, the work is the basis for developing a typology of public sector innovations and is yielding some interesting results.

- There are few true innovations and little adaptation: most adopt models taken from elsewhere with little change.
- Diffusion times appear to be slow as expected (a decade is common).
- However, they appear to spread more rapidly between contiguous countries.
- There are more 'demand-side' innovations (attempts to persuade people to use health services) than 'supply-side' innovations (attempts to improve the way health services are delivered or their quality).
- A surprising number of projects are funded by governments but most are being implemented by non-governmental organisations.

Corporate investments in public sector capabilities forum

In addition to delivering public services such as security, justice, health and education, effective public institutions can provide private investors with formalised structures and rules that protect their investments and minimise red-tape. However, many corporations operate in countries that lack the capabilities to deliver high-quality public services. If corporations are prepared to help governments improve their performance they can create a shared gain as a public sector that performs well delivers benefits both to firms and to society as a whole.



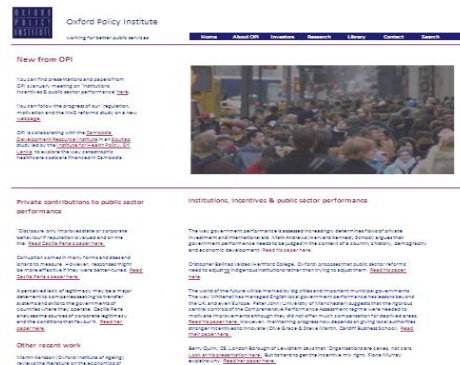
Some corporations, particularly in the oil and gas sector, are taking a long term view and investing in the development of public sector capabilities. This includes the provision of advice to governments on contract law and the regulation of extractive industry operations, advice on strategic planning and public investments, advice on public revenue management, human resource management and knowledge retention and support for procurement.

OPI is facilitating the development of a practitioner research community (PRC) on corporate investments in public sector performance composed of senior corporate managers and academic researchers. It will work on the basis of meetings, research, services and an international e-discussion forum. It will analyse contemporary issues and build scenarios of possible futures in commodity and energy markets, consider the implications of recent research on the effects of public sector failure on business activities and assemble case studies of private investment in public sector capabilities. Modest studies will fill knowledge gaps, pilot innovative study designs and develop hypotheses for further study.

The forum will build on the work that has begun under the ESRC funded [adding public value](#) and [private sector contributions to public sector performance](#) meeting series.

If you would like further information on the status of this project or to assist with its development, contact [Jerrett Myers](#).

Website



The OPI [site](#) has a new look and layout. New pages have been set up to provide more targeted information and the site menu has been redesigned for improved navigation. If you have any comments please send them to webmaster@opi.org.uk.

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