

## Chapter 9

# Acquiring Goods and Services: Public Procurement

---

*Where there is honey, there are bees.*  
– Nepali proverb

Besides financial resources, discussed in the two previous chapters, and labor, discussed in the next three, government needs a variety of equipment and materials, as well as consultants and other services, to perform its activities. The acquisition of these goods and services is normally referred to as procurement.

### NATURE AND SCOPE OF PUBLIC PROCUREMENT<sup>1</sup>

*Government procurement is the acquisition of goods, services, and public works in a timely manner that results in best value to the government and the people.* The performance criterion for evaluating procurement activities is economy, i.e., acquisition at the lowest price without sacrificing quality and timely delivery. Public procurement gives substance to the tasks of government. A major proportion of public expenditure at every level of government is incurred through the procurement of goods and services and construction activity. Typically, procurement accounts for 20 percent of central government expenditure, and up to 50 percent of public expenditure in developing countries (including construction contracts). The range of government contracting and purchasing is vast, from weapons systems and large industrial plants to raw materials, paper and milk, custodial services, etc. Poor procurement management has an impact beyond project implementation and the functioning of the public agency concerned. It also delays or dilutes the intended program benefits to society, constrains private sector performance, and is commonly perceived to be associated with bribes for the award of contracts. Consequently, procurement and public works engage the attention of a significant number of civil servants and

political leaders throughout the year, and the ex-post scrutiny of auditors and legislators.

Historically, the role of the public service was to procure goods and services for the king. Samuel Pepys was appointed in the 17<sup>th</sup> century by the British monarch to look into the reasons why the quality of ships and supplies for the British Navy was so unreliable, and prices so high (Box 9.1).

**Box 9.1**  
**Procurement Function in 17<sup>th</sup> Century England**

*... But I see it is impossible for the King to have things done as cheap as other men.*  
*- Samuel Pepys, 1662*

The diary of Samuel Pepys gives a striking description of the procurement function in 17<sup>th</sup> century England and the uncontrolled scope for self-enrichment by government officials in those times. Pepys managed to clean up the defense procurement process for the King by delving into administration as a professional, learning about what was required by the navy and why, negotiating fiercely on quality and price, and following up to see that contracts were properly fulfilled. He was troubled by the ease with which he (like many others before him in his position) could receive “tokens” of appreciation from successful contractors. On occasion, Pepys himself yielded to the temptation.

The diary also speaks about the required reporting on procurement to the increasingly assertive Parliament in its watchdog role, and the type of meticulous documentation that was needed to justify the conduct of the executive.

*Source: Richard Latham. 1978. The Illustrated Pepys. London: Bell and Lyman.*

Public procurement includes procurement by government and by statutory boards and nonministerial bodies as well. Often, the purchase of goods and services by nongovernment public entities is far greater than that undertaken by ministries and reflected in the budget. These entities follow regulations similar to those of ministries, and are subject to government audit in their use of funds. Procurement in the broad sense also covers issues of procurement strategy, storage, distribution, contract monitoring, and supplier management, and is thus synonymous with total supply chain management. The purchasing phase of the procurement cycle involves selecting suppliers, negotiating, and contracting for goods and services.

Contracting for public works and construction is usually treated separately from purchase of goods and services for a number of reasons.<sup>2</sup> Unlike goods and services that go into the consumption stream or serve as intermediate inputs, public works (roads, bridges, buildings, etc.) represent tangible final outputs. The standards and specifications for construction tenders and contracts are also different, and the contracting process lends itself to the unbundling of the project, and thus to separate contracts for each component (e.g., design, technical services, and actual construction). The process accordingly stretches over a much longer period than the procurement of goods and services, and calls for closer and continuous supervision.

As a part of the broad procurement process, contracting out in some countries has become more prominent. Contracting out the delivery of services, such as transport and garbage collection, has been common for years, but has increased in use since the late 1980s, at both national and subnational levels of government. (Contracting out is discussed in Chapter 13 on “exit” mechanisms.)

Procurement can be centralized or decentralized in different degrees. Central purchasing agencies continue to function in many countries; often prompted by the fear of waste and abuse of power by field offices. Genuine decentralization, as discussed in Chapter 5, would imply the autonomy and flexibility of subnational units to procure goods and services either under centrally financed programs or as an agency function carried out on behalf of the central government. Standards and criteria, however, should still be set at the central government level. Similarly, central procurement operations are generally to be carried out by the ministry or agency concerned, but under policy, guidelines, and oversight by a central procurement entity.

It is useful to distinguish between international and local procurement, and between large or complex purchases and routine procurement of daily supplies. These distinctions have practical implications for the manner of organizing the procurement function, the form of the bidding required, and the scope for decentralization and delegation.

There are essential differences between the procurement process in the government and that in a private firm. A private firm places less emphasis on formal competitive bidding, documented procedures, and constraining conflicts of interest than governments do. Private managers have built-in

incentives to purchase goods that provide high value for their price, and to hire contractors who will accomplish high-quality jobs at competitive prices. The dimensions of accountability are related to results, not process, because in the private sector the results are more easily quantifiable, by reference to their impact on overall company profit.

In contrast, the public manager must follow prescribed competitive procedures, and the rules give a major weight to fairness and equity. Also, public procurement is subject to oversight by the legislature and audit (in addition to internal accountability mechanisms). Mistakes or malfeasance in public procurement can have vast political repercussions, owing to the focus that the media and the public place on the subject.

Also, private firms and nonprofit agencies prefer stable relationships with suppliers and long-term contracts, for certainty and easier business planning, but several factors (including the fear of collusion with contractors and financial rules) prevent public agencies from developing such long-term relationships. Finally, public procurement is often used as a tool for public policy goals (e.g., fostering the growth of local industry, or benefiting groups of poor women or disadvantaged groups).

## OBJECTIVES OF PUBLIC PROCUREMENT

### Economy

As noted, the criterion of “economy” (which is common to both public and private procurement) involves acquiring goods and services of defined specifications on a timely basis and at the lowest cost. Economy is a useful criterion for administrative purposes, as it is linked to the performance of the procurement function. However, from an economic point of view, it is subsumed under the broader criterion of *efficiency*, i.e., lowest *unit* cost of production: if the goods and services to be procured are not the appropriate ones for efficient production, procuring them at least cost is no advantage.

Wasteful procurement can arise from duplication and overlap in government operations, from a lack of predictability in the flow of funds to public agencies (which leads the agencies to use the funds available when they happen to be available, entailing higher cost of storage), and from a lack of incentives for employees to make the best use of supplies. Sound procurement, therefore, depends also on a variety of organizational

and incentive factors within government well beyond the control of those in charge of the procurement function itself.

### **Import Substitution**

The government procurement strategy may deliberately encourage the growth of local industry by giving preferences to local suppliers or restricting purchases from foreign firms. Many governments seek to ensure some advantage for domestic industry in competing for the business of public organizations. These preferential practices must be kept carefully distinct from regulations intended to offset market imperfections that prevent domestic suppliers in developing countries from competing on a fair and equal basis with international suppliers. Unlike those regulations, preferential procurement practices may well be inadvisable from both an efficiency and a development viewpoint.

Some preference to domestic firms in international competitive bidding has traditionally been recognized by donor agencies, e.g., the World Bank. The European Union (EU) allows countries applying for membership (from central and eastern Europe) to keep domestic preference provisions, but only for a limited time. The rules of the World Trade Organization (WTO) call for uniform treatment of domestic and foreign suppliers in procurement. However, WTO provides for special and differential treatment of developing countries to safeguard their balance-of-payments position, promote the development and establishment of domestic industries, and support industrial units that are substantially dependent on government procurement.

### **Fostering Competition**

Competition in procurement is defined as equality of opportunity for qualified suppliers to compete for public contracts. Competition and impartiality are needed not only to ensure a beneficial outcome in price and quality, but also to promote public accountability in the process. Increasing competition in public procurement is a goal of most governments, and is supported by international organizations as well. In the United States (US), for example, the Competition in Contracting Act of 1984 aims to increase competitive efforts within departments and to narrow the justification for sole-source (direct selection) contracting. Countries like the United Kingdom (UK) require their local governments to resort to compulsory competitive tendering for all purchases and services. Many

countries require their national and subnational governments to increase their use of open bidding, improve the handling of competitive bids, and streamline administration and payment procedures, to attract more firms to compete for government business. Because the number of qualified suppliers is directly related to the degree of competition, many developing countries and most aid agencies support the provision of information and technical assistance to bidders to better understand the rules of procurement and become qualified to compete.

In developing countries, competition is often restricted by market imperfections such as barriers to entry and information gaps for small and less experienced suppliers. These barriers are sometimes put up by the administrative process itself, such as the tendency to float large bids to have a single centralized decision, or the expensive or formalistic overspecification of requirements that small and less experienced firms find very costly to fulfill. In some areas, e.g., emerging technology, specialized services, or complex equipment (as in military procurement), aid-dependent developing countries may be obliged to deal with only one or two bidders because the government is often restricted to choosing only from the donor country's suppliers. The long-term strategy is to encourage the development of the domestic contracting industry through various means, to lower the barriers to entry for small business and voluntary agencies, and to untie aid as much as possible through better cooperation among donors and stronger leadership by the multilateral financial institutions in this respect.

### **The Governance Dimension**

Predictability, a key principle of good governance, presupposes consistent principles and regulations for procurement, qualification of contractors, award of bids, and contract management. Information and documentation on these rules should be widely available, and the rules should be enforced fairly and consistently. Predictability in procurement also requires a well-understood system for registering and resolving complaints speedily, a well-functioning system for dispute settlement, and checks on the arbitrary behavior of procurement managers and on the inconsistent exercise of discretionary power in contract award, enforcement, and management.

Accountability and transparency are vital to procurement management as well. Lack of oversight mechanisms to ensure accountability undermines the capacity of governments to secure the confidence of

contractors in the public procurement process and the trust of citizens in the proper use of that public funds. Trust and confidence can be especially eroded by secrecy in procurement transactions, especially at the local levels (although a degree of confidentiality is essential to protect business privacy and the legitimate interests of individual bidders). Transparency reduces uncertainty and inhibits corruption in procurement by assuring equality of access to information for all bidders before, during, and after the bidding process.

### **Protecting the Interest of Citizens**

Whether or not the responsibility for service policy is separated from that for service delivery (Chapter 6), governments have a responsibility of assuring that the services reach the citizens, reaffirmed in judicial decisions in many countries. This responsibility implies setting up recourse mechanisms in case of contractor failure, carefully monitoring contract execution by private suppliers, giving credible information to citizens about the actual providers of service, and opening avenues of complaint.

### **Environmental Protection**

The United Nations (UN) advocates making the preservation of environmental quality and the reduction of waste a part of procurement guidelines.<sup>3</sup> Governments could review the purchasing policies of their agencies and departments to improve, where possible, the environmental impact of government procurement policies, including those related to packaging and recycling. In a policy of environmentally conscious procurement, apart from other requirements, the choice of products and production methods is based on criteria of environmental protection and conservation of nonrenewable natural resources; and no specifications discriminate against the use of recycled materials.

## **LEGAL AND REGULATORY FRAMEWORK FOR PROCUREMENT**

### **Public Procurement and the Law<sup>4</sup>**

The legal framework for public procurement includes international obligations, specific domestic legislation on procurement, contract and commercial law in general, and patent and copyright law, labor law, and laws governing lease- and hire-purchase agreements, arbitration, and

conciliation. Some countries (e.g., South Africa) have constitutional provisions as well as enabling laws for procurement (Box 9.2). Others (e.g., the Republic of Korea and US) have passed regulations and legislation. In the US, procurement-related laws include the Competition for Contracting Act of 1984 and the Federal Acquisition Streamlining Act of 1994. The Republic of Korea in 1990 passed the Act Relating to Contracts to which the State is a Party (ARCSP) and the regulations to enforce it.

### **Box 9.2**

#### **South African Constitution and Procurement**

South Africa is among the developing countries whose constitution contains a special provision on government procurement. Section 187 of its 1994 Constitution provides the following.

- The procurement of goods and services for any level of government shall be regulated by an act of Parliament and provincial laws, which shall provide for the appointment of independent and impartial tender boards to deal with such procurement.
- The tendering system shall be fair, public, and competitive, and the tender boards shall have to justify their decisions at the request of interested parties.
- No organ of state or any member of state or any other person shall improperly interfere with the decisions and operations of the tender boards.
- All decisions of the tender boards shall be recorded.

#### **Public Procurement Reform in South Africa**

Procurement reform in South Africa is part of the extremely difficult challenge of balancing short-term efficiency with the imperative of gradually redressing the racial discrimination of the apartheid regime. South Africa gained nine provinces after the 1994 election, but the Government was hampered by a procurement system that was fragmented, hard to use, and biased toward large, established businesses. The fragmented and onerous procedure often caused delays in delivering services and prevented the government from taking advantage of its size to negotiate in procurement contracts. All contracts had to be approved by 10 Tender Boards (one national and nine provincial), and there were separate boards or committees for parastatal and local authorities. Each of these boards was autonomous, with its own procedures, requirements, and policy interpretations.

*continued on next page*

*Box 9.2 (cont'd.)*

The procurement system clearly did not meet the requirements of the Constitution, which stated that procurement must be “fair, equitable, transparent, competitive and cost-effective.” Public sector procurement reform in South Africa is therefore aimed at three main objectives: good governance, uniformity, and achieving socioeconomic goals. An important aspect of the planned socioeconomic transformation, balanced with the objective of efficiency, is encouraging broader participation and overcoming discrimination. The Preferential Procurement Policy Framework Act 2000 is a key piece of legislation in this delicate process. The act specifies a two-tier preference system. For contracts below a certain threshold value, 80 points are rewarded for price and 20 points are allocated to empowerment and development objectives. For projects above the threshold, the split is 90/10. The aim is to enable smaller contractors to bid for lower-value contracts, and to allow some redress for past discrimination. The act will apply to all organs of government (not including the public enterprises), although the Minister of Finance may approve exemptions. A penalty clause is included to discourage established firms from establishing front companies to qualify for preference.

This South African legislation is well worth considering by other multi-ethnic countries that must reconcile short-term efficiency with long-term sustainability and equity.

*Source: Laura Walker. Personal communication. 2000.*

## The Regulatory Framework

Most countries that rely on *general contract law* regulate public procurement by internal rules that prescribe the formal process of bidding, the evaluation of bids, the award and conclusion of contracts, and contract management (Box 9.3). The rules also mandate procedures for dealing with possible court challenges from unsuccessful bidders, and procedures for contract interpretation, breach of contract, and dispute resolution and arbitration. The intention is to provide a self-contained regime for contract award and management, which would avoid recourse to external arbitrators.

The procurement regulations and audit rules place great reliance on competition and objective decision making (except in specified emergencies such as natural disasters). This approach often results in extensive regulatory control and oversight by external agencies, and heavy bureaucratic review and approval processes. Many government entities feel that the procurement

### Box 9.3 Procurement Guidelines in the United Kingdom

In the United Kingdom, the Procurement Practice and Development team is the central unit in the Treasury that promotes best practices and the development of procurement strategies by departments. The Government has stipulated the following key points for its senior management: value for money; compliance with national and international legal obligations; cost-effective fulfillment of users' needs; appropriate level of competition; and honest and impartial relationships with suppliers. The procurement process would ensure fairness, efficiency, courtesy, and firm dealings; high professional standards; wide and easy access to information on the procurement process and documentation; prompt notification of the outcome of the bidding; efficiency and integrity in contract management; and prompt response to suggestions and complaints.

In selecting bidders, undue emphasis should not be placed on size, and the standards of financial and technical capacity should be proportionate to the contract in question. The criteria for the award should not consist of price alone, but should also consider other factors like whole-life cost, quality, and delivery. Whole-life cost is relevant in complex procurements, including large supply and service contracts and construction projects, and in offsetting higher expenditure for better quality against the lower maintenance costs over the asset's life.

New Zealand has published *Government Purchasing: A Guide for Suppliers* to help suppliers understand and operate in the government purchasing environment. It is intended to improve communication between public sector buyers and industry to their mutual benefit. Canada provides an integrated electronic public tendering service, which supports open, cost-effective procurement for all levels of government, and all sizes of suppliers in the private sector.

*Source: UK Government and World Trade Organization web sites.*

process has become an end in itself, stressing compliance with rules to the neglect of economy or efficiency. In 1993, the US had 889 laws that controlled every aspect of defense procurement alone, making a product 50 percent by estimate more costly simply because it was being purchased by the government. Federal regulations filled 1,600 pages, supplemented by 2,900 pages of agency-specific regulations, supplemented in turn by instructions and case law (US Government 1993). Some of these additional regulations are important in public procurement because of its special nature

and risks. In many countries, however, procurement rules would be substantially simplified without compromising the integrity of the process.

After the award of contracts, additional regulations to deal with breach of contract and unsatisfactory contractor performance can be reduced in the first instance through clear and complete specifications, well-defined performance standards, and the inclusion of incentives and penalties in the contract. However, these measures inevitably add costs and delays to the initial phases of contract execution. Formal legal remedies, such as financial penalties or exclusion from future contracts, are costly and dilatory in countries with inadequate judicial systems.

Many countries are consequently moving to streamline and consolidate existing laws and regulations, or writing simpler laws and regulations to govern procurement transactions. In the US, as recommended by the National Performance Review, the Federal Acquisition Streamlining Act of 1994 repealed or modified 225 provisions, and raised the thresholds above which the agencies needed to follow the regulations, thus exempting 95 percent of transactions.

### **Model Codes**

The stress in recent years has also been on a uniform procurement code to set the basic framework for procurement, supplemented by the more detailed rules by implementing ministries. For example, in Australia, the procurement framework is contained in the 93-page *Commonwealth Procurement Guidelines* issued in December 1997. In the UK, the procurement function is exercised under Treasury guidance (Box 9.4). At the subnational level one of the earliest efforts at a uniform procurement code was the *Model Procurement Code for State and Local Governments* in the US. This was the most comprehensive and consistent attempt to apply the elements of good practice, and was meant to be adapted to particular state and local circumstances. The EU insists on enforcing a model procurement code (Box 9.4) as a condition for membership of countries in the Union. The People's Republic of China, for its part, has drafted procurement legislation with Asian Development Bank support.

### Box 9.4 Procurement Regulations in Europe

Countries seeking European Union (EU) membership are required to establish and maintain procurement systems that meet standards of transparency and of open and fair competition. Central and eastern European countries have been working to establish modern public procurement systems from the start of their transition to a market economy. Creating such systems is part of the process of forging an efficient, competitive market economy and is necessary for these countries' full integration into the international trading community.

To build and implement the system, significant changes have had to be made from the days of the command economy, when procurement was part of the central planning system. In particular, central and eastern European countries are designing a legal and administrative framework that facilitates the integration of the myriad procurement entities throughout the public sector into a functional and coherent network with high professional standards, and that is consistent with international obligations. Such a framework would define the financial and legal responsibilities of all participants in the procurement process, including suppliers and procurement entities in central and local government.

Slovakia and Latvia have already passed a national procurement law consistent with international standards. Poland has set up a central organization to draft and disseminate procurement regulations and rules for decentralized operation. The Organisation for Economic Co-operation and Development and the International Labour Organisation have collaborated in preparing a public procurement manual for central and eastern Europe.

*Source: OECD (1999a).*

The most widely used model public procurement law is the one adopted by the UN Commission on International Trade Law (UNCITRAL) in 1994,<sup>5</sup> consolidating previous model laws. A detailed guide was later issued. The model law was intended to be a model for developing and transitional economies in modernizing their procurement regulations or in establishing such regulations. It is expected to address the inefficiencies and the potential for abuse in the laws of many countries, and to make these laws more compatible with international trade practices. The law has formed the basis for national procurement legislation in many developing countries, with support from international donor agencies. Annex V lists the provisions of the model law. The model law does not supersede

international obligations or the applicable national laws for contract, criminal, and judicial procedures. Although as a framework law the UNCITRAL model law does not itself set forth all the necessary regulations, it mandates open tendering as the method of procurement that is generally most effective in promoting competition, economy, and efficiency in procurement. For circumstances in which tendering is not feasible, the model law suggests alternative methods of procurement.

### **Manuals and Procedures**

Public procurement manuals typically comprise (i) a policy manual, which can include purchasing rules and administrative procedures; (ii) an operations manual of internal practices and procedures; and (iii) a vendor manual, which often takes the form of a booklet entitled *Doing Business with the Government*. Matters of policy (e.g., giving preference to domestic suppliers in international competitive bidding) are generally issued as binding instructions for all ministries and departments, but different countries allow different degrees of departmental discretion in devising procurement regulations. In Singapore, for example, all government entities must follow the administrative procurement procedures laid down by the Ministry of Finance in an instruction manual. On the other hand, New Zealand, the United Kingdom, and other developed countries issue central guidelines but allow individual departments to issue regulations specific to their needs within those guidelines. There are advantages to issuing a single set of procurement guidelines for common guidance, while allowing individual agencies to supplement and vary these according to their needs and those of their clients.

## **ORGANIZATIONAL ISSUES IN PROCUREMENT<sup>6</sup>**

### **Systematic Neglect**

A fundamental problem in public procurement is disinterest and neglect by operational managers, who tend to leave procurement to the “specialists.” There are several reasons for this neglect. Managers are typically more interested in policy, and find the tasks of purchasing dull by comparison. Also, they rarely have enough time to understand the intricacies of product quality, pricing structures, and technical specifications. Moreover, in a climate where the integrity of government operations is coming under increasing scrutiny, keeping some distance from purchasing operations insulates a manager to some degree from potential charges of corruption.

Finally, management distance from procurement decisions is often encouraged by the procurement staff themselves—usually because they view management involvement as interference with little value added, and occasionally for less honorable reasons. A time-honored defensive response to a sudden interest by managers in procurement is to provide them with a large volume of indigestible technical material.

The general disinterest of public managers in procurement matters finds its expression in the absence of the subject from the curriculum of public administration schools. In contrast, business and management schools normally offer one or more courses in purchasing and in contract monitoring.

This is not a healthy state of affairs. In the first place, as noted earlier, the entire field of public administration has its historical origin in the ruler's concern with a malfunctioning procurement system. Second, as stressed throughout this book, the effectiveness of public management depends largely on achieving a good balance between control and flexibility; between protecting systemic equity and providing individual incentives for performance; and between short-term results and long-term continuity. Civil servants have an understandable aversion to risk because of the lack of corresponding rewards and the special external scrutiny to which public service is exposed. Only a climate of trust and higher-level support can prevent such risk aversion from turning into operational paralysis. In the area of procurement, this calls for more involvement by managers and consequently greater support for and control of the actions of the procurement specialists.

Therefore, senior public managers have a central responsibility to become much more involved in the procurement function, especially for large contracts, than is currently the case in most governments. The political leadership can persuade managers to accept this responsibility by making its exercise part of their explicit performance expectations. Of course, senior managers cannot and should not become procurement specialists, but they must be aware of the process and its risks, and there are a variety of ways through which senior public managers can assure themselves of obtaining competent contestable advice. Such an evolution in the public sector would find a parallel in the earlier evolution in the private sector—from product orientation to client orientation—with the result that in the 1970s the separate purchasing activities were merged and entrusted more and more to top levels of management.

## Organizational Arrangements

A central question is whether responsibility for procurement should rest with the agency that requires the service or with a central purchasing agency. The main advantage of centralization is that the central procurement officers know the law, policies, and procedures, and have the institutional memory to gain the maximum benefit for government. Decentralization, on the other hand, speeds up the process and places greater emphasis on the services and goods to be delivered. The conflict between central procurement offices and line agencies is typical, and is part and parcel of the general issue of central versus decentralized authority. This conflict draws attention to a number of broader issues that concern not only the executive branch of government but also the legislature and oversight entities such as the audit and anticorruption agencies.

In most countries, the ministries and other spending agencies undertake their own procurement and award contracts for civil works and supplies, subject to procurement guidelines and goals prescribed by a central unit (normally in the ministry of finance). The central unit fixes the threshold for purchases or contracts within the discretion of the head of each spending agency, as well as the procurement threshold for more rigorous tendering under central bidding procedures. In countries where executing agencies are set up for operational functions (Chapter 6), the framework agreement provides for financial autonomy in procurement, subject to certain binding features of national procurement policy.

The following illustrates the variety of practices in different countries. In the UK, a Procurement Policy Team, a joint unit of the Treasury and the Department of Technology and Industry, advises the ministers on procurement policy. In Slovakia, procurement is the responsibility of the Ministry of Construction and Public Works. In Singapore, the Government has decentralized the bulk of its procurement to the ministries, departments, and statutory boards, which make their own arrangements. However, several centralized procurement functions are performed by the Budget Division and the Procurement Policies Unit in the Ministry of Finance, the Construction Industry Development Board, and the Health Ministry (for pharmaceutical products). Australia's federal structure combines central agencies and decentralized departments, as well as central procurement entities with significant support functions (Box 9.5). It is a good example of strategic coherence in procurement. Some countries (e.g., Australia, Canada, and a number of Asian and European countries) have set up specialized

purchase agencies to provide common services and materials for several departments.

It is useful to build a consultation mechanism into the procurement process, not only to give the spending agencies the benefit of expert advice but also to check imprudence in procurement. As an outgrowth of such consultation, purchases by spending agencies may be exempt from the bidding process if they are made from an approved-rate contractor preselected by the central procurement agency. Alternatively, agencies may be required to consult specialized entities or experts when acquiring computer systems and scientific services. Interagency committees may be set up for procuring supplies involving several sectors or agencies. Various other coordination and flexibility mechanisms may be established for effective consultation between the procurement entity and the spending agencies.

**Box 9.5**  
**Procurement Organization in Australia**

In the commonwealth government, procurement management is substantially decentralized, with each agency responsible for its own procurement within a centrally prescribed framework of procurement policy and advisory guidance on best practices and techniques. The framework also covers government business enterprises. The Department of Administrative Services coordinates purchasing policy and civil purchasing.

Among the entities with procurement responsibilities is Purchasing Australia, which administers the purchasing and disposal framework of the commonwealth government.

Purchasing Australia also supports the general supplier community through the following mechanisms:

- a supplier development program, which assists small to medium enterprises in gaining access to the commonwealth marketplace by linking suppliers with buyers, providing information, and facilitating skills development; and
- The Government Electronic Marketplace Service, which provides information through the Internet about the purchasing policies of the Australian Government and special purchasing opportunities in the Government.

*continued on next page*

*Box 9.5 (cont'd.)*

The Office of Government Information and Advertising provides advice and assistance in advertising, market research, public relations, and related matters. It manages the centralized arrangements for commonwealth advertising; disposal of surplus assets; contracting assistance; the facilitation of electronic purchasing; buyer training; and publications and other advisory material on procurement matters.

The Public Works Policy Group (PWPG) assists agencies in applying public works policies. The PWPG promotes the implementation by agencies of best practices in the procurement of construction and related services, and facilitates the ongoing development of best practice strategies.

The National Procurement Board monitors, reviews, and reports on the efficiency and effectiveness of the Government's buying framework and plays a key role in ensuring that all agencies carry out the Government's policies.

---

*Source: World Trade Organization web site: <http://www.wto.org>*

## WHAT TO DELEGATE AND WHEN

### General Issues

As already emphasized in Chapters 5 and 8, the issues of delegation and decentralization pivot around the right balance between efficiency and risk. Typically, line ministries and spending agencies always push for delegating the procurement function, on the grounds that they are the best judge of their own requirements, and can meet them faster and at less cost than going through a central procurement agency. This would be almost always true, except for the problem of the senior managers' disinterest and neglect of the procurement process, discussed earlier. The disinterest of senior managers means that once procurement is delegated to the line agency, it falls under general administration and is no longer given the prudential attention it deserves. The risks correspondingly increase with the delegation of procurement. However, the solution is not to keep all procurement centralized because of the risks. On the contrary, the previous section has pointed to the advantages of decentralized purchasing and contract decisions, subject to central rules, criteria, and oversight. The risks, however, must be addressed—both by encouraging sufficient attention to procurement by senior managers in the line agency, and by retaining robust central oversight.

The key questions to be considered when deciding to decentralize procurement are

- whether it is more effective to develop strict purchasing procedures and contractual safeguards at the center, or to give public managers more discretion to develop procedures and safeguards tailored to the particular goods and services they need;
- how to delegate procurement to the line agencies, while installing appropriate safeguards to prevent abuses;
- the role of the central procurement agency in a context of delegated procurement responsibilities; and
- the degree of corruption and the inefficiency risks of delegation at different stages in the procurement cycle.

The degree of risk varies in different sectors, countries, agencies, and transactions. To achieve a good balance between efficiency and risk one should therefore unbundle the procurement issue. The following considerations may be useful in this context.

Generally, three variables determine the degree of risk:

- specificity;
- market structure; and
- size and complexity of the transaction.

Specificity is inversely related to risk: the more specific the product or contract, the fewer the opportunities for manipulating the procurement process. However, artificial specifications may be included in the standards to favor a particular supplier. Also, other things being equal, greater specificity also entails a smaller market. The market structure in a sector is itself important, with a more restricted and less competitive market associated with greater risk. Next, a large transaction is normally also technically more complex, thus offering greater openings for manipulation and making oversight more difficult. Note also that in the area of procurement the riskiest level of management is middle management, either in terms of inefficiency (through a narrow insistence on the literal application of every extant rule) or in terms of corruption.

To illustrate, information and communication technology is an especially sensitive area. It normally entails the bulk purchase of expensive equipment; requires a level of buyer expertise that is not normally found in

government; and is frequently supply- or donor-driven or both, irrespective of the real needs of the users in a particular country. In this and similar sectors, some mechanism is needed to obtain independent technical advice, as well as to assure much greater participation from the very beginning of the purchasing process by the final users of the equipment or the software.

The sequence of delegating procurement is as important as the end point. Government may delegate certain phases in the procurement cycle first, keeping close tabs on their functioning and strong central control on the other phases—progressively delegating more and more procurement phases as experience permits and performance warrants. Or, delegation may begin first in the less risky sectors or agencies, and gradually be expanded to other sectors. The main phases of procurement (as explained in the next section) are the setting of standards and criteria, the bidding process and evaluation, contract negotiations, and contract monitoring.

A simple scheme may help categorize the degree of risk (which will of course differ according to the specific circumstances of the country), and hence help in deciding which procurement phase to delegate, and for which sector. In the hypothetical illustration below, where the risk of delegating a specific stage of procurement is measured on a scale of 1 to 10 (10 being highest risk) and the risk potential of sectors is assessed on the three determinants discussed earlier (specificity, market structure, and size and complexity of transactions), procurement can be fully delegated in sector V, and not at all in sector Z, while strong central control should be kept in the monitoring phase for sector W, in the standard-setting phase for sector X, and in both the bid evaluation and negotiations phases for sector Y.

**Risk Matrix for Delegating Procurement Functions**

Sector	Phase of Procurement			
	Criteria/ Standards	Bidding/ Evaluation	Negotiations	Monitoring
V	1	1	2	2
W	3	3	3	9
X	9	2	2	2
Y	2	8	7	1
Z	8	8	8	9

## Local Government Procurement and Intergovernmental Aspects

Procurement is becoming important at the local level, in parallel with decentralization (Chapter 5) and the increasing range of functions performed by local governments in most countries. However, legal restrictions on procurement apply much more at the local level because of conditions attached to grants from the center or because of the mandates by national government in areas such as environment.

Some developed countries (e.g., the UK) have been enforcing compulsory competitive tendering at the local level for years, in the interest of service efficiency and quality. Model procurement codes for state and local governments, developed in countries such as the US, envisage a procurement policy unit reporting to the city manager or the district or county commissioner. The unit has no operational responsibility for procurement, but provides research support, maintains a contractor database, and monitors complaints. This could be a suitable system for cities in developing countries, with limited staff and skills.

As noted earlier, there is substantial agreement on the need to integrate centralized procurement policy with decentralized measurement operations. In developing countries, with their scarce skills at local levels, and the greater scope for imprudent and discretionary expenditure, such delegation has to proceed carefully. The higher levels of government must be cognizant of the risk of corruption and waste in local government procurement, and take steps to build local capacities, along with nonintrusive oversight mechanisms. Of course, in countries where corruption in the central government is pervasive, decentralized procurement is likely to improve matters even without special safeguards or technical assistance.

Once the authority is delegated, the higher government level should have the power to monitor and conduct audits, but should not intervene in the award or administration of any specific contract. To address the problem of limited capacities in local units, the state or provincial government could encourage joint procurement, or the award of contracts covering a number of jurisdictions, as is done in France. Also, the provincial government could have the important function of removing barriers to entry for small contractors in local jurisdictions, organizing training programs for contractors and construction firms, and providing support services. Some countries have set up public sector consultant organizations, staffed by experts, to assist local governments in planning and managing large construction and

irrigation works, and in procuring supplies and services from domestic and foreign sources. Finally, the subnational units could take advantage of central rate contracts with reputable suppliers (as in India).

Although not subject to the same rules and constraints, a good deal of procuring takes place *between* levels of government. This partly takes care of the problem faced by agencies in the audit and oversight of contracts with private parties. In addition, contracting with another state agency may ensure for smaller local units a more uniform level of assured services than contracting with private entities. It is important, however, to avoid making local government a captive consumer of higher government series, and therefore the choice of whether to purchase from higher-level government or from private suppliers must be left entirely to the local government concerned (subject only to the general procurement regulations).

## THE PROCUREMENT PROCESS<sup>7</sup>

### Forms and Stages of Procurement

The forms of procurement practiced in different countries depend mainly on the nature of the goods and services, the size and complexity of the contract, the administrative level, and the market structure. International organization guidelines and bid documents recognize the following forms of procurement, although special procurement procedures may also apply in certain cases:<sup>8</sup>

- competitive bidding (international or national),
- shopping (international or national),
- direct contracting (sometimes called sole-source contracting or direct selection),
- force account, or
- procurement through agents.

Competitive bidding (also known as open tendering) is aimed at providing all eligible bidders with timely and adequate notification of the requirements of the procuring agency and an equal opportunity to bid for the required goods, services, or works. Some countries may give preference to domestic suppliers, as noted earlier. National competitive bidding is normally used when foreign bidders are unlikely to be interested because of the nature of the goods and services or the purchase is of a small size.

Otherwise, international competitive bidding is used. Limited competitive bidding without public advertisement is indicated when the values are small or when there are only a few suppliers. Bids are sought from a limited number of potential suppliers, but broad enough to assure competitive prices. Many local governments float such limited tenders for repetitive purchases, including engineering items and construction materials, on an annual basis and place repeat orders with one or more contractors.

Shopping involves comparing price quotations obtained from at least three suppliers for readily available off-the-shelf goods of small value, such as office equipment, furniture, medicines, books and educational materials, information and communication materials, and similar small supplies. World Bank projects in India, for example, permit shopping procedures for items estimated to cost less than the equivalent of \$30,000 per contract, up to a specified maximum amount.

Force account, or direct government supply and public works, is the provision by the government's own personnel and with its own equipment. It is justified where the works are small or scattered, the amount of work cannot be specified in advance, or in emergencies. In all other cases, procurement by force accounts has tended to be less economical owing to the lack of any competition for the services.

Where the buying agency lacks the necessary organization or skills, it may employ as its agent a specialized procurement spending firm, or a project management firm for construction contracts. Consultants are also often used to draw up documents or to inspect supplies and works.

Direct selection, or sole-source selection, is used for relatively small contracts requiring the specialized skills of a specific individual or firm, and in situations where time is of the essence.

The different forms of procurement are applied to contracts of different value, with the simplest forms being used for lower-value purchases. For example, the World Bank normally requires international competitive bidding for purchases worth more than US\$200,000; permits national competitive bidding for purchases between US\$30,000 and US\$200,000; and permits shopping and direct selection for purchases of less than US\$30,000 (or vehicles costing less than US\$100,000).

In various forms of build-operate-transfer contracts or under turnkey projects for construction, the private company is allowed to procure the goods and services for the project, in accordance with designs and specifications agreed in the contract. Conversely, government agencies in developing countries sometimes handle international bidding and related services for small firms.

## **Competitive Bidding**

### *Stages of the process*

As noted, competitive bidding is prescribed for procurements above a specified value threshold set by the ministry of finance or the central procurement agency. Besides private suppliers, potential bidders include city and county departments (for local services), nonministerial public bodies, and nonprofit organizations.

The complexity of the process depends on the value and nature of the goods or services being procured, but the requirements for competitive bidding are similar in all cases and largely applicable to other forms of procurement as well (Transparency International 1996):

- a clear and fair description of what is to be purchased;
- a publicized opportunity to bid;
- fair criteria for selection and decision making;
- the receipt of bids from responsible suppliers (or contractors);
- comparison of bids and determination of the best or most responsive bid, according to the predetermined and publicized rules for selection; and
- contract award.

Accordingly, the stages in the process of competitive bidding are

- prebid,
- public notice and invitation of bids,
- bid opening and evaluation,
- resolution of complaints, and
- contract award and conclusion.

*Prebid process*

Prebid requirements include standardized bid and tender documents, rules for classifying and registering contractors and suppliers, rules for prequalification, bid evaluation committees (if necessary), and process of deciding on the award of bids. The documents must contain clear specifications, instructions to bidders, and contracting terms. The key requirement of a fair and open process is the easy availability of bid documents in comprehensible language to all willing bidders. A number of countries make the information and documents available in electronic form through convenient outlets or through associations of contractors.<sup>9</sup>

Enough time must be allowed for potential suppliers to bid, for the purchasing agency to evaluate the bids and make the award decision, for the final details of the contract to be negotiated, and for the goods and services to be received or the work to begin. Procurement planning must take these time requirements into account, and the purchasing agency needs to begin the process early enough to ensure that the goods and services will be ready when needed, and avoid having to make high-cost decisions. Recall that timeliness of purchase is one part of the economy criterion.

The bidding process in many developing countries is often impaired by unclear specifications because of a deliberate intent to leave room for discretion or imprecise thinking at the agency level. Contractors and suppliers need clear specifications to respond competitively to the requirements of the purchaser. The specifications should be substantive and permit the acceptance of offers of generic goods that substantially provide the performance specified. Services must be clearly specified in terms of their outcomes or outputs, not only their inputs, but without dictating exactly how the activity is to be performed. Sometimes the specifications and required qualifications are so detailed as to apply to only one or two potential bidders. This is almost invariably done to circumvent the requirements of competitive bidding and in effect operate by direct selection, for good or bad reasons.

Participation of small contractors is often facilitated by dividing the service area into a number of smaller regions or a number of similar packages of equipment and works (a form of unbundling), and encouraging competitive bidding for each area or package. There is less risk of disruption of supply or services in this process of unbundling, but the downside is the likely higher cost of overall procurement and the bias of central governments in favor of large tenders.

*Public notice and invitation to bid*

Timely notification of bidding opportunities is essential in competitive bidding. The notice should be published in local and national newspapers, official gazettes, or electronic bulletins, to suit the nature and size of the project. Information on the invitation to bid should be available in offices of the agency, and the district or county administration for local projects. Bid notices should be publicized in the local language where small contractors and community organizations may be likely to bid. International bids should be published in widely circulated trade journals and newspapers, and through the Internet.<sup>10</sup>

In the case of large, complex works, turnkey contracts, or large consultancies, a two-stage bidding procedure may be used. Unpriced technical proposals are first invited based on technical and performance specifications. Bidders whose proposals are judged to be responsive to the technical criteria are then invited to submit price bids.

*Prequalification* of bidders is usually necessary for large or complex works or in cases where the high cost of preparing bids may discourage competition, such as for custom-designed equipment, industrial plants, specialized services, turnkey contracts, or management contracts. The process ensures that invitations to bid are extended only to those with adequate capability and resources. Prequalification is also used to determine eligibility for preference for domestic contractors in donor-assisted projects. Prequalification should be restricted to the capacity, experience, and resources of the contractors to perform the particular contract satisfactorily, taking into account their past performance in similar contracts. As always, prequalification must be based on transparent and well-publicized guidelines.

Specified criteria are used in deciding which persons or entities are allowed to bid. Sometimes contractors are prequalified for a group or type of contracts over a period of time. In case of projects financed by donor agencies like the Asian Development Bank (ADB) and the World Bank, as well as some governments, prequalification also serves as a check on the integrity record of the contractor, by stipulating that the bidder shall not be under a declaration of ineligibility for corrupt and fraudulent practice. This practice is increasingly required, in parallel with the recent emphasis on fighting corruption in developing countries (Chapter 17).

The guidelines of ADB and the World Bank provide that, as far as possible, the bid package or contract is of such size as to attract competition. Where a number of separate but similar works or items of equipment are to be procured, bids may be invited under alternative contract options from large and small contractors so that the contracts can be evaluated separately or together, or sliced and packaged to secure the most advantageous terms.

The *bidding documents* should furnish all the information necessary for a prospective bidder to bid for the goods, services, or works to be provided. While the detail and complexity may vary with the size and nature of the proposed procurement package, the bidding documents generally comprise the following:

- invitation to bid;
- instructions to bidders, including the criteria for bid evaluation;
- form of bid;
- form of contract;
- general and special conditions of contract;
- specifications (and drawings where relevant);
- list of goods or quantities;
- delivery time or schedule of completion; and
- necessary appendixes for such items as the types of deposits or securities.

The documents should be both in the local language and in an international language (normally English).<sup>11</sup> To assist developing country governments, international organizations have prepared standard bidding documents for different types of procurement. In many cases, the aid-receiving government is required to use the standard bidding documents of the donor organization. This practice may appear to be intrusive, but it saves resources and provides needed protection for both the donor and the recipient, and boosts the confidence of suppliers.

#### *Bid opening and evaluation*

Key to transparency and fairness is to open the bids at a designated time and place in the presence of all bidders or their representatives who wish to attend. Such public bid openings reduce the risk that bids will be leaked to competitors, lost, or manipulated. After the bids are opened, no information on the bid evaluation and award recommendations should be disclosed until after the successful bidder is notified of the award.

Bid evaluation is one of the most difficult steps to carry out correctly and fairly in the procurement process, and one of the easiest steps to manipulate. Most countries provide for bid evaluation committees for procurement above a threshold value. Experts are called in to assist in evaluating complex bids. Decisions on bids of small value are delegated to the appropriate lower level. A report on the evaluation of bids should be prepared, giving the specific reasons for the recommendations. This process also calls for the exercise of judgment in spotting unrealistically low bids, which will lead to change orders during a project or to unsatisfactory performance. Management in developing countries especially has to be on guard against rigging of the process by a group of suppliers or contractors willing to share the market or rotate jobs. It is important for the results of the bidding process *as a whole* to be evaluated periodically to identify suspicious trends.

Unusual or lengthy delays in bid evaluation are often a sign of trouble, an indication that someone in the system is attempting to discourage the best bidders or give extra time to favored bidders on the basis of leaked information. Such delays should be strongly discouraged.

#### *Award of contract*

The agency should award the contract within the period of validity of the bids to the bidder whose bid has been determined (i) to be substantially responsive to the bidding documents and (ii) to offer the lowest evaluated cost. The bidder should not be required to undertake responsibilities not stipulated in the bidding documents or to otherwise modify the bid. However, if the winning bid exceeds the prebid estimates, the agency may negotiate with the successful bidder to lower the contract price by reducing the scope of work or reallocating responsibility. This process should be transparent and according to objective criteria. There, too, delays are often a symptom of unfair or corrupt practices.

EU requires purchasing agencies to make the results known by means of a contract award notice published in the official journal and the data bank of the EU. The notice should specify the conditions under which the contract was awarded (i.e., the criteria applied and the price). EU also requires agencies to give the reasons for selecting the successful bid to the unsuccessful bidders, and entitles the latter to ask for review based on the claim that proper evaluation procedures were not followed. While many countries follow the practice of making information on the award of contracts

available to the public, there are no uniform practices for informing the unsuccessful bidders.

Rejecting all bids is justified where there is lack of effective competition or none of the bids is substantially responsive. If it rejects all bids, the agency should consider wider advertising, after examining the reasons for the lack of responsive bids or the low number of bidders, and possibly make suitable revisions in the bid documents. Note, however, that rejecting of all bids is sometimes an indication that improper negotiations are being conducted on the side. Similar to undue delays in evaluating bids, rejecting bids may be a device to elicit bribes from contractors, or provide privileged information to “friendly” contractors who can subsequently place an artificially low bid.

#### *Redress of complaints*

Avenues should be available for entertaining legitimate grievances and complaints from bidders about the fairness and confidentiality of the process, and for furnishing clarifications. Most countries provide for procedures within the procurement entity itself for investigating complaints from contractors and their redress or disposition. In Japan, a special unit in the cabinet office considers complaints relating to international competitive bidding. In some countries, complaints can be addressed to the ombudsman if the purchasing agency is unresponsive. Some countries provide for a review of the decision on the award of the bid if representations are received from the other bidders in time, but all procurement decisions are open to judicial challenge in most countries. Attitude is also important. The unresponsive behavior of procurement staff to complaints and suggestions can make it less attractive to do business with the government, and thus reduce effective competition in the future. This, of course, may sometimes be precisely the goal of the unresponsive behavior of procurement staff.

EU requires the establishment of complaint procedures, which allow the bidding firms to challenge decisions taken during the procurement process, either in general courts or in courts with standing jurisdiction over public procurement, or (as in central and eastern Europe) by administrative commissions empowered to intervene. Hungary and Poland have created specialized institutions to deal with public procurement complaints, inspired by the model UNCITRAL law.

## Other Forms of Procurement

### *Sole-source procurement*

Sole-source procurement is also called single-tender purchase, direct selection or direct contracting. It is manifestly appropriate for the purchase of highly specialized systems and equipment, in cases of emergency or natural disasters, or when the standardization of equipment or spare parts (and reasonable prices) justifies additional purchases from the same supplier. In some developing countries, competitive bidding is waived if the procuring entity directly entrusts the supply or works contract to a state-owned enterprise on a negotiated basis. Sole-source purchases account for more than 50 percent of federal purchases in the US, mostly for certain specialized equipment or supplies (as in the aerospace and defense industries), where only one firm is technically qualified to provide the goods, services, or works.

Direct selection is also appropriate and cost-effective in the procurement of consulting services, when a track record of specialized technical expertise is essential and timing is important. This is often the case for public sector management services, when contracts are comparatively small and individual consultants are required.

Direct selection is defensible in developing countries if there are rules for how and when this form of procurement is used and the determination is based on some form of market research and product testing. Otherwise, it could become a cover-up for collusive corruption or bureaucratic laziness in exploring better alternatives. Care must be exercised especially in evaluating the bids in spot purchases of commodities like crude petroleum and armaments, as these have been the subject of scandals in many countries.

### *Requests for proposals*

Requests for proposals (RFPs) are negotiated bids, wherein the parties enter into a contract after discussing its terms, provisions, costs, and other elements. There is no formal bidding. RFPs are most common in consulting or other personal professional services, such as those of architects. Unlike the invitation to bid, which focuses on minimum qualification, RFPs focus on quality. RFPs are also used for sole-source suppliers of special products such as computer software programs or special patents (as for experimental programs like a new process of sewage disposal).

The RFP process starts with defining the scope of services and proceeds to identifying the possible bidders, who are then encouraged to make an offer to provide the service or product. The price and other terms are then negotiated. In developing countries, RFPs create an impression of corruption as they are inherently judgmental, often not transparent, and may lead to higher costs. The combination of technical judgment and negotiation calls for agency skills that are in short supply in many countries, possibly leading them to depend on the judgment of foreign consultants. Since many developing countries use RFPs for projects, this procedure needs carefully worded and transparent policy guidelines and procedural regulations, and personnel skills to manage the process.

*Procurement from other government entities*

Intergovernmental contracting is a service delivery choice in which one government unit agrees to provide a service to another government unit (Rehffuss 1989). A simple example of such a contract is one where a county agrees to collect refuse for a city—a service for which it would normally bill the citizens directly. The county may receive payment from the city or use property tax levies to defray the costs. These quasi-contractual arrangements could be informal.

Joint service agreements, such as those in countries following the French tradition, are formal agreements between local government units (and sometimes state agencies) for joint planning, financing, and delivery of services (such as water supply or data processing) to the inhabitants in the participating jurisdictions. These agreements generally entail formal service contracts (such as for the maintenance of streets and sewage plants) approved by the legislature or the government and legally enforceable. A newly incorporated city could compare the cost of providing all services through its own employees, with the cost of having them provided by another city, and make a rational choice between self-provision and joint services.

Intergovernmental contracting is also a useful means of governmental integration in developing countries. It can ensure uniformity of services and economies of scale, avoid many of the hassles of contract management, and, more importantly, create a habit of cooperation among local government units, or what we may call governmental social capital.

### *Small purchases*

Virtually all countries and international organizations have established a value threshold below which competitive bidding is not required and procurement is delegated to lower levels of authority or shopping procedures are permitted (India and Singapore are Asian examples; also refer to the World Bank practice noted earlier). The procuring entity is allowed to award the contract based on a simple evaluation of at least three quotations obtained from a number of known suppliers. The contract agreement is simple and often consists of a mere exchange of letters. Some countries permit the registration of authorized vendors and the placing of orders with them by rotation during the year. Many countries have made provisions for contracts to be awarded, at a negotiated price, to labor and community associations, after ascertaining their competence and experience.

In developing countries, poor-quality goods are often bought at exorbitant prices through collusion, using the procedure of purchase through quotations, as the Presidential Commission in Tanzania (Box 9.6), for example, has found. This is sometimes the reason behind the practice of splitting annual purchase requirements into several small packages below the threshold level. However, the practice may also be due to fluctuations in the availability of funds for agencies during the year, and the considerable delay from central purchasing. Splitting up a large purchase may be the only way for an agency to get around the inefficiencies of central purchasing offices. Still, since small purchases can add up to a significant part of the budget, the scope for corruption and waste can be substantial. The main safeguards are alert public managers and robust audits of such small purchases on a sample basis. When the splitting-up practice is forced on public managers by inefficient central procurement or overly complex rules, however, the solution is not to prevent the practice but to reform the central procurement entity or streamline the procurement rules.

**Box 9.6**  
**Government Procurement in Tanzania**

The report of the Presidential Commission against Corruption in Tanzania has described and illustrated the nature of corruption in construction tenders and procurement. It noticed a total disregard for rules and regulations. There were huge differences between the tendered cost and the final cost of completion. The commission felt that these contracts were being used to defraud the Government.

Government procurement procedures revealed several deficiencies, allowing loopholes for corruption and large financial misappropriations to develop. Corruption in procurement from the central government stores was because of poor leadership, scarcity of essential commodities due to poor recordkeeping, a lengthy bureaucratic process of collecting goods, and poor procurement systems. Purchase through price quotations, which was to be used only during emergencies, had become the normal procurement procedure. Poor-quality goods had been procured at exorbitant prices through collusion and without the approval of the relevant authority. The procurement of nonexistent goods through the use of proforma invoices had become widespread because of this procedure. Financial orders were not updated and were deficient in laying out procedures for construction tenders. The personnel who handled costing and evaluated tenders did not check current market prices in evaluation. Some bidders bribed their way into the preparation of favorable bid specifications and prequalification. The procurement officers sometimes advised the bidders to quote a low price, and then assisted them with change orders to enable them to receive higher payment. Bids awarded in violation of procedures were nonetheless often ratified by higher authorities.

*Source: Tanzania (1996).*

*Procurement from nonprofit and community agencies*

Local communities or nongovernment organizations (NGOs) are encouraged to participate in contracts in a number of countries, and even in projects assisted by donor agencies. The objective could be to promote project sustainability, achieve specific social objectives, develop local “ownership” of a project, meet user requirements more precisely, or reduce transaction costs. The approach is particularly relevant to the delivery of social services to targeted groups. The nature of community-based procurement will depend on local circumstances and could vary even within the same country. Despite the many advantages of NGO participation in government procurement, there are also risks and pitfalls, and developing

countries need to exercise caution. These issues are discussed at length in Chapter 15.

In many countries, affirmative action policies dictate set-asides for small business, minority business, or women-owned business. These transactions are not always meant to be market-based because they attempt to correct perceived market imperfections or introduce social purposes into economic outcomes.

### **Bidding in Projects Financed by Donor Agencies<sup>12</sup>**

Because of the importance of public procurement in the management of public expenditure and the proper use of external aid, multilateral organizations such as the UN, ADB, World Bank, and EU have issued guidelines for procurement in projects they finance. Most bilateral donor agencies have also issued procurement guidelines, but their practices vary. Several still insist on tying aid to the purchase of all goods and services that are not locally available, including consulting services, to suppliers in the donors' own country, despite the well-known distortions and inefficiencies caused by tied aid.<sup>13</sup> Some donors insist that international competitive bidding be limited to countries within the region. Others require contract clauses relating to social purposes such as the prohibition of child labor. Preference for domestic suppliers is not always included. However, all donors insist on integrity provisions similar to those of the ADB and the World Bank.

The World Bank, ADB, and the other regional development banks recognize that the responsibility for implementing a project rests with the borrower and that the mode of procurement for the project depends on the circumstances and policies in the aid-recipient country. However, they generally insist on the use of standard bidding documents.

Four considerations generally guide the requirements of aid organizations (World Bank 1995):

- economy and efficiency in implementing the project;
- opportunity for all eligible bidders from developed and developing countries to compete for the right to provide goods and works financed by the organization;
- promotion of domestic contracting and manufacturing industries in the aid-receiving country; and
- transparency in the procurement process.

Independently, both the World Bank and ADB have been assisting member countries in incorporating the best principles of procurement in new or amended regulations, and in devising procurement procedures and tender documents that meet the requirements of international conventions. A similar objective has guided the efforts of the Organisation for Economic Co-operation and Development (OECD) to assist the countries of central and eastern Europe in reforming their procurement regulations and practices.

Recently, ADB and the World Bank have issued guidelines on fraud and corruption to require borrowers, as well as contractors, to observe the highest standards of ethics in the procurement and execution of contracts. Some credits have been canceled and a number of contractors and suppliers have been sanctioned—some who were found to have engaged in corrupt practices were barred for long periods (Chapter 17).

## **CONTRACT ADMINISTRATION AND MONITORING<sup>14</sup>**

### **Importance of Contract Administration**

Contract administration and monitoring is a neglected area in many developing countries, reflecting poor implementation capability in government in general. Contracts must be carefully implemented and monitored. Resorting to contracts with private parties does not solve the problems of bureaucracy. Indeed, accountability may become more difficult because at least three organizations are involved: the public organization that completed the bidding process and awarded the contract, the public agency that is expected to oversee the execution of the contract, and the private entity that will execute the contract. Developing countries are rife with examples not only of outrageous delays and excessive costs of implementation, but also of abuse, waste, and fraud in contract execution. Contracting out services, supplies, or works does not relieve the government of responsibility for the manner in which the service is provided or the work constructed, and for the quality of both. Any government that forgets this rule will be very sharply reminded by an angry public as soon as something goes wrong.

The effectiveness of contract management is strongly influenced by decisions made prior to the award of contract. Ambiguous, unrealistic, or conflicting agreements make it very difficult for the public manager to oversee their execution. Contract size also plays a part in determining the scope of contract administration, but the skills of coordination and

negotiation, and in-depth knowledge of contract terms and customer expectations are important in all cases.

Many contracts do not have clear performance standards, which permit the contractor's work to be judged and also protect contractors from arbitrary interference. Procurement managers need to be encouraged to draft contracts that emphasize results, make monitoring feasible, and are easily understandable to field officers and contractor representatives alike.

It is important to note that while the government operates all over the country its procurement for large contracts is concentrated at the center. Consequently, the field administrative units responsible for supervising contract execution often have no idea of the basis for the award of the contract, but nevertheless have to subject themselves to inspection by the oversight agencies.

### **Nature of Contract Monitoring**

#### *Contract monitoring*

Monitoring continues through the life of the contract. No amount of careful preparation of the contract or detailed specifications will ensure adequate performance if the actual performance is not monitored. Monitoring contract execution includes reviewing contractor reports, making inspections, commissioning audits, and obtaining citizen feedback. The relationship between the public official and the contractor should not be adversarial and antagonistic. Nevertheless, direct inspection and observation of the progress of the work remains the most important element. Financial audits, while necessary and usually required, come too late to remedy problems of execution, though they can provide evidence of wrongdoing, which can be used to fight a court case or disqualify the contractor from future work. In contrast, experience suggests that detailed reviews by higher officials often take up too much time and effort without significant results. On the positive side, establishing good and professional relations with the contractor can do much to assure good contract execution.

Often, corruption is permitted by the filing of unrealistically low bids, in the tacit agreement that the contract assessment will be increased after contract negotiations due to unforeseen circumstances. Only strong contract monitoring can prevent these practices.

*Quality assurance*

Quality is a component of economy and quality assurance is a critical aspect of contract monitoring. It relates critically to the clear drafting of the technical and other characteristics of the product, work, or service to be provided under the contract. The nature of the quality assurance task will depend on the nature of the output. Inspectors of construction work, for example, demand compliance with building codes and similar legal mandates in addition to compliance with the purchaser's specifications. Many countries have established quality control units in their public works ministries.

Some developed countries have established the policy of making the contractor responsible for verifying and assuring product quality prior to delivery. However, this policy requires a high degree of contractor responsibility, contract management skill, and swift dispute resolution. All three factors may be deficient in many developing countries. Accordingly, governments in developing countries should be especially careful about relying on physical output performance indicators as this could lead to a lower-quality output (Chapter 18 for a full discussion).

The central procurement office should disseminate guidelines for the inspection and testing of goods and services under different types of contracts, including information on the available testing facilities and on other quality assurance techniques (such as a requirement to obtain certificates of compliance or certified test results to accompany deliveries). There should be a formal system for reporting complaints against vendors by user agencies and the public, for taking action on deficiencies noted during inspection, and for dealing with product warranties and latent defects in goods. The payment schedule should be tied to inspections so that payments can be withheld when problems occur and until they are resolved satisfactorily. Citizen associations should be systematically consulted, not only because of their involvement as stakeholders, but also because feedback from informed citizens is a highly reliable and cost-effective way of monitoring contracts and ensuring the integrity of public officials.

**MILITARY PROCUREMENT<sup>15</sup>**

Military procurement differs from civilian procurement as it is affected by considerations of national security and conducted in a less transparent manner than other forms of procurement. Equally important is the bilateral

monopoly structure of the market for military equipment and weapons on both the supply and the demand side in the US and some European countries, and the consequent political sensitivity of this area of procurement. On the supply side, the enormous fixed costs and scale economies involved in the production of costly defense equipment, and the need for high research and development (R&D) investment in new technology, raise barriers to entry for new companies and establish different principles for recovering costs from the contract. On the demand side, the government exercises monopsony control as single buyer of the equipment and spares produced by the defense industry.

As noted in Chapter 1, despite its decline in the past decade, military expenditure is still huge, amounting to almost US\$500 billion worldwide in 1998, or US\$130 per year per person. Military expenditure must be considered together with the turnover of arms-producing companies in order to comprehend the magnitude of military procurement. The top 100 arms-producing companies had combined arms sales of US\$156 billion in 1997, with the US, France, Russia, and Germany as the major producers.

The officially reported military expenditures in developing countries do not reveal the much higher actual expenditure. Defense allocation is not often disaggregated, and is shown as a single line item in the budget. The additional income from arms exports and the earnings from the business activities of the army are not shown on the revenue side. Off-budget items, such as expenditure on paramilitary forces, food subsidies to army personnel, military research and development, and subsidies for arms production and imports, are often not shown at all. Secrecy in security matters leads to the omission of provisions made for major equipment purchases. All this makes it difficult for oversight agencies to exercise audit and vigilance.

Military expenditure goes to staff emoluments and pensions, various forms of civilian supplies and amenities, and military equipment and supplies. In the US, 60 percent of the amount spent on depot-level weapons systems and maintenance supplies in 1995 was acquired under contract (Jones 1999). Regional agreements, such as those of the EU, seek to eliminate local preferences in the public purchase of civilian goods but exempt military equipment.

It is usually difficult for the ministries of finance in developing countries to regulate expenditure on defense procurement and the use of scarce foreign exchange because of overriding political perceptions of threats

to national security, internal solidarity, and the sensitivity and secrecy surrounding the purchase of major equipment. The requirement for the emergency purchase of equipment and supplies and the superior bargaining advantage of foreign suppliers in many cases, circumscribe the capacity of purchasing departments and the treasury in striking financially favorable deals.

A distinction has to be drawn between sophisticated equipment with a specific defense use and commercial off-the-shelf defense supplies, including items for both civilian and defense use. In the case of purchases of foodstuff, transport, and civilian supplies, the defense establishment can easily apply the principles of procurement discussed above. But even here, of course, there are stories of grotesque overpricing, such as US\$5,000 coffeepots and US\$200 pliers, etc. (Gregory 1998). Aside from possible fraud, overpricing usually arises because of excessive specifications even for everyday items in military contracts, and the need for the military contractor to recover the entire sunken cost of production from a few items supplied to the army (as opposed to spreading the cost across millions of items in the production run for civilian sales).

In the case of defense supplies, many countries tend to buy from home suppliers, even at some additional cost. The label military-industrial complex sums up popular perceptions of the nexus between domestic industry and the defense establishment. Military hardware (aerospace equipment, electronics and telecommunications equipment, explosives, shipbuilding equipment, etc.) accounts for the largest share of total equipment expenditure. Defense equipment and R&D contracts can give a competitive advantage to supplying firms in technological, commercial, and financial terms. The Association of Southeast Asian Nations (ASEAN) countries have pursued a policy of preference for local private industries when it comes to defense supplies.

Other countries rely on defense equipment and supplies from public factories to reduce their dependence on foreign suppliers and their vulnerability to arms embargoes. Some form of arms production is undertaken by 41 countries, including Asian countries like People's Republic of China, India, Korea, and Pakistan (Brazoska 1999). Many of them, including Brazil, Israel, Republic of Korea, Singapore, and South Africa, undertake defense exports of varying magnitudes. Production of arms by the public sector helps to avoid the fraud and abuse associated with procurement from private domestic and foreign suppliers. However, such

production usually covers small arms and ammunition, rather than high-technology equipment, and may be much more costly than outright purchases. Some countries in Europe and Asia have sought to achieve a compromise between outright imports and indigenous self-sufficiency in defense by setting up licensed production units with foreign companies.

It is important to note that the risks and costs of defense procurement are markedly different for countries without an advanced defense industry. Where the countries are obliged to secure defense supplies through imports or purchases in overseas markets, the balance of bargaining power is with the suppliers. Aside from force and corruption considerations, there is a risk of purchasing outdated equipment—weapons that do not fire, planes that do not fly, etc. At the same time, self-sufficiency in defense requirements has not been possible or desirable for developing countries. Even countries with defense production units are obliged to shop for sophisticated arms and aircraft from foreign suppliers. Apart from problems of patents and secrecy, the research and development costs of defense equipment and supplies are unaffordable to most developing countries.

Some countries have sought to apply the principles of civil procurement to defense supplies as well, with built-in procedures for confidentiality. There is a specialized defense procurement division in the Singapore Ministry of Defense, and other countries like Canada have set up similar specialized divisions or agencies for defense procurement. The procurement process is subject to oversight by supreme audit agencies in many countries, and the publication of audit reports for the benefit of the legislature and the public.

Many developed countries have prescribed an elaborate process for defense procurement and a protracted approval process through various levels from the contracting officer to the treasury, and then to a cabinet subcommittee. The process is further complicated by detailed requirements and specifications, compelling the industry to prepare costly and voluminous proposals, which are then analyzed in great detail by a large team of evaluators. Much of the waste and delay that has been publicized in the US has been attributed to overregulation, overspecification, excessive paperwork and audit compliance, too many layers of authority and supervision within the executive, and micromanagement by the Defense Department and the Congress (Gregory 1989). Canada devised the Smart Procurement Initiative in consultation with the defense industry to improve the procurement process. It included innovative steps like incremental acquisition, greater

flexibility and delegation for small-value and off-the-shelf items, streamlined decision making, and partnerships with business.

The situation is different for most developing countries that have a poor defense industry and depend on imports, and the question is not just one of making things easier and fairer for the contractors. The problem there is not overregulation and complexity, but the lack of transparent, credible, and consistent systems for defense procurement, inadequate legislative and audit oversight, and the failure to institutionalize decisions relating to the acquisition of costly equipment. In countries with a weak defense industry base and inadequate purchase evaluation capacity, the potential for bribery is mixed with the danger of purchasing inefficient equipment. Where military aid is provided by developed countries with tied purchases from the donor country, the recipient country often has no control over the cost and quality of the equipment and spares, and merely watches as its foreign debt rises with its defense spending. The country that is locked into the use of particular equipment and transport also becomes vulnerable to a supply cutoff in spare parts and replacements by the donor country. Defense procurement thus becomes the handmaiden of the vicissitudes of foreign policy. At the same time, developed countries seeking to procure military supplies in support of their army operations in a friendly country are beset by collusion and cartels (as in the case of the Republic of Korea in the 1960s; see Klitgaard 1998). Efforts to deal with the problem through bilateral bargaining have opened new avenues for corruption.

The military procurement process is permeated by the interplay of international and domestic companies, liaison agents, arms bazaars, contributions to political parties, and bribes, and is punctuated by the outbreak of scandals and media exposés. The best single cover for corruption in international defense procurement is the commission paid to a local agent by the foreign arms manufacturer or supplier. The agent is given sufficient funds to land the contract without the parent company having to know the details, creating a comfortable wall of distance between the supplier and the act of corruption, and enabling all the parties in the recipient government and the parent company to disclaim any association with the unsavory details of the deal, should these be exposed.

Once again, Singapore is one country that has declared and observes a transparent policy for defense procurement based on open tender. The principle is to go for the best source that meets the requirement and gives value for money. The policy is to deal directly with overseas and domestic

suppliers and avoid dealing with intermediary agents in contract negotiations. This is much easier said than done, however, for most developing countries, where accountability and public management are not as strong.

## SAFEGUARDING INTEGRITY IN PROCUREMENT<sup>16</sup>

### Areas of Corruption

The subject of corruption is dealt with in Chapter 17. This section discusses briefly specific aspects of corruption in procurement, which is a major problem in all countries and at all levels of government and administration. This problem is hardly new. Over 2,000 years ago, Kautilya wrote in *Arthashastra*

*Just as it is impossible not to taste honey or poison that one may find at the tip of one's tongue, so is it impossible for one dealing with government funds not to taste, at least a little bit, of the king's wealth.*

Corruption can occur in procurement mainly if there is excessive regulation; the rules are not clear and accessible to the public; the bid documents are poorly drafted or ambiguous; the specifications and standards are not clear; and contract monitoring is loose. Accordingly, either the procurement unit or the bidder can corrupt the procurement process. The procurement unit can

- tailor the specifications to benefit particular suppliers or contractors;
- restrict information on bidding opportunities to only some potential bidders;
- claim urgency as an excuse to award the contract on a sole-source basis;
- give preferred bidders confidential information on offers from other bidders;
- disqualify potential suppliers through improper prequalification or excessive bidding costs; and
- act directly in collusion with the bidders or outside influences to distort the entire process.

The bidders, too, can take a number of actions to distort the bidding process and its outcome, such as

- colluding among themselves to fix bid prices;
- colluding to establish a rotation or other system by which bidders will not participate by turns or will deliberately submit unacceptable or technically unsuitable offers (even the most careful scrutiny of individual transactions will not reveal this tactic, as mentioned earlier, it is necessary from time to time to review all the procurement results for a given period);
- promoting discriminatory technical standards; and
- using their influence or bribes to push political leaders or senior public officials to interfere improperly in bid evaluation.

However, the most direct approach to bribery is to avoid competitive bidding altogether, and contrive to have the contract awarded to the desired party through direct negotiations without any competition.

After the bids are submitted, other opportunities for misbehavior arise. As noted earlier, confidentiality is critical to the fairness of the exercise. Where the rules do not provide for all bidders to be present at the time the bids are opened, it is easy for the procurement officer to reveal the lowest bid to the desired bidder and enable the latter to submit an even lower bid, which is then included in the bid evaluation process.

Serious corruption problems arise also during the contract execution phase, after the award of contract, through practices such as

- failing to enforce quality standards, quantities, or other performance standards of the contract (it is often understood in advance that enforcement will be superficial or nonexistent);
- paying for shoddy construction, or agreeing to the delivery of unacceptable goods and services, or acceding to fictitious claims of losses in transit or false deductions for material losses in construction;
- permitting “lowballing” (accepting artificially low bids, which are then jacked up by mutual consent, for a price);
- delaying payments to extort a bribe;
- spot purchases of commodities during emergencies; or
- giving individual legislators influence over the award of contracts in their constituencies (the so-called pork barrel).

By far the easiest and most profitable form of corruption in public procurement or works is simply not to deliver the goods or build the works.<sup>17</sup> In countries with weak accountability systems, very low administrative

capacity, or widespread systemic corruption, it is not a difficult matter to falsify delivery documents or certificates of work completion. It is in this area that citizens' feedback can be a powerful weapon against corruption.

Political corruption, either financing of political parties in exchange for contracts or official posts, or cooptation of legislators by giving them influence over the award of contracts in their constituencies, is frequent in many developed and developing countries, but goes beyond the scope of this book. It is clear, however, that illicit political financing or pork-barrel politics are a blight on the integrity, efficiency, and effectiveness of public administration. The remedies, however, are almost entirely political and not technical or administrative. This is a major reason why illicit political financing is excluded in the OECD Anti-Bribery Treaty (Chapter 17).

### **International Efforts to Secure Integrity in Procurement**

International lending agencies like UN, World Bank, and ADB are contributing significantly to combating corruption in procurement. The General Procurement Principles for UN agencies require all procurement officials in these agencies to maintain an unimpeachable standard of integrity in their business relationships, both inside and outside the organizations in which they are employed, and not to use their office for personal gain. The amendment made by the World Bank to the standard bid documents in October 1996 requires the borrowing countries, as well as bidders, suppliers, and contractors, to observe the highest standards of ethics in the procurement and execution of such contracts.

The guidelines of all UN agencies and many bilateral donors require that the bidders shall not be under a declaration of ineligibility for corrupt and fraudulent practices. ADB encourages the borrowing country to introduce, in the bid forms for large contracts, an undertaking by the bidder to observe the country's laws against fraud and corruption in competing for and executing the contract. The World Bank will disqualify a firm indefinitely or for a stated period from contracts for World Bank-financed projects if it finds that the firm has engaged in corrupt practices.

Bidders are also required to furnish information on commissions or gratuities paid to agents relating to the bid and to certify that they have not given or received any gifts, commissions, or payments other than those shown in the bid. It is too early to evaluate the impact of these measures.

## **Building Capacity for Public Procurement**

As Walsh and Leigland point out (in Perry 1996), the skills and professional standards of the procurement officials, while not easy to attain, are the most effective safeguard against irregularities and graft. It is risky, and unwise in the interest of building up long-term skills, to rely fully on external consultants to operate the procurement system. And, as noted earlier, the procurement function should be made a part of the required competencies of senior managers, and efficient discharge of this function should be made a performance requirement of senior management.

Postaward contract administration and monitoring require special skills to ensure that the contracting obligations are met on time and to resolve problems. Legal skills are required to interpret contracts and to pursue complaints before arbitrators and the courts. The central procurement agency should help the departments to maintain current information on technical aspects, contract law, management, and procurement practice, and finance the attendance of civil servants in procurement courses; rotation, promotion programs, and the lateral recruitment of experienced individuals from the corporate sector and universities for managerial positions; and develop procurement internship programs.

Countries need to incorporate modules on procurement management in their civil service training. Donor agencies could promote these efforts and assist in the transfer of training expertise from developed countries.

Government agencies have the additional responsibility of initiating and assisting in the professionalization of small contractors, and building the capacity of voluntary agencies and community organizations at the local level to handle service and small work contracts.

Chambers of commerce and contractors' associations in different countries could also develop networks and transfer good procurement practices and training programs for their members and for government procurement managers.

In highly politicized operating environments, honest and efficient procurement demands that civil servants be protected from political "suggestions" and provided the security of adequate compensation, swift penalties for violators of the rules, and protection for whistle blowers.

## KEY POINTS AND DIRECTIONS OF IMPROVEMENT

### Key Points

Government procurement of goods, services, and public works accounts for a large proportion of public expenditure in all countries, and is one of the major sources of corruption in many countries. Clearly, the procurement function is very important, and yet it typically does not receive commensurate attention from senior leadership in most governments.

The government and the private sector differ significantly in the way they conduct their purchasing operations. The main criterion for sound procurement in both sectors is *economy*, i.e., the timely acquisition of goods and services of a given quality at lowest cost. In public procurement, however, other criteria also apply: import substitution, fostering competition, and protecting the consumers. In most countries, environmental considerations and additional social criteria, such as affirmative action for small business, minorities, women, and depressed regions are also relevant.

The legal framework for public procurement consists of general contract law, specific procurement regulations, and procedural manuals. The framework has been shaped in recent years by the international trade regime and the advocacy by multilateral donor agencies of guidelines to prevent corruption and fraud.

In managing the public procurement process, centralization is required for setting the standards, monitoring the outcomes, and providing an appeal mechanism. It may also be advisable in the short run to retain central procurement of strategic and critical supplies such as information technology. In most cases, however, actual procurement operations should be decentralized to the ministries and agencies concerned within the framework of central procurement standards, rules, and oversight.

Procurement procedures must be clear, simple, and made available to the public. Procurement decisions should be recorded and communicated in writing, along with the reasons behind them. Accountability agencies should be able to determine after the fact who made the crucial decisions and why. Tender opportunities in large contracts should be widely publicized, to attract an adequate number of qualified

bidders. Shared databases on contractor performance are needed at national and regional levels to limit the likelihood that the wrong contractors will be selected, and to weed out contractors with a record of dishonesty or incompetence.

Competitive bidding is the rule in public procurement. However, there is justification for giving preference or set-aside quotas in local contracts for goods and services to small businesses and informal enterprises, cooperatives, and disadvantaged groups, provided the costs are not excessive and that unsustainable subsidies are not required over time. Also, construction contracts for local works and services lend themselves to direct contracting to community associations, without competitive bidding. Some degree of domestic preference is also legitimate for developing countries, as recognized by international organizations, to boost local businesses and small suppliers' capacity. Governments should avoid, however, cost-plus direct selection, or the captive purchase of the production of ailing public enterprises to enable their survival.

As mentioned, competition is the rule in public procurement. Private sector procurement, instead, relies to a large extent on semipermanent commercial relationships with specific suppliers. The different forms of procurement are international competitive bidding, national competitive bidding, shopping, and direct (or sole source) selection. For large purchases and contracts, competitive bidding is almost always preferable. The stages of competitive bidding include setting of clear specifications; issuing public notice and invitation to bid; bid opening and evaluation; and contract award and conclusion. The process must incorporate safeguards to ensure its integrity and impartiality, and to prevent collusion, corruption, and fraud.

After the contracts are concluded, they must be carefully monitored. Several types of controls and reporting, including audits and citizens' complaints, can be used to deal with contractual problems, but there is no substitute for close government supervision of the execution of a clean contract.

### **Directions of Improvement**

In developing and transitional economies, improving the procurement system to meet standards of economy, competition, accountability, and honesty generally requires moving to

- simplified legal and regulatory framework for procurement;
- clear organizational arrangements, combining centralized procurement policy/oversight with decentralized operations;
- improved public access to information and documentation;
- measures to ensure that only civil servants of competence and integrity are in charge of government procurement, and providing for commensurate rewards through career options and frequent rotation;
- simple and transparent process of procurement, whichever method is chosen;
- more effective mechanisms to curb fraud, abuse, and corruption, with appropriate assistance from international organizations; and
- more attention to contract execution and monitoring.

In many developing countries, efforts to close loopholes for corruption or to achieve social goals have created increasingly detailed regulations and centralized control. The problem is especially acute for the acquisition of technology and other products that change rapidly and have a short product cycle. A major improvement would be to review the value thresholds above which the complex bidding rules apply in their entirety, and to raise these thresholds with inflation. In many developing countries, low-value items make up the bulk of procurement, especially in local government and field offices, and complicated regulations intended to prevent the misappropriation of very small sums generate far greater transaction costs for both the government and the private supplier. Worse, as noted in Chapter 1, they are usually ineffective in preventing large-scale corruption, precisely because of their complexity and the resulting delays, discretion, and lack of transparency. The main direction of improvement is to achieve a better balance between controls and managerial flexibility. Most developing countries need fewer but clearer and more robust rules, together with swift and predictable enforcement.

In developing countries, the uneven documentation and bidding procedures of different government entities compound the problem of excessive controls. Standard bid documents for goods and services, as well as work contracts, are in fact enforced for donor-assisted projects. Major

improvements in economy and integrity would result from extending such standard bidding documents to all government procurement because their use reduces opportunities for undue discretion, collusion, and extortion. Developing countries can also benefit from external assistance to improve the regulatory and organizational framework, and build capacity in their procurement offices, but should not rely mainly on external consultants for actual procurement operations.

Other improvements in procurement in developing countries could be realized by addressing the slowness of the dispute resolution mechanisms. The process is slow partly because of weaknesses in the judicial system and partly because of the complex appeal procedures. The process of recovering money from suppliers in case of bad performance or default is cumbersome and often fruitless because of antiquated foreclosure laws and the manipulation of bankruptcy laws by defaulters. Contractors also face protracted legal battles in recovering disputed sums from government. With the government and the contractors thus forced to take steps to protect themselves from these eventualities, transaction costs increase for both sides, making the purchase of goods and services, and contracting, much more costly in the government than in the private sector. Overall weaknesses in the judicial system are a broader problem, which could be dealt with by establishing a streamlined and fast-track procedure for appealing administrative court decisions on procurement disputes.

Finally, although the process of procuring goods, services, and works is critical for the economical and effective use of public funds, procurement issues have not received much attention from senior public managers and political leaders. In part, senior managers are not interested in the mechanics of procurement; they are also concerned with keeping their distance (and deniability) from potential waste or corruption scandals. Yet, they must realize the great importance of procurement in an efficient, effective, and honest government, and place it at the center of their responsibility rather than shunting it off to lower-level staff. In turn, political leaders must give them their support in the exercise of this delicate responsibility.

Annex V

**UNCITRAL MODEL LAW ON PROCUREMENT OF  
GOODS, CONSTRUCTION, AND SERVICES<sup>18</sup>**

**WITH  
GUIDE TO ENACTMENT**

**CONTENTS**

**PREAMBLE**

**CHAPTER I GENERAL PROVISIONS**

- Article 1 Scope of Application
- Article 2 Definitions
- Article 3 International obligations of this State relating to procurement  
[and intergovernmental agreements within (this State)]
- Article 4 Procurement regulations
- Article 5 Public accessibility of legal texts
- Article 6 Qualifications of suppliers and contractors
- Article 7 Prequalification proceedings
- Article 8 Participation by suppliers or contractors
- Article 9 Form of communications
- Article 10 Rules concerning documentary evidence provided by  
suppliers or contractors
- Article 11 Record of procurement proceedings
- Article 12 Rejection of all tenders, proposals, offers, or quotations
- Article 13 Entry into force of the procurement contract
- Article 14 Public notice of procurement contract awards
- Article 15 Inducements from suppliers or contractors
- Article 16 Rules concerning description of goods, construction, or  
services
- Article 17 Language

**CHAPTER II METHODS OF PROCUREMENT  
AND THEIR CONDITION FOR USE**

- Article 18 Methods of procurement
- Article 19 Conditions for use of two-stage tendering, request for  
proposals, or competitive negotiation

- Article 20 Conditions for use of restricted tendering
- Article 21 Conditions for use of request for quotations
- Article 22 Conditions for use of single-source procurement

### **CHAPTER III TENDERING PROCEEDINGS**

#### **SECTION I SOLICITATION OF TENDERS AND OF APPLICATIONS TO PREQUALIFY**

- Article 23 Domestic tendering
- Article 24 Procedures for soliciting tenders or applications to prequalify
- Article 25 Contents of invitation to tender and invitation to prequalify
- Article 26 Contents of solicitation documents
- Article 27 Clarifications and modifications of solicitation documents
- Article 28 Clarifications and modifications of solicitation documents

#### **SECTION II SUBMISSION OF TENDERS**

- Article 29 Language of tenders
- Article 30 Submission of tenders
- Article 31 Period of effectiveness of tenders; modification and withdrawal of tenders
- Article 32 Tender securities

#### **SECTION III EVALUATION AND COMPARISON OF TENDERS**

- Article 33 Opening of tenders
- Article 34 Examination, evaluation, and comparison of tenders
- Article 35 Prohibition of negotiations with suppliers or contractors
- Article 36 Acceptance of tender and entry into force of procurement contract

### **CHAPTER IV PRINCIPAL METHOD FOR PROCUREMENT OF SERVICES**

- Article 37 Notice of solicitation of proposals
- Article 38 Contents of requests for proposals for services
- Article 39 Criteria for the evaluation of proposals
- Article 40 Clarification and modification of requests for proposals
- Article 41 Choice of selection procedure
- Article 42 Selection procedure without negotiation

- Article 43 Selection procedure with simultaneous negotiations
- Article 44 Selection procedure with consecutive negotiations
- Article 45 Confidentiality

## **CHAPTER V PROCEDURES FOR ALTERNATIVE METHODS OF PROCUREMENT**

- Article 46 Two-stage tendering
- Article 47 Restricted tendering
- Article 48 Request for proposals
- Article 49 Competitive negotiation
- Article 50 Request for quotations
- Article 51 Single-source procurement

## **CHAPTER VI REVIEW**

- Article 52 Right to review
- Article 53 Review by procuring entity (or by approving authority)
- Article 54 Administrative review
- Article 55 Certain rules applicable to review proceedings under Article 53 [and Article 54]
- Article 56 Suspension of procurement proceedings
- Article 57 Judicial review

## **NOTES**

- <sup>1</sup> This section has drawn mainly on Transparency International (1996); Walsh and Leigland in Perry, ed. (1989); WTO statistics; internal ADB memoranda and country profiles; Kettl, et al. (1991); Dehoog in Cooper and Newland, eds. (1997); and Commonwealth Secretariat (1995a).
- <sup>2</sup> The World Bank, for example, has stipulated the use of a separate set of documents for construction contracts.
- <sup>3</sup> Following the adoption of Agenda 21 in the International Conference on Environment and Development in 1992.
- <sup>4</sup> This section relies partly on WTO statistics; OECD (1997e, 1999a); Sherman (1987); Dehoog in Cooper and Newland, eds. (1997); and internal ADB memoranda and country profiles.

- <sup>5</sup> The commission is a UN agency set up to promote the harmonization of international laws relating to trade. It has formulated other model laws on international commercial arbitration and conciliation, international sale of goods and related transactions, cross-border insolvency, international payments, international transport of goods, electronic commerce, and international construction contracts.
- <sup>6</sup> This section has drawn partly on Dehoog in Cooper and Newland, eds. (1997); Perry (1989); WTO statistics; Corrigan et al. (1999); and internal ADB memoranda and country profiles.
- <sup>7</sup> This section has drawn from Walsh and Leigland in Perry, ed. (1989); Dehoog in Cooper and Newland, eds. (1997); OECD (1999a); internal ADB memoranda and country profiles; procurement guidelines issued by the World Bank and the Asian Development Bank; and details of national practices available in the statistical data published by the World Trade Organization.
- <sup>8</sup> These may include procurement from UN agencies, procurement in loans to financial intermediaries, procurement under build-operate-transfer and similar private sector arrangements, and community procurement.
- <sup>9</sup> Prebid action in the case of construction and works also requires the prior assembly of land and site where the work will be performed.
- <sup>10</sup> Donor organizations normally publish these in both paper and electronic forms, as, for example, the *Asian Development Bank Business Opportunities*.
- <sup>11</sup> The fee charged for the documents should be reasonable and should reflect only the cost of printing and delivery, and not so high as to discourage small bidders. Bid security should also not be set so high as to discourage bidders. The security could be in any acceptable form, such as a certified check, bank draft, letter of credit, or cash.
- <sup>12</sup> The description is based on the published guidelines and bid documents of the World Bank and the Asian Development Bank.
- <sup>13</sup> See Schiavo-Campo and Singer (1970).
- <sup>14</sup> This section relies mainly on Sherman (1987); Dehoog in Cooper and Newland, eds. (1997); and Rehfuss (1989).
- <sup>15</sup> This section was drawn in part from Stockholm International Peace Research Institute (1999); Gregory (1989); Brazoska (1999); and Jones (1999).
- <sup>16</sup> This section was drawn in part from Pope, ed. (1996); Cooper and Newland, eds. (1997); Walsh and Leigland, in Perry, ed. (1989); Tanzania (1996); Mccampbell, et al. (1997); and World Bank (1997).
- <sup>17</sup> Although even this pales in comparison to the single most efficient and least verifiable form of corruption by far: privileged access to undervalued foreign exchange, which is then sold at a premium on the informal market, for a riskless, costless, and almost instant profit. Procurement is a major source of corruption, but is by no means the only one.
- <sup>18</sup> For a detailed treatment of the model, the interested reader is referred to (<http://www.uncitral.org/english/texts/procurem/mlprocur.htm>).