

**CONTRACTING, TRANSACTION COSTS, BEHAVIOURAL PRACTICES AND
PROCUREMENT PERFORMANCE OF PUBLIC ENTITIES: THE CASE OF STATE
OWNED ENTERPRISES IN UGANDA.**

BY

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UNIVERSITY**

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DECLARATION

I declare that this dissertation is as a result of my own effort and has never been published or submitted in any institution of learning for any award. Where it is indebted to the works of other authors, due acknowledgement has been made to that effect

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DATE

This research report has been written under my supervision and is now ready to be submitted for examination with my approval.

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DATE

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DATE

(SUPERVISOR)

DEDICATION

To my Late father; Masaba Abdul, My mother Katisi Mary and My daughter Katisi Husna.

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LIST OF ACRONYMS

SOE.....	State Owned Enterprises
PPDA.....	Public Procurement and Disposal of Public Assets Act
PDE.....	Procuring and Disposing Entity
IGG.....	Inspector General of Government
USAID.....	United States Agency on International Development
GOC.....	Government Owned Corporation
SPSS.....	Scientific Package for Social Scientists

ABSTRACT

The purpose of this study was to establish the relationship between contracting, transaction costs, behavioural practices and procurement performance of the state owned enterprises (SOEs) in Uganda. SOEs are the private arm of government that must make profit and must therefore compete favorably with other private enterprises. One key issue that must be addressed is procurement performance. Procurement performance of these SOEs is greatly influenced by contracting, transaction costs and behavioural practices. If the contracting processes of the SOEs are not well managed, transaction costs are likely to increase. This coupled with the mal-practices like opportunistic behaviour and absence of trust, puts the SOEs in more vulnerable position as opposed to the private entities.

This was a cross-sectional study and a correlation survey design was applied. From a population of 36 SOEs, 20 SOEs that were listed in the PPDA compliance Audit report of 2009 were selected. Data was collected using structured questionnaires administered to the respondents. Validity and reliability tests were performed to ensure consistence of the questionnaire. Data was analyzed using the Statistical Package for Social Scientists to establish relationships between the variables.

Findings revealed that there exists a positive relationship between contracting, transaction costs, behavioural practices and procurement performance of the SOEs. For example it emerged that as transaction costs increased, procurement performance of SOEs dropped. It was also revealed that the existence mal practices in procurement practices negatively affected procurement of the SOEs.

The study recommends that SOEs should clearly set contract objectives that will guide all those involved in the contracting process. It also recommends that mal behaviour should be avoided by those who are involved in procurement related activities; this will in turn reduce transaction costs which later improve procurement performance.

CHAPTER ONE

1.0 Introduction

This chapter presents the background to the study, statement of the problem, the purpose of the study, research objectives, research questions, scope and significance of the study. The chapter ends with a description of the conceptual framework.

1.1 Background to the Study

Globally public institutions and in particular, State Owned Enterprises (SOEs), are operating in an increasingly competitive business environment that demands aspects like cost reduction strategies, flexibility in operations, efficient and effective procurement processes in order to ensure that their performance is good and can match that of competitors or customer requirements. This means that, to a certain extent, SOEs have to grapple with converting pure private sector best practices into public sector practice in order to improve performance (The Economist, 1995; Corcoran and McLean, 1998). A study by Omran (2004) reveals that there is inadequate performance due to increased transaction costs by SOEs caused by irregular contracting processes.

In Uganda SOEs are considered public entities, so they must follow the PPDA Act as far as procurement and disposal of assets is concerned. The PPDA Act was enacted in 2003 by the Government of Uganda to decentralise and streamline all public procurement and disposal activities that were formerly performed by the tender boards. These new reforms sought to improve procurement performance in terms of efficiency, effectiveness, reduce corruption and above all achieve value for money (PPDA, 2003; Agaba, 2006; Akampumuza, Kayonga and Flavian 2009).

Despite the above reforms, public procurement performance has not improved and this has consequently led to poor performance of SOEs (Bwino, 2008). For example it takes four (4) working days to advertise and a bidding period of thirty three (33) working days, if the open international bidding method was used. This coupled with time taken to evaluate bids, contract and communicate award decisions approximately takes not less than four months as opposed to the private entities that take an average of ten (10) days. The time spent if well compounded and quantified transcends into high transaction costs (Gratton and Ghoshal, 2005), which puts SOEs in a vulnerable position as opposed to private entities. It must be noted that SOEs are the private arm of government that must compete with the private sector, so given such bureaucratic procurement procedures, SOEs can not be at exhibit the same level of performance as other commercial entities.

In line with the above, the presence of opportunistic behaviour, absence of trust and mal practices like corruption and bribery by the contracting parties has greatly affected procurement performance in SOEs. It is estimated that 7% to 9% of the total contract values are paid to corrupt officials (PPDA, IGG & USAID, 2006) while 45.5% companies expect to give gifts in order to secure contracts (World Bank Enterprise Survey, 2006). The Global Integrity Survey reports that 300 Million US dollars are lost in Uganda each year due to opportunism and other procurement mal practices. Furthermore, the Uganda Auditor General's Report (2005) estimates that 20% of the value of public procurement is lost through corruption, prompted by weak public procurement regulations. There is therefore need to effectively manage the behaviour of those concerned with managing the procurement process because this plays a great role in determining the success of the contracting process (Martin et al., 1997; Cecchini, 1992).

According to the PPDA (Act, 2003) a "contract" means an agreement between a Procuring and Disposing Entity (PDE) 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.

Contracting is one of the most important aspects in public procurement because it provides the “framework” for the economic exchange, outlining the nature and terms of the relationship, objectives of the contract, legality of parties, what is to be provided and the rights and obligations of parties to the contract (Cuganesan, 2007). Contracts fulfil an important role in minimising potential opportunistic behaviour and reducing unanticipated transaction costs. This can occur through ex ante mechanisms that bind the parties together, such as requiring parties to undertake transaction-specific investments or credible commitments to the relationship to minimise transaction costs (Williamson, 1983).

Contracting has increasingly become problematic for Ugandan SOEs because of the nature of the public procurement procedures that are prone to heavy transaction costs and mal practices. For example the teams entrusted with negotiating do not abide with the contract objectives and some times do not have the ability to contract. This coupled with the bureaucratic nature of the public procurement procedures and opportunism, leads to exploitation of the entire contracting process. This in the future leads to uncertainties and incomplete contracting (Williamson, 1985) which negatively impacts procurement in terms of efficiency and effectiveness. For example National Social Security Fund’s Nsimbe Estate Housing Project was cancelled by the IGG citing contracting difficulties like inflated costs and corruption through out the procurement process.

Procurement performance refers to how procurement as a function contributes to the set strategic objectives and the two fundamental dimensions that must be measured relate to efficiency and effectiveness of procurement because they show how successful procurement is (Neely, 1999; Chan, 2004; Chai, 2005; Khudsen, 2008).

If the transaction costs are high and there is evidence of mal practices in the contracting process, then efficiency and effectiveness will not be achieved; this will consequently affect procurement performance of the SOEs. Currently SOEs face challenges in terms of high acquisition costs of items, non involvement of key stakeholders in decision making, absence of information systems, inconsistency of delivery schedules and mal practices among others.

Therefore if SOEs continue to follow the current procurement procedures, they will be faced with the challenge of balancing between their bureaucratic and irregular contracting processes and competing with the private firms for the same customers (Bwino, 2008). For example it is difficult for National Housing Construction Company to favourably compete with the privately owned construction companies whose procurement processes are not bureaucratic.

1.2 Statement of the Problem

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 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 is need to empirically find out whether contracting, transaction costs and behavioural practices have an impact on procurement performance of the SOEs.

1.3 Purpose of the Study

The purpose of the study was to examine the relationship between contracting, transaction costs, behaviour practices and procurement performance of State Owned Enterprises in Uganda.

1.4 Research Objectives

- a) To examine the relationship between contracting and transactional costs in State Owned Enterprises.
- b) To investigate the relationship between contracting and behavioural practices in State owned Enterprises.
- c) To investigate the relationship between contracting, transaction costs, behavioural practices and procurement performance of State Owned Enterprises.

1.5 Research Questions

- a) What is the relationship between contracting and transactional costs in state owned enterprises?
- b) What is the relationship between contracting and behavioural practices in State owned Enterprises?

- c) What is the relationship between contracting, transaction costs, behavioural practices and procurement performance of state owned enterprises?

1.6 Scope of the study

1.6.1 Subject scope

The study confined itself to the area of contracting, transaction costs, behavioural practices and procurement performance of State Owned Enterprises.

1.6.2 Geographical scope

The study focused on selected Ugandan State Owned Enterprises in Kampala and Entebbe. This is because most of the key State Owned Enterprises in the country are located in Kampala and Entebbe.

1.6.3 Time Scope

The study was carried in period of 8 months.

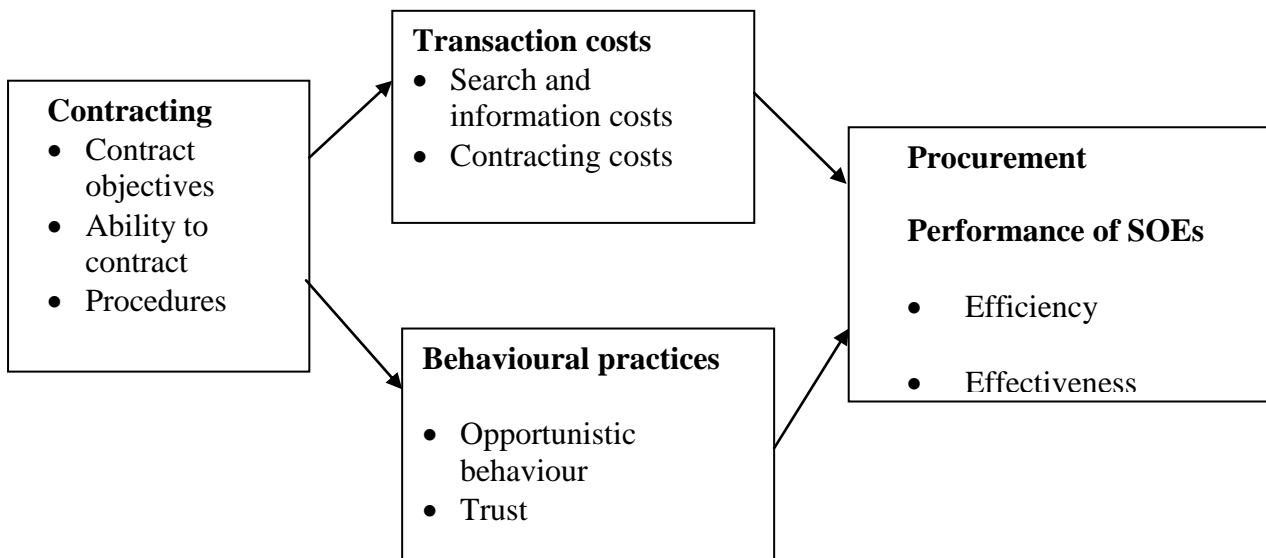
1.7 Significance of the study

- a) The research provides up-to-date literature to other scholars and researchers interested in carrying out more research in the area of public procurement, transactional costs, Behavioural Management and performance of SOEs.
- b) Findings of this study aid 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.

- c) The study 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.
- d) To the PPDAA and other government entities, 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.

1.8 Conceptualization

Figure 1: Conceptual Framework



Source: Developed based on literature Review: (Coase,1961; Demsetz, 1968; Kumar, 1995; Brooks, 1999; PPDA Act, 2003; Kumar e tal, 2005; Neely 1998; European Investment Bank, 2007; Ruben et al 2001; Dorward, 2003)

1.9 Description of the model

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 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 as SOEs carry out procurement contracts, a number of unethical behaviour is evidenced among the procurement practitioners, these fall in the categories 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 personel, policies and procedures, information systems, user involvement (Weele, 2000; Kumar, 2000).

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

The chapter reviews literature about the study variables. From literature, the concepts of the variables are described and the relationship derived.

2.1 State Owned Enterprises

There is no standard definition of a State-Owned Enterprise (SOE) or Government-Owned Corporation (GOC), although the two terms can be used interchangeably. The defining characteristics are that they have a distinct legal form and are established to operate in commercial affairs. While they may also have public policy objectives, SOEs should be differentiated from other forms of government agencies or state entities established to pursue purely non-financial objectives that have no need or goal of satisfying the shareholders with return on their investment through price increase or dividends.

Many reasons can be invoked to explain the existence of SOEs (Bozec and Breton, 2003). These include facilitating regional development and developing strategic sectors. In most cases, SOEs are created with the unique and clearly stated goal of generating profits (Ramanadham, 1991; Gray, 1984; Gordon, 1981). Actually, the nature and functions of SOEs are not very different from those of the privately-owned enterprises (POEs). As public sector organizations, SOEs are expected to manage social issues (Ouellet, 1992). Their activities are mainly directed towards citizens as the first beneficiaries, and the whole society is considered as whole.

2.2 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).

2.3 Transaction costs

The concept of using transaction costs to explain the organization of firms and the way in which they interact along a supply chain gets its roots in the works of Coase (1937). While there is no standard definition of the term “transaction costs”, they can be broadly interpreted to include costs associated with market exchange, including costs of searching for options, negotiating contracts and enforcing agreements (Singh, 2008). They arise wherever there is any form of economic organization, i.e. within a vertically integrated firm or in a market (Hobbs, 1996).

In procurement, transaction costs fall into three main classifications: information costs (costs related to searching for providers), negotiation costs (contracting costs), and monitoring (or enforcement) costs. SOEs incur costs in the search for information about products, prices, inputs and buyers or sellers (Hobbs, 1996). Negotiation costs arise from the physical act of

the transaction, such as negotiating and writing contracts (costs in terms of managerial expertise, the hiring of lawyers, etc.), or paying for the services of an intermediary to the transaction (such as an auctioneer or a broker). Monitoring or enforcement costs arise after an exchange has been negotiated. This may involve monitoring the quality of goods from a supplier or monitoring the behaviour of a supplier or buyer to ensure that all the pre-agreed terms of the transaction are met (Hobbs, 1996). Also included are the costs of legally enforcing a broken contract, should the need arise. This is consistent with Coase (1961) who asserted that in order to carry out “a transaction by means of an exchange on the open market”, it was necessary for one to find out who was willing to participate in exchange process, to inform potential traders that some was willing to trade on specific terms. He further pointed out that there was need to conduct negotiations which would lead to a contract and inspections that were necessary to make sure that contract terms were being observed.

2.4 Behavioural practices

These are acts that are manifested in any transaction or dealing and these broadly relate ethical issues. In this study attention is given to opportunistic behaviour and trust. “Opportunism refers to the incomplete or distorted disclosure of information, or calculated efforts to mislead, distort, disguise, obfuscate or otherwise confuse” (Williamson, 1985). Such behaviour greatly affects agreements between parties and as such, there is need to avoid opportunism (Bergen et al, 1992; Brown e tal 2000). Findings by Grzeskowiach et al, (2008) reveal that opportunism is a general behavioural problem in contracting. Hunter et al, (1982) and Grzeskowiach et al, (2008) view opportunism in three distinct moral standards i.e. flattery (strategic behaviour designed to influence the other party in contract), Cynicism (violation of set laws and standards) and deceit (deliberate act or omission of facts by one party intended to create support for false belief or taking advantage of the situation).

According to Morgan and Hunt (1994), trust is existent when one party has confidence in an exchange partner's reliability and integrity. To Anderson and Narus, (1990), trust is viewed as the firms' belief that the other company will perform actions that will result in positive outcomes and not in negative outcomes for the firm. Scholars like (Morgan and Hunt, 1994; Ganesan, 1994; Kumar, 1995; Ertel, 2004; Greenberg et al, 2008) present accountability, integrity, honesty, ability, benevolence, credibility, reliability and confidentiality as key issues in trust.

According to Adobor (2005) management theorists identify trust as one critical element for performance in inter-firm alliances or strategic partnerships. Trust appears important in inter-firm alliances because alliances entail substantial risk (Das, 2005) and it aids in lowering transaction cost associated with economic exchange (Zaheer and Venkatraman, 1999), and reduces opportunism (Wathne and Heidi, 2000). Trust allows for a free exchange of useful information (Larson, 1992; Adobor, 2005).

2.5 Procurement Performance

In order for an organization to achieve its goals of satisfying its customers, it must measure its performance. Among key areas to be measured is procurement performance. But there is no best way to measure procurement performance for example Syson (1995) states that "one of the problems that arises in respect of the procurement function, is that there is no common opinion on what should be measured". However it is broadly accepted by scholars like (Kotter, 1978; Neely, 1999; Knudsen, 1999; Cavinato and Kauffman, 1999; Van Weele, 2000) who assert that procurement performance can be measured by using two dimensions i.e. Efficiency and effectiveness. Efficiency measures how successfully the inputs have been transformed into outputs while Effectiveness measures how successfully the system achieves

its desired output (Kumar, 2005). Effective procurement practices offer high level of transparency, accountability and value for money while efficient procurement practices are those that meet the needs of customers, achieve optimum conditions and value in regard to allocation of scarce taxpayers resources, efficient use of public resources, manage risk and pose a less liability to the public(ministry of fence handout 2004; Mbabazi etal, 2008)

2.5.1 Procurement performance measurement

A procurement performance measurement system is supposed to provide the purchasing department with unbiased and objective information regarding procurement performance (Knudsen, 1999). According to literature the generic measures performance measures include, time, service quality, resource utilisation and cost among others.

This study adopted the two dimensions of efficiency and effectiveness as far measuring procurement performance was concerned.

Whereas the aims of the public procurement are worthy, the procurement processes may not achieve the end objectives of the SOEs since they must compete with other private firms (Bwino, 2008). Given the nature of the procurement procedures and specifically the contracting process, SOEs may not register the same level of procurement performance as private firms in terms commercial considerations like discounts, payment terms, etc . An effective procurement performance management approach must be put in place for the SOEs to understand what is involved (Moran and Avergun, 1997) while usefully embedding change (Johnson and Scholes, 1993). To be effective though, a performance management systems must focus on “measuring the correct things” (Speckman et al., 1994; Leenders, 1998; White and

Hammer-Lloyd, 1999). SOEs must therefore measure their performance in relation to the procurement processes.

2.6 Public procurement process

These are the successive stages through which public organizations/entities acquire goods and services. The public sector procurement process begins with procurement planning, an advertisement to tender for services, projects and works based upon documents and specifications usually developed within the responsible ambit of some level of government (PPDA Act, 2003; Balunywa, Mwebaza, Sserwanga and Matama et al, 2009).

The tender documents are in turn considered by contractors or providers who later submit their tenders for evaluation (Steane and Walker, 2000; Balunywa et al, 2009). After evaluation, Services or projects are awarded by the state entity (principals) to the successful contractor who acts as an "agent". This entire process presents costs and as a result the public entities incur a number of procurement transaction costs (Steane and Walker, 2000).

It is said that the costs of both public and private institutions have increased highly and unpredictably because of the procurement processes that are complex, unrealistic and expensive (summit business review, 2009).

2.7 Contracting and Transaction costs

According to transaction cost economics literature (Nj, 2007), the criterion for efficient contract management is to minimize contract costs (Bello and Lohtia, 1995). Such costs arise from impediments in reaching and enforcing agreements within a procurement contract and are associated with activities such as bargaining (Nj, 2007). In contracting, objectives of the

contract must be determined so as to guide the entire process. Usually what needs to be achieved at the contract must be communicated early enough. There must also be governance structures in terms of clauses and conditions if the contract is to be successful.

As technocrats meet to agree on the specific clauses to be enforced by either party in the contract, a number of costs are incurred; these may include contract amendment costs, allowances for contract negotiators and time. These have been classified by the scholars as transaction costs which are as a result of an economic exchange and can not be avoided but can be mitigated by ensuring that every each party in the transaction attains value for money. In public procurement costs are manifested at this phase for example it may take up to six months when SOEs are still negotiating. The contracting process can last this long because of contracting difficulties like unrealistic objectives set by the SOEs or instances of corruption geared towards inflating the contact values.

The PPDA audit report (2008) pointed out that some government agencies did not even have evidence of contract award decisions. Contracts had been awarded to providers without award letters. This meant that some contractors could have exploited such loopholes to rescind the contracts at any time in case of disagreement. The report further pointed that user departments were not involved in the contracting processes leaving such contracts at the mercy of those involved in drafting them. According to this very report contracting was the most abused stage by PDEs and consequently the represented the number one cause of unwanted costs.

In certain cases contracts are signed with the providers but the public entities take long to enforce and this forces providers to abscond the contracts which takes back the public entities

to the first stage since market conditions would have changed drastically this simply increases the costs of transacting (Summit Business Review, 2009). Therefore in the contracting stage is mismanaged, unnecessary costs will be incurred for example costs of re-advertising the procurement opportunities, allowances for the contracting teams, correcting defects among others . Such costs will later translate into high transaction costs for example enforcement costs which will later negatively impact procurement performance of the SOEs.

2.8 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 etal, 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 etal, 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 the 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).

2.9 Contracting, Transaction Costs, Behavioural Practices and Procurement

Performance of State Owned Enterprises

The procurement decisions taken at the contracting stage of the procurement process can not establish governance forms that facilitate better procurement performance of public entities through price, output control, and behaviour management throughout the contracting process (Erickson & Laan, 2007). For example Ethical codes of conduct in contracting are seldom used (Erickson & Laan, 2007). In contracting, trust is the most important variable in relational exchange (Lambe et al., 2001) and is considered to be the foundation of future successful strategic partnerships. The importance of trust in contracting is that all opportunistic behaviour will be avoided and the contract will achieve all the stated objectives without any party losing.

The behaviour of procurement practitioners especially trust and cooperation is affected by the procurement procedures (Latham, 1994; Egan, 1998) yet good behaviour is a key factor that

contributes to project success (Cheung et al., 2001). Reports commissioned by the World Bank and USAID indicate that fraud, mistrust and opportunistic behavior are common during the contracting stages of the public procurement process; It is common for companies to pay bribes for public contracts and it is alleged that procurement officials and administrators inflate the cost of procurement contracts in collusion with private suppliers and share the non-reported difference, which can be as much as five times the true cost. This greatly affects the performance of state owned enterprises because there will be no value for money.

Furthermore, the constant replacement of employees due to fraud tendencies creates inefficiencies, since a new learning curve must be climbed by all the parties each time (Cox and Thompson, 1997). This non value adding activities erode sustainable contracting leading to poor procurement performance (Ingirige and Sexton, 2006). Scholars suggest that it is hard for SOEs to register good procurement performance due to high transaction costs and poor procurement practices (Williamson, 1996; Das and Teng, 2001)

Better procurement performance results from clear contracting objectives and efficient governance of contracts which requires tailoring of procurement procedures to contracting characteristics (Williamson, 1985; Aulakh et al, 1996; Eriksson, 2006). Hence, it would be interesting to investigate the current contracting procedures from a transaction cost analysis, and behavioural perspective in order to examine their relationship with the procurement performance of SOEs.

2.10 Conclusion

Contracting costs arise from impediments in reaching and enforcing agreements within activities such as bargaining, contracting, monitoring performance, and activities that are not

directly productive but which are engaged in only as a consequence of a need to coordinate procurement activities. Poor behavioural practices also affect the contracting process and contribute towards transactional costs and consequently affect procurement performance.

From the above it can be concluded that for the current public procurement processes (specifically the contracting stage) cannot help the SOEs to register better performance given that transaction costs and the unethical practices that are evident in the contracting process.

CHAPTER THREE

METHODOLOGY

3.0 Introduction

This chapter entails the methodology that was used during the study. It describes the research design, the study population, sampling procedure, methods of the data collection and analysis and presentation, measurement of variables, reliability and validity tests and the limitations of the study.

3.1 Research design

The study adopted a cross sectional study. A correlation survey research design was applied to establish the relationship between contracting, transaction costs, behavioural practices and performance of State Owned Enterprises.

3.2 Study population

The current population of State Owned Enterprises (SOEs) is thirty six (36) were the Ugandan Government is the majority shareholder and they are required to use the PPDA laws (Public Enterprise Reform and Divesture Act, 1993; Public Finance and Accountability Act of 2003; Public Utility Sector Reform Project, 2001; Parliament of Uganda, 2009; Monitor Business Directory, 2009).

3.3 Sample design and Size

The unit of analysis is the SOE. From a population of 36 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 3.0: 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)

3.4 Sources of data

3.4.1 Primary sources of data

Primary data was obtained from respondents using self administered questionnaires to get data on the study variables.

3.4.2 Secondary sources

Secondary from reports, journals, text books among others were used. Information got from the secondary sources was in form of literature and used too a great extent in chapter of two of this report.

3.5 Measurement of variables

The responses to the statements in self administered were anchored on five Linkert point scale ranging from 1- strongly disagree to 5- strongly agree. The variables were measured using scales obtained from the works of previous scholars and adopted the Ugandan setting.

- i. Contracting was measured in relation to the terms of contract objectives, contract Governance and ability to contract (Nj, 2004; Loader, 1997)
- ii. Transaction costs was measured using the search and information costs; information gain, information relevancy, information reliability, time (Arun, 2009) while contracting costs were measured in relation to time spent while drafting contracts, negotiating, agency costs and contract governance costs (Williamson, 1985; Steane and Walker, 2000; Bello and Lohtia, 1995). Enforcement costs were measured in relation to monitoring costs, legal costs, communication costs among others (Grimwood, 1996)
- iii. Behavioural practices were measured through examining opportunistic behaviour and trust. Trust was measured in terms of accountability, integrity, honesty, ability, benevolence, credibility, reliability and confidentiality (Morgan & Hunt, 1994; Ganesan, 1994; Kumar, 1995; Ertel, 2004; Greenberg et al, 2008). While measures like deceit, cynicism, flattery, misrepresentation and exploitation were used to measure opportunistic behaviour (Cramtom & Dees,1993; Lewich & Robbinson, 1998; Grzeskowiach)
- iv. Procurement performance of SOEs was measured using efficiency and effectiveness. Efficiency was measured using cycle time, quality, and internal customer satisfaction. Effectiveness was be measured by examining the information system, personel, policies and procedures. Scholars like (Neely, 1998; 1996; Chan and Chan, 2004; Shenhar, 1997; Kumar et al, 2005) have used these measures.

3.6 Research Instruments and data collection.

Data was collected using structured questionnaires that were administered to the respondents who were requested to fill in the various parts of questionnaires.

3.6.1 Administration

The researcher got an introduction letter to the SOEs. Appointments were made with the respondents to determine the appropriate times that questionnaires can be administered. Permission was also sought from the company administrators before the questionnaires are administered.

3.6.2 Data analysis

Editing and coding of data was done when questionnaires were collected and there after data was analysed using the Statistical Package for Social Scientists(SPSS), different tests were performed to analyse the data collected. The relationship between contracting, transaction costs, behavioural practices and procurement performance of SOEs was determined by using correlation statistics. Multiple regression analysis (which determines the predictive strength of the independent variable on the dependent variables), was used to answer objective three (to investigate the relationship between contracting, transaction Costs, behavioural practices and procurement performance of State Owned Enterprises).An Exploratory Factor Analysis method was used to extract the salient factors in the model as well as data reduction for further analysis.

3.7 Reliability Testing

A questionnaire was developed in harmony with the guidelines specified by Sekarani (2003).

Item analysis was done to check whether the items in the instrument were correct and a pre-test was carried out using focus group and experts, to check for validity and reliability.

Reliability (internal consistence and stability) of the instruments was tested basing on Cronbach (1951). Coefficient Alpha values of 0.5 and above were accepted.

Table 3.1 Reliability testing

	Cronbach's Alpha
Contracting	0.900
Transaction	0.866
Behavioural Practices	0.788
Procurement Performance Of SOEs	0.883

Source: Cronbach (1951)

3.8 Limitations

- i. The researcher anticipated a challenge in receiving all questionnaires full filled from the respondents because of the uncooperative nature of respondents for fear of losing information classified. However the research used an introduction letter and guaranteed the respondents that the information provided would be treated as confidential.
- ii. The time accorded to this study may not have been adequate to permit a comprehensive study of the research problem. However the study population and sample size chosen were adequate to examine relationships between the variables.

- iii. The researcher also incurred high costs while carrying the study. These related to data collection, communication among others yet the funds for the study were limited.

- iv. There was limited literature in the area of the public procurement in relation to transaction costs, behavioural management and performance of SOEs in Uganda. However the researcher took advantage of online libraries to access the relevant literature.

- v. There was a challenge finding measures standard measures of the variables. To counter this challenge the researcher used measures that had been adopted by other scholars.

CHAPTER FOUR

PRESENTATION OF FINDINGS

4.0 Introduction

This chapter presents study findings in relation to the objectives which are:

- i. To examine the relationship between contracting and transactional costs in State Owned Enterprises.
- ii. To investigate the relationship between contracting and behavioural practices in State owned Enterprises.
- iii. To investigate the relationship between contracting, transaction Costs, behavioural practices and procurement performance of State Owned Enterprises.

4.1 Response Rate

One hundred and sixty (160) questionnaires were administered and 120 usable ones were returned, giving a response rate of seventy five (75%). According to Rubin and Earl (2009), a response rate of 70% is very good for analysis and reporting.

4.2 Characteristics of respondents and respondent enterprises

This section describes the respondents according to their academic qualifications, age, sex, range of sales and number of employees

i). Academic qualifications of the respondents

The table below presents the academic qualifications of the respondents. Majority of the respondents had undergraduate degrees (43%), 28% masters degrees 10% professional qualifications, 9% diploma qualifications and 6% had attained high school education as shown in the table below;

Table 4.1 Academic qualification of the respondents

Qualification		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	High school	7	5.8	5.9	5.9
	Diploma	11	9.2	9.3	15.3
	Degree	52	43.3	44.1	59.3
	Masters	34	28.3	28.8	88.1
	Professional	12	10.0	10.2	98.3
	Others	2	1.7	1.7	100.0
	Total	118	98.3	100.0	
Missing	System	2	1.7		
Total		120	100.0		

ii). Age of respondent

The results showed that majority of the respondents were between 25-35 years of age (42%) and 36-45 years (27%) while the distribution of respondents with ages below 25 years and / or between 46-55 years was about 15% and 16% respectively as shown in the table below.

Table 4.2 Age of respondents

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Below 25 years	18	15.0	15.8	15.8
	25-35 years	48	40.0	42.1	57.9
	36-45 years	31	25.8	27.2	85.1
	46-55 years	17	14.2	14.9	100.0
	Total	114	95.0	100.0	
Missing	System	6	5.0		
Total		120	100.0		

(iii) Gender of the respondents

66% of the respondents were male and 34% were female. The results are shown in the table below.

Table 4.3 Sex of the 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		

(d) Sales revenue per year

The analysis of sales revenue per year indicated that most state owned enterprises were in the category of more than 360,000,000/= sales revenue per year (46%), 33% of the SOEs experienced sales revenue below 12,000,000/=, while 16% had sales revenue between 13,000,000 – 360,000,000/=. These results are presented in the table below;

Table 4.4: Sales revenue per year

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	below 12,000,000	39	32.5	37.5	37.5
	13,000,000-360,000,000	17	14.2	16.3	53.8
	more than 360,000,000	48	40.0	46.2	100.0
Total		104	86.7	100.0	
Missing	System	16	13.3		
Total		120	100.0		

(e) Number of employees employed by the SOEs

The results in the table below show that most State Owned Enterprises employed more than 50 employees (41%) while those that employed below four employees and between 5-50 employees constituted about 31% and 28% of the sample respectively.

Table 4.5 Number of employees

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Below 4 employees	35	29.2	31.0	31.0
	5-50 Employees	32	26.7	28.3	59.3
	More than 50 Employees	46	38.3	40.7	100.0
	Total	113	94.2	100.0	
Missing	System	7	5.8		
Total		120	100.0		

4.3 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 the table below:

Table 4.6 The relationship among variables

	1	2	3	4
Contracting (1)	1			
Transaction Costs (2)	.441**	1		
Behavioral Practices (3)	.353**	.148	1	
Procurement Performance of SOEs (4)	.653**	.145	.533**	1

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

* Correlation is significant at the 0.05 level (2-tailed).

4.3.1 The Relationship between Contracting and Transactional Costs

The results in the table above showed that there exists a significant and positive relationship between contracting and transactional costs. These results indicated that as SOEs contract, transaction costs increase ($r = .441^{**}$, $p < .01$). Such transaction costs arise because of the unclear contracting processes for some contracts are cancelled and the SOEs have to re-advertise procurement opportunities to the potential

contractors. It must be noted that advertising itself is a search and information costs under transaction costs.

4.3.2 The Relationship between Contracting and Behavioural Practices

A positive and significant relationship was observed to exist 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.

4.3.3 The Relationship between Contracting and Procurement performance

On the relationship between Contracting and procurement performance of SOEs, the study revealed that there existed a strong positive relationship ($r = .653^{**}$, $p < .01$). In addition, Procurement performance was also positively related to contract objectives, ability to contract, and procedures. This implies that SOEs with a good procurement performance are associated with good contracting systems. It is therefore evident from the findings that if SOEs are to improve on their procurement performance attention should be devoted towards strengthening the contracting process and avoiding activity that would undermine the successful working of the contracting process.

4.3.4 The Relationship between Behavioural practices and Procurement performance

Behavioural practices and procurement performance were significantly and positively related to each other ($r = .533^{**}$, $p < .01$). These results further highlight the fact that if elements of behavioural practices especially if Trust is well addressed, the institutions

will realize an improvement in the procurement performance. This is because trust was found to be a very strong factor in determining behavioural practices.

4.4 Regression Model

Regression analysis was used to establish the variance in the procurement performance of SOEs (dependent variable) that is explained by the independent variables which are contracting, transaction costs, and behavioural practices.

Contracting, transaction costs and behavioural practices predict nearly 55.8% (adjusted R square = 0.558) of the observed variance in procurement performance of SOEs. The model was a good fit and significant ($F=49.4$; $p<0.01$) and this means that the independent variables that were used accurately account for the variance in the dependent variable.

Findings revealed that contracting was the most important factor, predicting nearly 60% variance in procurement performance of SOEs for every unit percentage positive change ($Beta=0.595$; $p<0.01$). These results suggest that SOEs that exercise good contracting processes have higher procurement performance levels and vices versa.

It was also established that behavioural practices contributed positively to procurement performance of SOEs with a prediction power of about 40% change in procurement performance for every unit percentage change in behavioural practices (holding other factors constant). This implies that SOEs that emphasized good behavioural practices in their procurement systems are more likely to attain high procurement performance.

However, transaction costs were found to have a negative effect on procurement performance of SOEs ($B=-0.190$; $p<0.01$). It was found out that -19% of procurement performance was as a result of a unit percentage change in Transaction costs. This implies that the more an SOE perceives the transaction costs as high, the less likely will be the performance of its procurement systems. These results are shown in the table below;

Table 4.7 Regression model of Contracting, Transaction costs, Behavioural practices on Procurement performance

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Adjusted R ²	F	Sig.
	B	Std. Error	Beta					
(Constant)	.115	.318		.362	.718			
Contracting	.596	.071	.595	8.346	.000	.558	49.408	.000(a)
Transaction costs	-.233	.086	-.190	-2.694	.008			
Behavioral practices	.516	.087	.399	5.913	.000			

Dependent Variable: Procurement Performance State Owned Enterprises (PPSOEs)

CHAPTER FIVE

DISCUSSION, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents a discussion of the findings, conclusions drawn from the study findings and literature, recommendations. The chapter ends by suggesting areas for further research.

5.2 Discussion of findings

5.2.1 Contracting and Transactional costs in State Owned Enterprises

As earlier mentioned in the literature the principle for efficient contract management is to minimize contract costs (Bello and Lohtia, 1995) and that such costs arise from impediments in reaching and enforcing agreements within a procurement contract (Nj, 2007). Therefore if the contracting stage is not well managed, there is likelihood that SOEs will incur high transaction costs. Literature further points out that, contract objectives must be determined so as to guide the entire contracting process and that what needs to be achieved at the end contract must be communicated early enough. The implication here is that failure to communicate what must be achieved by the contract may increase the contracting costs which would later increase the transaction costs and consequently affect the performance of SOEs.

Findings from this study indicated that there exists a significant and positive relationship between contracting and transactional costs. For example before SOEs contract, they must look for the person/firm they are going to contract with; perhaps that is why the study found out that as SOEs contracted; a number of transaction costs were incurred and to be specific contracting was found to be positively related to

search and information costs and enforcement costs. This means that SOEs incur costs during the contracting stage and therefore there is need for all officers involved in such activities to effectively and efficiently manage the contracting process. The above findings are consistent with the findings of NJ, 2007 and Summit Business Review, 2009) who found that as public entities contracted a number transaction were incurred since this was a pure market exchange.

Contract objectives, a well defined process and People with ability to contract must be clearly assessed and if such issues are not given attention, transaction costs are likely to increase.

5.2.2 Contracting and Behavioural practices in state owned enterprises

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 a 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 a high value procurement (Daily monitor, 2010). Even 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 moral hazard and negatively impacts execution of procurement contracts (Irene, 2005).

However Cuganesan (2007) asserts that it is difficult to 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.

5.2.3 Contracting, Transaction costs, Behavioural practices and Procurement performance

Findings revealed that contracting, transaction costs and behavioural practices had an effect on procurement performance of the SOEs. The above findings are in line with (Williamson, 1996; Das and Teng, 2001) who found that it was hard for SOEs to register good procurement performance if transaction costs were high and if poor procurement practices were evident.

From the above it can be said that if contracting, transaction costs and behavioural practices are not well managed, procurement performance of SOEs is likely to be affected negatively. The contracting objectives, procedures and the capabilities of those who contract on behalf of the SOEs must be critically assessed so as to avoid future negative consequences for example if there are no clear objectives or

procedures that must be followed, this means that the procurement contract made may be costly or at worst not even take place. If an SOE does not contract with good providers, costs of enforcing a contract will arise. Suppliers may have a tendency of not respecting the terms and conditions especially if they believe that they are in a better bargaining position than the SOE which may later lead to litigation.

Findings from this study again show that behavioural practices contributed positively to procurement performance of SOEs with a prediction power of about 40% change in procurement performance for every unit percentage change in behavioural practices (holding other factors constant). Procurement in the SOEs is affected by bad procurement practices for example the Global Integrity Survey reported that 300 million dollars are lost in Uganda each year due to opportunism and other procurement mal practices. Trust and opportunistic behaviour according to this study were critical in determining the effectiveness and efficiency of procurement contracts. Scholars like Adobor (2005) identify trust as a critical element for performance in strategic partnerships and that trust aids in lowering transaction costs associated with economic exchange (Zaheer and Venkatraman, 1999), it also reduces opportunism (Wathne and Heidi, 2000).

Therefore for better procurement performance to be achieved in terms of effectiveness and efficiency, there is need to firstly come up with a well formulated and thought contract (determine the objectives, have procedures to follow and guide those involved in the process and those contract on behalf of the SOE should have the ability to contract), secondly managing transaction costs and avoiding unethical

behaviour in all procurement related activities. Procurement performance measures should also be established to work as a guide.

5.3 Conclusions

Contracting is fundamental in determining procurement performance. If the contracting process is mismanaged by the SOEs, transaction costs will increase. Increased costs mean that procurement will be affected in terms of efficiency and effectiveness.

Therefore for an SOE to achieve better procurement performance it is important for it to set clear contracting objectives that will determine what to be achieved at the end of the contract.

There should be clear contracting procedures or governance structures that must be followed throughout the contracting process and above all, those involved in the contracting process should have the ability to contract so as to avoid future contracting costs and non execution of the procurement contracts. If a contract is not performed then the costs of enforcing such a contract will rise tremendously. Increased costs mean poor performance.

Transaction costs impact procurement performance, the higher the transaction costs the lower the procurement performance of the SOE. It is widely accepted that transaction costs are in three forms, i.e. search and information costs, contracting costs and enforcement costs. SOEs incur all these costs, for example they look for providers and when looking for these providers, costs are incurred such as communication costs, advertising, physical visits among others. When an agreement has been reached between the SOE and providers, enforcement costs that get the contract performed are incurred by the SOE. These costs are in form sending reminders to suppliers, litigation or arbitration costs etc. SOEs should therefore devise means of managing such costs in an effective manner.

Behavioural practices affect procurement performance. When the behaviour of those involved in the procurement activities is unethical then procurement will be affected. Unethical behaviour affects effective execution of the procurement contracts. Trust is critical in procurement. When there is no trust either party in the contract either party will not release relevant information to aid in effective execution of contracts. Also the parties will be suspicious of each other if there is no trust between them. Opportunistic behaviour affects procurement performance, acts such as flattery, cynicism and deceit will manifest if there is opportunism among the parties. It can be concluded that absence of trust and evidence of opportunism will increase transaction costs and negatively affect procurement performance.

There is a positive and significant relationship between contracting, transaction costs, behavioural practices and procurement performance. If the contracting process is not well planned and executed, and if there is evidence of mal behavioural practices like bribery and deceit, then the transaction costs will increase which later impacts on the procurement performance of the SOEs. Contracting is a key predictor of procurement performance this is because every activity to be performed in the agreement must have been determined at this stage. So failure to have clear contracting objectives is likely to affect procurement performance. It can further be said that transaction costs and bad behavioural practices will also affect procurement.

5.4 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.

SOEs should also set clear procedures for those who are involved in the contracting process. If there is no set criteria/procedure, then the contracting team may set its own procedures that it will follow. An established criterion guides the contacting team on what to do. This criterion should not be complex because it would cause confusion in the contracting team.

Since SOEs are the private arm of government, the government should allow the SOEs to develop their own procurement procedures that will enable them to effectively compete with other private businesses. SOEs are in business not only to provide services to the public but also to make profit. Therefore there is need for the SOEs to align their procurement activities to those of the private sector. If this is done then SOEs will register better performance in terms of efficiency and effectiveness. This is being done in other countries and can be done here in Uganda.

The behaviour of those involved in the contracting process must be “checked”. This can be through reference checks and selecting people with a proven record of integrity. Trust should be emphasized by both the SOEs and their respective providers in order to build a positive long-term relationship and opportunistic behaviour by both the SOE and the providers should be avoided. Acts like deceit, cynicism and flattery must also be avoided at all costs.

Procurement performance measures should be developed by the SOEs. Performance measures help SOEs to align their procurement activities to set measures. The set performance measures should aim at achieving efficiency and effectiveness in terms reduced costs, acquisition of better products and value for money among others.

If the above are observed, transaction costs will significantly reduce which later will lead to better performance in terms of efficiency and effectiveness of the processes of the SOES. It also important that SOES exploit other forms of searching for providers for example they can use pre-qualified suppliers and developing a computerised system of assessing and appraising the providers. The costs of enforcing contracts will consequently be reduced if the above recommendations are put in practice.

5.5 Areas of further research

Due to the scope and the limitations highlighted in chapter three, 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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APPENDIX 1: QUESTIONNAIRE

MAKERERE UNIVERSITY BUSINESS SCHOOL

QUESTIONNAIRE

Dear respondent, your organization has been selected to participate in a study on titled “CONTRACTING, TRANSACTION COSTS, BEHAVIOURAL PRACTICES AND PROCUREMENT PERFORMANCE OF PUBLIC ENTITIES: THE CASE OF STATE OWNED ENTERPRISES IN UGANDA”.

Makerere University Business School (MUBS) has sponsored this study and the research is intended for only Academic purposes. The information provided will be treated as highly CONFIDENTIAL. The researcher guarantees the destruction of the acquired information by shredding or burning once the data has been analyzed and inferences drawn. I thank you for your co-operation in advance.

BACK GROUND INFORMATION (Please tick as appropriate)

a) Highest Academic qualification of the respondent.

High school	Diploma	Degree	Masters	Professional	Others (specify)

b) Age of respondent

Below 25 years	25-35 years	36-45 years	46-55years	Above 55 years

c) Sex of the respondent

Male	Female

d) Range of sales revenue per year

Below Ugsh.12,000,000	13,000,000 - 360,000,000	More than 360,000,000

e) Number of employees

Below 4 Employees	5 – 50 Employees	More than 50 Employees

The table below shows the alternative responses and the number assigned in each response. Please evaluate the statement by ticking in the box with the number that best suits you.

Expropriation

I strongly disagree (SD)	I disagree (D)	I am not sure (NS)	I agree (A)	I strongly agree (SA)
1	2	3	4	5

CONTRACTING

Contracting involves writing formal arrangements 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). Specifically contract objectives, procedures to manage the contract and the ability of those contracts must be addressed. This section of the question aims at gathering information related to these aspects.

Contract objectives

		SD	D	NS	A	SA
1	We set contract objectives before we start the contracting process					
2	I'm involved in setting contract objectives					
3	There is a policy in place that guides formulation contract objectives					
4	Key deliverables are clearly considered when drafting objectives					
5	The contract objectives are realistic to the providers					

Ability to contract

		SD	D	NS	A	SA
1	The people chosen to contract on behalf of the company are well trained					
2	The people who contract on behalf of the company are trained					
3	Those chosen to contract are chosen on merit					
4	We involve legal experts in the contracting process					
5	For every contract we constitute a different negotiation team					

Procedures

		SD	D	NS	A	SA
1	There are well established procedures that govern our contracts					
2	The contract procedures are well observed during the contracting process					
3	The procedures are documented					
4	We have independent parties to turn to in case of disagreement					
5	Terms and conditions are well defined					

TRANSACTION COSTS *(Transaction costs are broadly interpreted to include costs associated with market exchange, including costs of searching for information/options, negotiating contracts and enforcing agreements) (Singh, 2008).*

Search and information costs

		SD	D	NS	A	SA
1	We incur high costs in gathering information about our providers					
2	Information gathered about the providers is relevant					
3	The information provided is reliable					
4	The information is timely					
5	We hire independent personnel to gather information about providers					

Contracting costs

		SD	D	NS	A	SA
1	We spend more time while contracting with providers					
2	The costs of managing the contracting process are high					
3	We hire professional personnel to negotiate on behalf of the company					
4	Those who participate in the contracting process are paid allowances					
5	Sometimes we fail to reach agreement with providers					

Enforcement costs (*These relate to costs incurred in trying to make the providers to perform their contracts*)

		SD	D	NS	A	SA
1	We incur high costs in sending reminders to the providers to perform contracts					
2	We involve courts of law to try to compel providers to perform the contracts					
3	The providers perform their duties in time					
4	There is a team put in place to monitor the performance of contracts					
5	The contract monitoring team is paid allowances					

BEHAVIORAL PRACTICES (*This relates to either the bad or good practices that either party in contract may be involved in*)

Opportunistic behaviour - *opportunistic behaviour usually entails one using certain “loopholes” within a contract in such a way that does not actually breach the terms of the contract, but to take advantage of terms in the contract (Masten, 1996; Irene, 2007).*

		SD	D	NS	A	SA
1	We exploit loopholes in contracts to our benefit					
2	If we are in a better position, we always renegotiate the contract terms					
3	The providers use technical terms during the contracting process					
4	We and our providers do not stick to the set standards of the contract					
5	We manipulate information to our benefit					

Trust (*According to Morgan and Hunt (1994), trust is existent when one party has confidence in an exchange partner’s reliability and integrity*)

		SD	D	NS	A	SA
1	We are accountable to the relevant stakeholders					
2	We are honest and demonstrate high a level of integrity when contracting					
3	Our organization expects that the future relationship with providers will be good					
4	Our organization and providers are truly sincere in their promises					
5	Our organization and providers act kind to each other					

PROCUREMENT PERFORMANCE OF SOEs (*Purchasing performance is the qualitative and quantitative assessment of the degree to which the purchasing function and those that are involved in procurement activities achieve the general and specific set objectives of procurement*)

Efficiency (*Efficiency measures how successfully the inputs have been transformed into outputs*).

		SD	D	NS	A	SA
1	Our suppliers supply items within the agreed prices mechanisms					
2	Supplier delivery schedules are reliable					
3	We are contented with products and service level of our suppliers					
4	The quality of items supplied is that agreed upon in the contract					
5	The products are delivered in the agreed time					

Effectiveness (*Effectiveness measures how successfully the system achieves its desired output*)

		SD	D	NS	A	SA
1	We have good information systems in place to keep track of our performance					
2	We have good policies and procedures that govern procurement activities					
3	There is a good management framework					
4	We are motivated and trained to perform our tasks					
5	Those who perform procurement activities are qualified					

Do you think that the contracting process is well managed in the organization?

Please tick as appropriate

Thank you for your time

YES

NO
