OUTSOURCING PROCUREMENT IN THE PUBLIC SECTOR

Asian Development Bank
# Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>iv</td>
<td>Tables and Figures</td>
</tr>
<tr>
<td>v</td>
<td>Foreword</td>
</tr>
<tr>
<td>vi</td>
<td>Acknowledgments</td>
</tr>
<tr>
<td>vii</td>
<td>Abbreviations</td>
</tr>
<tr>
<td>viii</td>
<td>Executive Summary</td>
</tr>
<tr>
<td>1</td>
<td>Introduction</td>
</tr>
<tr>
<td>3</td>
<td>I. General Role of Procurement Agents in the Public Sector</td>
</tr>
<tr>
<td>6</td>
<td>II. Procurement Agents and Official Development Assistance</td>
</tr>
<tr>
<td>6</td>
<td>A. Using Procurement Agents in Projects Financed by Official Development Assistance</td>
</tr>
<tr>
<td>10</td>
<td>B. Using Procurement Agents in ADB-Financed Projects: Policy and Related Issues</td>
</tr>
<tr>
<td>14</td>
<td>III. The Regulated Market-Based System in the People’s Republic of China</td>
</tr>
<tr>
<td>14</td>
<td>A. Legal and Institutional Frameworks</td>
</tr>
<tr>
<td>17</td>
<td>B. Accreditation of Procurement Agents in the People’s Republic of China</td>
</tr>
<tr>
<td>18</td>
<td>C. Analysis: Advantages and Challenges of the People’s Republic of China Model</td>
</tr>
<tr>
<td>23</td>
<td>IV. The Centralized Procurement Agency Model</td>
</tr>
<tr>
<td>24</td>
<td>A. Case Studies</td>
</tr>
<tr>
<td>35</td>
<td>V. Conclusion: Basic Considerations for the Future</td>
</tr>
<tr>
<td>36</td>
<td>A. Developing the Legal, Regulatory, and Institutional Frameworks</td>
</tr>
<tr>
<td>38</td>
<td>B. Outsourcing Procurement at the Project and Agency Levels</td>
</tr>
<tr>
<td>42</td>
<td>Appendixes</td>
</tr>
<tr>
<td>42</td>
<td>1 Case Studies on the Two Roles of Procurement Agents</td>
</tr>
<tr>
<td>45</td>
<td>2 The Success Story of Consip, Italy</td>
</tr>
</tbody>
</table>
# Tables and Figures

## Tables

<table>
<thead>
<tr>
<th>Table</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Procurement Agent Service Fees Set by the National Development and Reform Commission (as of 2010) (%)</td>
<td>15</td>
</tr>
<tr>
<td>2</td>
<td>Certified Procurement Agents in the People's Republic of China, 2010</td>
<td>16</td>
</tr>
<tr>
<td>3</td>
<td>Advantages and Disadvantage of the Centralized and Decentralized Procurement Models</td>
<td>27</td>
</tr>
<tr>
<td>4</td>
<td>Differences between Highest and Lowest Prices for Similar Goods in the United Kingdom</td>
<td>40</td>
</tr>
</tbody>
</table>

## Figures

<table>
<thead>
<tr>
<th>Figure</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Target Time Taken for Single-Stage-One-Envelope International Competitive Bidding</td>
<td>11</td>
</tr>
<tr>
<td>2</td>
<td>Actual Average Time Taken for Bid Evaluation by Executing Agencies for Single-Stage-One-Envelope International Competitive Bidding</td>
<td>11</td>
</tr>
<tr>
<td>3</td>
<td>Total Value of Public Procurement in the Republic of Korea and the Percentage of Public Procurement Service Pass-Through, 2011</td>
<td>27</td>
</tr>
<tr>
<td>4</td>
<td>Reduction of the Procurement Budget in the Public Procurement Service through Price Analysis ($ million)</td>
<td>28</td>
</tr>
<tr>
<td>5</td>
<td>Price Comparison Samples: Private Market Prices versus Multiple Award Schedule Contract Prices</td>
<td>29</td>
</tr>
<tr>
<td>6</td>
<td>Price Comparison Samples for Common Use Items: Private Market Prices versus the Procurement Service of the Department of Budget and Management Prices (%)</td>
<td>32</td>
</tr>
<tr>
<td>7</td>
<td>Planned Responsibilities for the New Procurement Service of the Department of Budget and Management Corporate Entity</td>
<td>34</td>
</tr>
<tr>
<td>8</td>
<td>Decision Process for Make or Buy, Adapted to Public Procurement</td>
<td>41</td>
</tr>
</tbody>
</table>
In the development world, we constantly encounter the terms capacity development and capacity building. In the Asian Development Bank, within the context of project implementation arrangements and risk assessments, we often identify the executing agency’s limited project management capacity to implement a certain project, and regularly consider risk mitigating measures to build capacity. However, we have to start considering whether it is absolutely essential for all public agencies to handle all aspects of project implementation. In particular, if procurement is not a core function of an agency, it may investigate the option of outsourcing this responsibility, especially if its resources are limited. This paper explores the issues surrounding such an option, not only at the public agency level but also within the context of broader policy considerations, particularly in terms of improving the impact of development projects.

Sean O’Sullivan
Director General
Operations Services and Financial Management Department
Asian Development Bank
Acknowledgments

Asian Development Bank (ADB) staff member Jose Luis Syquia was responsible for writing this publication, with the guidance of Yinguo Huang, Ignatius Santoso, and Jeffrey Taylor. Ahmadou Barry, Qing Zheng, and Keiko Koiso provided significant input, and Ailene Susara was responsible for all administrative matters.

This paper also expounds on the presentations and discussions during the Regional Conference on the Use of Procurement Agents in Public Procurement, held on 6–7 September 2012, in Beijing, People’s Republic of China. The conference was jointly organized by ADB and the China Tendering and Bidding Association to provide a venue for developing member countries of ADB to share experiences and approaches on the use of procurement agents, and to discuss related issues such as governance, integrity, and capacity development. National and international procurement agents also shared their experiences, and representatives from the following developing member countries participated in the conference: Bangladesh, Cambodia, Indonesia, Mongolia, Nepal, Pakistan, the Philippines, and Viet Nam.

The ADB team wishes to express its sincere appreciation to all the senior officials of the National Development and Reform Commission, the Ministry of Finance, the Ministry of Commerce, and the China Tendering and Bidding Association in the People’s Republic of China; the National Public Procurement Agency of Indonesia; and the Public Procurement Service of the Republic of Korea—particularly Li Kang, Wu Jin Kang, Zhou Ruo Jun, Agus Rahardjo, Hee-Seok Byeon, and Huo Chun Lin—for participating in the conference, and for sharing their vast knowledge and experiences on the subject. The ADB team also wishes to thank all of the distinguished speakers in each of the conference sessions for patiently elaborating upon the various issues at a technical level; each of the government representatives from Bangladesh, Cambodia, Indonesia, Mongolia, Nepal, Pakistan, the Philippines, and Viet Nam; as well as the representatives from the World Bank, Australian Agency for International Development, Charles Kendall and Partners, Crown Agents, and the International Procurement Agency, for candidly sharing their own experiences and challenges. These have certainly enriched the discussions during the conference, and the content of this publication.
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>CKP</td>
<td>Charles Kendall and Partners</td>
</tr>
<tr>
<td>CTBA</td>
<td>China Tendering and Bidding Association</td>
</tr>
<tr>
<td>DBM</td>
<td>Department of Budget and Management</td>
</tr>
<tr>
<td>DMC</td>
<td>developing member country</td>
</tr>
<tr>
<td>EU</td>
<td>European Union</td>
</tr>
<tr>
<td>GDP</td>
<td>gross domestic product</td>
</tr>
<tr>
<td>ICB</td>
<td>international competitive bidding</td>
</tr>
<tr>
<td>ICGP</td>
<td>institutions for the centralized government procurements</td>
</tr>
<tr>
<td>IPA</td>
<td>Independent Procurement Agent</td>
</tr>
<tr>
<td>JICS</td>
<td>Japan International Cooperation System</td>
</tr>
<tr>
<td>JNPGA</td>
<td>Japan Non-Project Grant Aid</td>
</tr>
<tr>
<td>KONEPS</td>
<td>Korea On-line E-Procurement System</td>
</tr>
<tr>
<td>MCC</td>
<td>Millennium Challenge Corporation</td>
</tr>
<tr>
<td>MAS</td>
<td>Multiple Award Schedule</td>
</tr>
<tr>
<td>MOC</td>
<td>Ministry of Commerce</td>
</tr>
<tr>
<td>MOFA</td>
<td>Ministry of Foreign Affairs</td>
</tr>
<tr>
<td>NDRC</td>
<td>National Development and Reform Commission</td>
</tr>
<tr>
<td>ODA</td>
<td>official development assistance</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>PPS</td>
<td>Public Procurement Service</td>
</tr>
<tr>
<td>PRC</td>
<td>People's Republic of China</td>
</tr>
<tr>
<td>PS-DBM</td>
<td>Procurement Service of DBM</td>
</tr>
</tbody>
</table>
Executive Summary

Public procurement should not only be viewed as a one-off process of obtaining goods and services but should also be considered within the broader context of supplier and contractor management, and getting value for money. Even if the procurement function is not part of an agency’s primary mandate, its relevance should not be underestimated, because the attainment of the overall organizational goals and specific project objectives will depend heavily on the way such function is managed. It is within this context that one should consider an agency’s institutional capacity to handle procurement, and determine whether it would be a viable option to outsource this function.

The use of specialized agents in public procurement can be an effective step towards ensuring that development outcomes are achieved. When the problems of weak institutional capacities, high costs, delays, and high integrity risks are systemic in a government, outsourcing the procurement function may be a sound option to consider, whether as a short-term gap-filling measure or as a longer-term strategic approach. Similarly, for official development assistance projects, some important considerations factor into a decision to engage the services of procurement agents: (i) inefficiencies; (ii) fiduciary concerns; (iii) weak capacities, compounded by the possibility of having to operate under a number of different and unfamiliar procurement systems; and (iv) the need to obtain the best quality and value of goods and services. With respect to (iv), procurement agents are considered to be knowledgeable of, and able to operate under, the procurement systems of several development partners and national laws and regulations.

However, some basic issues need to be considered before a decision to outsource the public procurement function can be reached. For example, since a procurement agent is contracted by the client agency, a question may arise as to how a procurement agent can maintain its independence and objectivity during the evaluation of bids, particularly when a difference in opinion arises with the executing agency. This question is especially crucial in situations where decisions are made within environments with high integrity risks. Therefore, for a procurement agent system to effectively work within the public procurement structure of a country, it is absolutely essential to establish the appropriate legal framework at the national level, along with effective agency-level mechanisms to ensure the independence and integrity of procurement agents, so that the entire procurement agent system actually supports a competitive, fair, and transparent public procurement environment.

Based on their experiences, executing and implementing agencies in the People’s Republic of China have reported that procurement agents actually provide substantial benefits in that they (i) minimize information asymmetry by providing agencies with the necessary leverage in terms of market and technical expertise, knowledge of the rules, and integrated information channels; (ii) reduce legal risks through their familiarity with relevant laws and regulations; (iii) provide professionalism; and (iv) contribute to the advancement of new approaches and international practices. The experiences of the governments of Italy, the Republic of Korea, and the Philippines reveal that a centralized national procurement agent system can also generate substantial savings (an average of 20%–30%) through the aggregation of requirements and bulk purchasing.
Since public procurement constitutes a significant part of a government’s total budget (around 15%–20%), there is a compelling argument for countries to explore various options to ensure that public funds are effectively utilized, value for money is achieved, and intended development outcomes are realized. Indeed, procurement outsourcing may be an effective option if utilized properly and thoughtfully. However, it should be recognized that this subject spans at least three levels: (i) the development of policies and frameworks at the national policy level, (ii) implementation at the project management and administration level, and (iii) organizational decisions at the procuring agency level. The basic considerations and options that are open to a decision maker will depend on the level at which she or he operates. However, all these levels are inevitably intertwined. For instance, the decision to outsource procurement at the project and organizational levels will depend heavily on the enabling environment that is established at the national level; in that, a decision to outsource can only be implemented if the law or relevant regulation allows it, and if the appropriate institutional arrangements exist. Unfortunately, most legal frameworks still do not recognize the option of procurement outsourcing and the potential benefits it may provide. Moreover, even if some of these laws open the doors to varying forms of procurement agent systems, only a few jurisdictions have managed to successfully integrate such an approach into actual operations so that broader developmental impacts are realized.

As with most reforms, while it may not be difficult to adjust the legal framework to accommodate procurement outsourcing, implementing it effectively is a different matter altogether. It demands a thorough understanding of several issues, such as the scale of a country’s public procurement budget at both the national and local levels, the various categories of a government’s total spending for public goods and services, the capacity of both the local and international markets to meet the government’s requirements, and the appetite of both the public and private sectors for procurement agents. For this reason, if a government seriously intends to consider procurement outsourcing, it needs to ensure that any policy it adopts is not only compatible with its country’s political, cultural, and operating environments but is also practical and suitable for its procuring agencies.
Multilateral development banks and bilateral aid agencies may dedicate major resources developing the capacity of public agencies tasked to handle development projects, with the objective of improving implementation outcomes and reducing project-related risks. For example, agency risk assessments are regularly undertaken for projects to be financed by the Asian Development Bank (ADB), and it is not uncommon to have a risk mitigating measure that addresses capacity constraints in procurement through a capacity development program.

If one considers that public agencies are normally expected to handle all administrative responsibilities for the projects they manage, whether financed through local funds or with development assistance, then it would be reasonable to focus resources towards developing their capacities to effectively perform these tasks. However, one may also consider that it may not be absolutely essential for all public agencies to handle each and every aspect of project implementation. Procurement is one area that may fit this category. For example, it may not be advisable to dedicate substantial resources to train agency personnel in public procurement management for a foreign-assisted project if the agency does not regularly implement such projects. The same argument may be made even in the case of locally financed projects. When project administration, management, and implementation forms part of an agency’s primary mandate (as with civil works agencies), it would be prudent to invest in building in-house capacity to handle public procurement. However, other agencies such as social welfare agencies or local government units where staff resources may be insufficient to effectively undertake all project management responsibilities may have to focus most of their scarce resources on delivering direct public services. In
these cases, since procurement is not normally a core function, it may be more efficient and effective to simply outsource this responsibility.

The subject of outsourcing raises yet another set of issues, such as whether or not there actually is a market to outsource the procurement function. Indeed, since procurement is a highly specialized field, one would expect the market to exist in varying degrees throughout Asia and the Pacific. For example, while the People’s Republic of China appears to have a developed market with around 5,000 procurement agents certified at the state-level ministries, the situation in other countries may not be as conducive to a market-based approach. In most countries, the local market is totally missing, while in others, such as the Republic of Korea and the Philippines, the role is being performed by centralized procurement agencies.

The broader issue of linkage with development impacts also needs to be considered. The operational role of a procurement agent is widely recognized in both the private and public sectors, particularly in identifying, soliciting, and selecting sources, and in advising the client during contract implementation. Their services are also being used in projects financed by development agencies such as ADB and the World Bank. Yet, it seems that this subject has not been fully explored within the broader context of public sector development, such as in terms of its relevance to a country’s governance and anticorruption program. This broader context is extremely relevant within ADB’s framework on managing for development results because of its potential for improving country outcomes and overall development effectiveness.

All of these issues are considered in this paper. The general role of procurement agents in the public sector and foreign-assisted projects is first discussed in sections I and II, followed by an analysis in section III of the market-based system in the PRC, which looks at how such a system developed, the necessary frameworks that underpin the system, the use of an accreditation system, and some observations on its advantages and challenges. Section IV presents various models of the centralized procurement agency approach, particularly those adopted by Italy, the Republic of Korea, and the Philippines. Finally, section V explores basic principles and various options that need to be considered in developing a procurement agent system.
I. General Role of Procurement Agents in the Public Sector

Procurement has been defined as the process of obtaining goods and services in any way, including borrowing and leasing, and is considered to be a broader term than purchasing, which implies the acquisition of goods or services in return for a monetary or equivalent payment. While technically sound, the problem with this definition is that it gives the impression that procurement and purchasing are (i) reactive service activities where one is simply instructed to buy, rather than a decision-making process where one takes the initiative to help determine appropriate procurement approaches; (ii) transactional activities that are merely concerned with the placing of orders on a one-off basis, with no consideration of market dynamics; and (iii) focused on short-term objectives, rather than being crucial aspects of a project cycle that contribute to the achievement of organizational goals, project objectives, and overall development outcomes (footnote 1). Several contracts in the public sector may be viewed as one-off activities, such as the construction of a road or the supply of school desks and armchairs; however, project objectives are certainly medium to long term, like the development of local markets and increased access to primary education. In this sense, whether in the private or public sector, procurement and purchasing should always be considered within the context of supplier or contractor management, which may be defined as that aspect of purchasing or procurement concerned with rationalizing the supplier [or contractor] base and selecting, coordinating, appraising the

---

performance of and developing the potential of suppliers [or contractors] and, where appropriate, building long-term collaborative relationships (footnotes 1, 7).

If public procurement is considered within this context, rather than as a one-off transaction, then the relevance of institutional capacity within an agency becomes clearer, and the decision to outsource becomes a more thoughtful and strategic process. The relevance of the procurement function should not be underestimated, even if it is not a regular undertaking in an agency, because attainment of the overall organizational goals and specific project objectives will depend heavily on the way such function is managed. Therefore, an agency would do well to weigh the benefits and costs of directly managing the procurement function, and developing its in-house capacity to handle such a responsibility. Its strategic options will also increase if the applicable legal and institutional frameworks allow it to outsource the procurement function to specialized third parties, whether private service providers or other public agencies that regularly handle such procurements.

Outsourcing is defined as “a management strategy by which major noncore functions are transferred to specialist, efficient, external providers” (footnote 1, 392). It developed as a reaction to the overdiversification during the 1970s and early 1980s that led several enterprises to review their core activities and concentrate on their core competencies (footnote 1). Within this context, some private and public organizations that have regarded procurement to be a noncore activity have actually made the strategic decision to outsource such function to specialized procurement agents. Nevertheless, although multilateral development banks and some developing member countries (DMCs) in Asia and the Pacific have been engaging the services of procurement agents to handle the procurement function, it is important to note that the actual responsibilities in most of these arrangements differ from the approach in the private sector. When a private organization decides that the purchasing activity is not among its core competencies, it may hire a specialist service contractor (i.e., a procurement agent) to take over the responsibilities for logistics and supply chain management. This means that the procurement agent will then handle the entire process of planning, implementing, and controlling the flow and storage of materials, inventories, and finished goods. A key consideration in contracting a procurement agent is its ability to tap large and diverse markets and to identify, qualify, and support suppliers. Indeed, buyers in the private sector recognize that, by forcing numerous suppliers offering similar products to compete against each other, procurement costs can be reduced significantly, and that significant expertise in the procurement process is needed to actually achieve these lower costs. This is the reason for not only the increasing trend to outsource the procurement function in the private sector but also the development of the e-market industry, where the ultimate objective is not just to reduce procurement costs but to improve supply chain processes and efficiencies.

On the other hand, when procurement outsourcing is allowed and practiced in the public sector, one may regard the role of procurement agents as less involved than those in the private sector, particularly with respect to capital expenditure projects. In fact, except in the case of centralized procurement agencies (which will be discussed later), procurement agents may simply function as tendering agents.


agencies that handle the bidding portion in the entire procurement cycle of a government project. For example, according to Tan Li, director of Project Division II of the Ministry of Railways in the PRC, national procurement agents participate as tendering agencies in the bidding activities of all foreign-assisted projects managed by the Ministry of Railways Foreign Capital and Technical Import Center. The procurement agents are supposed to ensure that the interests of the state and the public, as well as the legal rights of all participants in a bidding activity, are protected. Executing agencies and implementing agencies engage procurement agents for practically all ADB-financed projects in the PRC. The responsibilities of the procurement agents cover the drafting of the invitation for bids and the bidding documents, and the examination and evaluation of bids. For civil works contracts, the obligation of the procurement agent ends upon contract signing. For the procurement of goods, the contractual relationship between the procurement agent and the agency can end upon the delivery of the goods. In the latter case, the responsibilities of procurement agents may extend up to the provision of support in processing the formal requirements for deliveries, such as importation permits, but no further. The case of centralized procurement agencies in the public sector can be considered more similar to the centralized purchasing departments of some organizations in the private sector, because these agencies are tasked with aggregating demand across multiple end users so that benefits from economies of scale are maximized. They also tend to have more flexibility in developing supplier relationships, such as through the use of framework agreements.

In terms of regulation, while the objectives of reduced costs and increased efficiency are common to both the private and public sectors, the policy and operating environments differ in each. Quite obviously, government contracts are subject to more regulatory controls than private contracts. Also, while commercial organizations tend to look towards developing and maintaining working relationships with suppliers, capital expenditure projects (as opposed to supply requirements under the operations budget, especially those procured through centralized agencies) of public agencies may simply be addressed through one-off contracts. Public agencies may also have to deal with strict anticorruption regulations, which may in fact discourage some forms of supplier–buyer relationships that are commonplace in the private sector.

Despite these differences, the use of specialized agents in public procurement can be effective in ensuring that development outcomes are achieved. When the problems of weak institutional capacities, high costs, delays, and high integrity risks are systemic in a government—at the national or local level, or even in any given sector—outsourcing the procurement function may be a sound option to consider, whether as a short-term gap-filling measure or as a longer-term strategic approach that may include capacity development (such as a “learning by doing” methodology). Indeed, the link between procurement agents and the broader issue of development impacts in the public sector is one that deserves closer consideration, especially since public procurement can account for as much as 15%–22% of a country’s gross domestic product (GDP).5

II. Procurement Agents and Official Development Assistance

A. Using Procurement Agents in Projects Financed by Official Development Assistance

1. Roles of Procurement Agents in Projects Financed by Official Development Assistance

In the case of official development assistance (ODA) projects, inefficiencies, fiduciary concerns, weak capacities, and the need to obtain the best quality and value of goods and services are key considerations that factor into a decision to engage the services of procurement agents. Also, whenever a country is a recipient of ODA from various sources, it may be faced with having to operate under a number of different and unfamiliar procurement systems. It is in this sense that the usefulness of procurement agents has also been widely recognized, in that such agents would be knowledgeable of, and able to operate under, the procurement systems of several development partners and national laws and regulations.\(^6\) In fact, development partners may sometimes specify in the financing agreement that an internationally recognized procurement agent will have to be appointed to handle all procurement activities under the grant or loan. This tends to be the default position of some bilateral development partners, such as the United States’ Millennium Challenge Corporation (MCC) and the Department for International Development of the United Kingdom. It is in this context that procurement agents take on the role of an independent procurement agent (IPA). Although the procurement agent is contracted by the client agency, it performs its duties independently of the client and holds sole responsibility over its

functions, which normally cover (i) drafting and issuing bidding documents, and (ii) evaluating bids and recommending contract award (footnote 6).

The role of the IPA is different from the traditional role of procurement agents in the public sector, where the procurement agent forms an integral part of the client agency’s team and works in close association with it throughout all stages of the procurement process, including drafting and issuing bidding documents, evaluating bids, recommending awards and, in some cases, contract management (footnote 6). Because of the close working relationship between the procurement agent and the client agency, this approach is said to be advantageous for capacity development purposes. Appendix 1 presents case studies on the two roles of procurement agents.

While procurement agents can generally perform two types of roles, the motivations for appointing a procurement agent may be numerous. As Karen Harries, senior procurement advisor of Crown Agents, explains:

 Sometimes there is a need for a transitory function, maybe following a natural disaster, conflict or the emergence of a new country, where capacity gaps exist. Often procurement agents are regarded as [fulfilling] a purely administrative function, a necessary process that can delay implementation. Development partners may look to appoint a procurement agent as a “policeman,” notably where there are concerns about fraud and corruption. Conversely, through the devolution of responsibilities, the procurement agent is authorized to act in the name of the partner government and, therefore, this provides [it] with a degree of distance from the process.7

2. Procurement Agents in Japanese Official Development Assistance

In Japan, the Public Accounts Law (1947) and the Cabinet Order on Budget, Settlement of Accounts and Accounting Regulations (1947) provide that national government agencies, local governments, and public entities should conduct their own procurement. However, the approach is different for the ODA that Japan provides to recipient countries, where procurement agents are mainly used for grant assistance under the Ministry of Foreign Affairs (MOFA) and the Japan International Cooperation Agency. For example, in fiscal year 2010, bilateral grant assistance under the MOFA was ¥179 billion ($2.29 billion at $1 = ¥78.16), of which roughly 50% either fully or partly used an IPA. The approach of using IPAs began when the MOFA established the Japan Non-Project Grant Aid (JNPGA) scheme in 1987 to provide budgetary assistance as a way to respond to the current trend of international aid. Since there was no Japanese procurement agent at the time, the MOFA initially appointed Crown Agents and the United Nations Development Programme (later handled by the United Nations Office for Project Services), both of which had offices in Japan, as the IPAs for the JNPGA scheme. In 1989, the MOFA and the Japan International Cooperation Agency decided to establish a Japanese procurement agent, known as the Japan International Cooperation System (JICS). JICS commenced its services as an IPA for the JNPGA scheme in 1993. With the closure of the United Nations Office for Project Services office in Japan, Crown Agents and JICS are the remaining registered IPAs for the JNPGA scheme.

Traditionally, under Japanese ODA, the grant fund was kept by the Government of Japan and the recipient countries only received the assistance in the form of completed works and goods.

The role of the independent procurement agent is to conduct the procurement on behalf of the recipient government and handle fund management.

with the new scheme of providing cash to recipient governments, and the need to secure transparency in fund management, the MOFA decided to request recipient governments to recruit an IPA recommended by the Government of Japan. In Japanese ODA, the utilization of an IPA is defined in the agreed minutes attached to the exchange of notes that are signed for a particular assistance project. The role of the IPA is to conduct the procurement on behalf of the recipient government and handle fund management. This role is provided for in the guidelines for the JNPGA scheme.

The utilization of IPAs for Japanese ODA has since expanded from a single scheme for the simple supply of goods to multiple schemes with various types of procurement. The role of the IPA has also widened in that, currently, the IPA under Japanese ODA is not only responsible for the procurement activity prior to the contracting stage but also for contract management and fund disbursement on behalf of the recipient government. In such case, the contract is signed between a supplier or contractor and the IPA. The recipient government also opens a bank account for the grant and authorizes the IPA to arrange disbursement. The recipient government pays the fees of the IPA, which are covered by the grant received from the Government of Japan.

The following may be regarded as benefits arising from the utilization of IPAs for Japanese ODA:

(i) Since the introduction of the JNPGA scheme, the main purpose of the IPA has been to ensure transparent and efficient procurement activities.

(ii) Under Japanese law, the approved budget needs to be fully disbursed within the same fiscal year. With this in mind, by using an IPA, the budget can be disbursed from the Government of Japan’s account to the account of the recipient government immediately after the exchange of notes. This allows the project to be implemented with a more flexible schedule.

(iii) Based on the agreement signed between the recipient government and the IPA, the IPA is obliged to report the progress and results of the procurement. The IPA is also able to provide data to the Government of Japan whenever these are needed, even after the completion of the project. Finally, the IPA can centralize all data and information pertaining to the assistance.

3. Maximizing the Benefits of Procurement Agents in Projects Financed by Official Development Assistance

Since the benefits of using procurement agents can be swift and defined, there is a possibility that procurement agents may be seen as a “quick fix” for procurement-related risks that have been identified in any given project, with little consideration given to a more strategic approach (footnote 7). It is also not unusual for partner governments to harbor some degree of resentment, particularly if they feel that the proposed appointment of a procurement agent is being imposed upon them (footnote 7). This leads one to consider the link between the use of procurement agents and broader development outcomes, not only at the level of national strategies and policies, but also in terms of project-specific objectives. In other words, in weighing the advantages of appointing a procurement agent for an ODA project, the government and its development partners should not only consider immediate project implementation risks but should also assess how procurement agents may help achieve value for money and contribute to the overall development objectives that the project is expected to achieve. As Harries points out:

Often a quick, maybe low cost solution, is what is required; but increasingly we are seeing the role of the procurement agent being applied in more strategic
environments. As part of project preparation, development partners invest considerably in strategies that will achieve the desired project outcomes. But longer term benefits of the effective use of procurement agents are often overlooked. Project design will often consider the “Exit Strategy.” This may include a capacity building initiative or a second phase to the project. However, how procurement fits within this is not always debated further. (footnote 7)

In discussing the capacity development aspect of procurement agents, Harries stresses that the potential of procurement agents is not just limited to the implementation aspects of the project, but actually reflects the Kaizen cyclical method where experience and capacity grow as the client agency and the procurement agent move through the cycle together, where needs are monitored and reassessed, and where reforms are implemented. Soon enough, or even in parallel, the government will then look at its own procurement systems and procedures, and apply the knowledge and experience it has gained through its partnership with procurement agents. Certainly, there are benefits from formal training courses, but capacity is ingrained through mentoring, sharing of experiences, and transfer of skills (footnote 7).

In terms of helping client agencies achieve value for money, Bouwe Vlietstra, managing director of the International Procurement Agency, points out that, as professional purchasers that know the market and possess experience across a wide range of governments, procurement agents are in a unique position to support the client agency in (i) identifying opportunities to achieve economies of scale, (ii) incorporating logistical requirements related to public service delivery, and (iii) managing the overall costs for the procurement of general commodities. According to Vlietstra, these advantages may be achieved through the use of framework agreements, as these can relieve both the government and the private sector of excessive opportunity costs (footnote 8). Based on research conducted by the International Procurement Agency within the European Union (EU) regarding the cost of public procurement, Vlietstra stresses that the sum of costs for both the public and private sectors is high, and that the bulk of the costs are absorbed by the public sector. The research further featured a time–cost analysis, which showed that, when procurement procedures are efficient and both the public and private sectors are experienced with such procedures, the procuring agency will receive improved responses and better value for money (footnote 8). In fact, according to Vlietstra, the research confirmed that the investments made by the private sector to participate in public procurement opportunities ranged from 200% to more than 1,700% of the time governments spend on such procedures. This imbalance implies two things: (i) private firms are very careful in deciding whether or not to participate in a public procurement opportunity; and (ii) bidding prices tend to be higher when procurement procedures are inefficient, because the cost of tendering that is absorbed by private firms will be incorporated in their bids (footnote 8).

While Vlietstra’s argument provides a good case for combining the use of procurement agents with framework agreements, it also highlights an important element

---

8 Vlietstra, B. 2012. Use of Procurement Agents in Public Procurement (Strategic Procurement through the Use of Framework Contracts). Presentation and Briefing Note for the Regional Conference on Use of Procurement Agents in Public Procurement. Beijing, PRC. 6–7 September.

9 Under the 2011 United Nations Commission on International Trade Law’s Model Law on Public Procurement, a “framework agreement” is an agreement between the procuring entity and the selected supplier (or suppliers) or contractor (or contractors) that arises out of a procedure involving two stages: a first stage to select a supplier (or suppliers) or a contractor (or contractors) to be a party (or parties) to the framework agreement with a procuring entity, and a second stage to award a procurement contract under the framework agreement to a supplier or contractor that is a party to such framework agreement.
that was discussed earlier by Boddy (footnote 6) and Harries (footnote 7), i.e., the importance of ensuring that procurement agents support the capacity development of both the government and the private sector. When this happens, the government can develop clearer bidding documents and manage the process more efficiently, and the private sector may better understand the bidding requirements and have sufficient confidence to participate in procurement opportunities.

B. Using Procurement Agents in ADB-Financed Projects: Policy and Related Issues

The agreement establishing the Asian Development Bank (the “ADB Charter”), Chapter I, Article 1, provides as follows:

The purpose of the Bank shall be to foster economic growth and co-operation in the region of Asia and the Far East (hereinafter referred to as the ‘region’) and to contribute to the acceleration of the process of economic development of the developing member countries in the region, collectively and individually.

Chapter III, Article 8, of the ADB Charter also requires that “[T]he resources and facilities of the Bank shall be used exclusively to implement the purpose and functions set forth respectively in Articles 1 and 2 of this Agreement.”

ADB’s Procurement Guidelines were formulated in accordance with this broad policy framework and are based on the general consideration that responsibility for implementation of a project, and therefore the award and administration of contracts under that project, rests with the borrower

(i) eligibility to participate in ADB-financed contracts,
(ii) economy and efficiency,
(iii) equal opportunity to compete,
(iv) transparency, and
(v) the development of domestic contracting and manufacturing industries.

With respect to efficiency, ADB has set specific time lines to complete the procurement process, starting from advertising the invitation for bids up to signing the contract: (i) not more than 145 days for single-stage-one-envelope bidding (Figure 1), or 189 days for single-stage-two-envelope bidding. Unfortunately, these targets are not always met—most ADB DMCs have taken much more time to accomplish these two commonly used bidding processes. In fact, some executing agencies have taken more than 1 year (or even 2 years) to complete a relatively simple bidding process. In the case of more complex bidding processes—such as two-stage bidding; turnkey contracts; and bidding for plant design, supply, and install contracts—the actual time spent by executing agencies in DMCs was generally 2–3 times more than expected.10 Figure 2 shows the actual time taken by executing agencies to conduct a bidding activity, from bid opening to completion of the bid evaluation (based on statistics of contracts valued at more than $10 million in 2011). Comparing the data in figures 1 and 2, it may be noted that, while ADB expects executing agencies to complete bid evaluation in 30 days for single-stage-one-envelope activities, the executing agencies in most regions (except East Asia) actually took 42–90 days to complete bid evaluation and submit the bid evaluation report to ADB for review and approval (footnote 9).

Needless to say, substantial delays in project implementation hold up valuable financial resources that could otherwise be used for social and economic development, and procurement is often a

---

Figure 1  Target Time Taken for Single-Stage-One-Envelope International Competitive Bidding

<table>
<thead>
<tr>
<th>Procurement Activities</th>
<th>Average Time Taken for ICB Single-Stage-One Envelope Bidding Process</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Receive &amp; review bidding documents and specific notice and acknowledgment by ADB</td>
<td>Day 0</td>
</tr>
<tr>
<td>2. Receive and Comments on specific notice/IFB</td>
<td>3 Days</td>
</tr>
<tr>
<td>3. Documents sent to COSO &amp; OGC</td>
<td>1 Day</td>
</tr>
<tr>
<td>4. Comments received from COSO &amp; OGC</td>
<td>7 Days</td>
</tr>
<tr>
<td>5. ADB Approval for bidding documents</td>
<td>14 Days</td>
</tr>
<tr>
<td>6. Advertised in Local Newspaper</td>
<td>1 Day</td>
</tr>
<tr>
<td>7. Bidding documents issued</td>
<td>14 Days</td>
</tr>
<tr>
<td>8. Issuance of bid documents to bid submission date</td>
<td>100 Days</td>
</tr>
<tr>
<td>9. Bid opening/Opening date</td>
<td>90 Days</td>
</tr>
<tr>
<td>10. Bid evaluation</td>
<td>42 Days</td>
</tr>
<tr>
<td>11. ADB approval or non-concurrence</td>
<td>57 Days</td>
</tr>
<tr>
<td>12. Contract signing date</td>
<td>42 Days</td>
</tr>
</tbody>
</table>


Figure 2  Actual Average Time Taken for Bid Evaluation by Executing Agencies for Single-Stage-One-Envelope International Competitive Bidding (Works)*

<table>
<thead>
<tr>
<th>ADB Regional Departments</th>
<th>Number of Days</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia Department</td>
<td>26</td>
</tr>
<tr>
<td>Central and West Asia Department</td>
<td>90</td>
</tr>
<tr>
<td>Southeast Asia Department</td>
<td>57</td>
</tr>
<tr>
<td>Pacific Department</td>
<td>42</td>
</tr>
</tbody>
</table>

ADB = Asian Development Bank.

* The South Asia Department recorded no 2011 transaction above $10 million for Single-Stage-One-Envelope International Competitive Bidding (Works).

bottleneck in ADB projects. Procurement that is handled incompetently not only creates delays in the project cycle but also adversely affects the quality of the goods, equipment, and civil works being procured (footnote 9). In turn, these cause financial losses or even, sometimes, failure of the investment projects (footnote 9).

A closer look at Figure 2 reveals that the average time taken to evaluate bids for all contracts greater than $10 million in the East Asia region for 2011 was much less than the average time taken in all other regions (footnote 9). ADB records also show that nearly all international competitive bidding (ICB) for contracts greater than $10 million in East Asia was undertaken in the PRC (footnote 9). If one relates this to the fact that public procurement for most sectors in the PRC is done through procurement agents, then there may be some room to argue that the use of procurement agents in the PRC has resulted in shorter bidding time lines (footnote 9). In any case, it may be argued that highly competent procurement agents can help improve procurement efficiencies and outcomes, especially in executing agencies with weak capacities.

Indeed, weak capacity to handle procurement is a major reason for most of the delays in procurement. To address this issue, paragraph 3.10 of ADB’s *Procurement Guidelines* (2010, as amended from time to time) provides as follows:

> Where borrowers lack the necessary organization, resources, and experience, borrowers may wish (or be required by ADB) to employ, as their agent, a firm specializing in handling procurement. The agent shall follow all the procurement procedures provided for in the financing agreement and the Guidelines, including use of ADB Standard Bidding Documents (SBDs), review procedures, and documentation. This also applies in cases where UN [United Nations] agencies act as procurement agents.

While ADB continues to prioritize executing agency capacity development, it is important to explore other options that foster efficient project implementation within the context of each country’s specific circumstances. In this sense, selection of a qualified procurement agent through a competitive selection process and maintenance of a healthy client and service provider relationship are also important aspects that need to be considered. ADB’s *Guidelines on the Use of Consultants* recognizes two types of roles that procurement agents may have in a public procurement transaction: (i) as an agent that takes over the outsourced procurement function of an executing agency, or (ii) as an advisor that supports the executing agency in undertaking its procurement responsibilities. In particular, paragraph 2.39 of ADB’s *Guidelines on the Use of Consultants* (2010, as amended from time to time) provides as follows:

> When procurement agents are specifically used as “agents” handling the procurement of specific items and generally working from their own offices, they are usually paid a percentage of the value of the procurements handled, or a combination of such a percentage and a fixed fee. In such cases procurement agents shall be selected using Quality-and-Cost-Based-Selection (QCBS) procedures with cost being given a weight up to 50%. However, when procurement agents provide only advisory services for procurement…for a whole project in a specific office for such project they are usually paid on a time basis, and in such cases, they shall be selected following the appropriate procedures for other consulting assignments using QCBS procedures and time-based contract, specified in these Guidelines. The agent shall follow all the procurement procedures outlined in the loan agreement and in the procurement plan approved by ADB on behalf of the borrower, including the use of RFP [request
for proposals, review procedures, and documentation.

Since procurement agents are recruited and paid by the executing agencies, a question may arise on how the procurement agent can maintain its independence and objectivity in evaluating the bids, particularly when a difference in opinion arises with the executing agency. This question is particularly crucial in an environment where decision-making processes can easily be influenced by seniority in the bureaucracy, and especially where integrity risks are high (footnote 9). ADB’s Anticorruption Policy (1998, as amended to date) requires that borrowers, beneficiaries, bidders, suppliers, and contractors under ADB-financed contracts observe the highest standard of ethics during the procurement and execution of contracts. But more than this, for a procurement agent system to effectively work within the public procurement structure of a country, it is absolutely essential to establish the appropriate legal framework at the national level, along with effective agency-level mechanisms to ensure the independence and integrity of procurement agents. In this way the entire procurement agent system actually supports a competitive, fair, and transparent public procurement environment (footnote 9).
III. The Regulated Market-Based System in the People’s Republic of China

A. Legal and Institutional Frameworks

In the PRC, a procurement agent is a legal entity entrusted to undertake procurement activities on behalf of another party, with the other party still holding the legal responsibility for the procurement. There are two kinds of procurement agents in the PRC: (i) profit-oriented procurement agents, and (ii) nonprofit procurement agents. The first kind of procurement agents are called tendering agents or tendering companies in the Tendering and Bidding Law of the PRC, which took effect on 1 January 2000. Procurement agents that handle ICB contracts usually call themselves international tendering companies (or corporations). Article 13 of the PRC’s Tendering and Bidding Law defines a tendering agent as “a social intermediary organization which is set up according to law to engage in tendering business on behalf of its clients and provide related agent services.” On the other hand, Article 16 of the Government Procurement Law of the PRC, which took effect on 1 January 2003, provides specific reference to institutions for centralized government procurements (ICGPs) as procurement intermediaries, and defines these as “non-profitable institutional legal entities carrying out the procuring activities entrusted by the procuring entities.” All government procurement appearing in the centralized procurement catalogue needs to be carried out by ICGPs on behalf of the procuring entities concerned.11 Procuring agencies are defined as “state organs, institutions, and social organizations engaging in government procurements,” while government procurement is defined as “all the purchasing activities conducted by the state organs at all levels, institutions and social organizations where the intended goods, construction, and

services are those listed in the Centralized Procurement Catalogue published by the procuring authority or those whose value exceeds the respective prescribed procurement thresholds for goods, construction or services” (footnote 11, Article 15).

Prior to 1993, most procurement agents were registered as public institutions. However, the Government of the PRC subsequently implemented the policy of separating these enterprises from the government. Currently, except for ICGPs, most procurement agents in the PRC are now profit-oriented and can take the form of state-owned enterprises, stock-shared corporations, or private companies legally established under the PRC’s commercial law and registered in the local industrial and commercial administration bureau as commercial enterprises. The service fees that may be charged by procurement agents in the PRC are fixed, with predefined thresholds. Currently, the rule is that the “[S]ervice fee charged for procurement agent services shall be paid by the entity [that] invites bids, except [as] otherwise agreed by the entity, procurement agents and bidders; in such case, the agreement reached by the entity, procurement agents and bidders shall apply.”12 Although the procurement service contract is signed between the executing agency and the procurement agent, the government can allow up to 80% of the procurement agent’s fees to be paid by the successful bidders.13 In practice, the procuring agency, procurement agent, and bidders agree that the winning bidder will pay for the service fees, and this is indicated in the bidding documents.14

The procurement agent service fees that are set by the National Development and Reform Commission (NDRC) are in Table 1.

Procurement agents started operating in the PRC in 1982 to support the implementation of a $100 million World Bank loan for the University Development Project managed by the Ministry of Foreign Trade and Economic Development. Since ICB and open

Table 1  
Procurement Agent Service Fees Set by the National Development and Reform Commission (as of 2010) 

<table>
<thead>
<tr>
<th>Award Price</th>
<th>Procurement of Goods</th>
<th>Procurement of Services</th>
<th>Procurement of Works</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than CNY1 million</td>
<td>1.50</td>
<td>1.50</td>
<td>1.00</td>
</tr>
<tr>
<td>CNY1 million–CNY5 million</td>
<td>1.10</td>
<td>0.80</td>
<td>0.70</td>
</tr>
<tr>
<td>CNY5 million–CNY10 million</td>
<td>0.80</td>
<td>0.45</td>
<td>0.55</td>
</tr>
<tr>
<td>CNY10 million–CNY50 million</td>
<td>0.50</td>
<td>0.25</td>
<td>0.35</td>
</tr>
<tr>
<td>CNY50 million–CNY100 million</td>
<td>0.25</td>
<td>0.10</td>
<td>0.20</td>
</tr>
<tr>
<td>CNY100 million–CNY1 billion</td>
<td>0.05</td>
<td>0.05</td>
<td>0.05</td>
</tr>
<tr>
<td>More than CNY1 billion</td>
<td>0.01</td>
<td>0.01</td>
<td>0.01</td>
</tr>
</tbody>
</table>

CNY = Chinese yuan.

Note: The rates shown are for completed procurement agent services. If only bidding documents are prepared, the charge rate will be 30% of the listed rates.


13  This practice is not accepted by multilateral development banks for projects they finance.
bidding were required by the World Bank, and executing agencies in the PRC did not have adequate experience in these procurement methods, the government authorized a few certified PRC foreign-trading companies to act as procurement agents for the executing agencies. The few procurement agents were state-owned enterprises under the then Ministry of Finance, Trade and Economy Cooperation, which was subsequently restructured as the Ministry of Commerce (MOC) in 2008.

Prior to 2000, procurement agents were semigovernment agencies that existed to supplement the central government’s supervision and management authority. Initially, there were only 4–6 procurement agents in the PRC and so competition was very limited. However, the industry eventually grew exponentially, to the point that around 9,000 certificates have now been issued to procurement agents at the central government level (Table 2). With such a large number of procurement agents, the market is now very competitive.

According to Zhu Jianyuan, president of China Bidding, a procurement agent in the PRC generally has the following functions:

(i) Advice and consultation. Procurement agents provide professional advice to the executing agency on the relevant laws, the market, and selection of suppliers.

(ii) Coordination. Procurement agents are responsible for coordinating the transactions and relations among all the parties involved in the procurement activity, such as the executing agency, bidders, government regulatory bodies, and the general public.

(iii) Administration. Procurement agents handle all the administrative tasks involved in the public procurement activity, including importation and tax relief requirements.

To meet these functions, the job description of procurement agents normally cover the following:

(i) coordinating with the executing agency for the project requirements,

(ii) filing all necessary documents,

(iii) drafting all the bidding documents,

(iv) issuing the bidding notice,

(v) inviting and receiving bidders,

(vi) selecting the bid evaluation experts,

(vii) organizing the bid opening,

(viii) organizing the bid assessment and evaluation,

(ix) recommending the winning bidder,

(x) announcing the winning bidder and informing all losing bidders of the results, and

(xi) all related logistical work.

(footnote 15)

### Table 2  Certified Procurement Agents in the People’s Republic of China, 2010

<table>
<thead>
<tr>
<th>Procurement Agent Certification at the Central Government Level</th>
<th>Grade A</th>
<th>Grade B</th>
<th>Grade C</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ministry of Commerce</td>
<td>105</td>
<td>26</td>
<td>77</td>
<td>208</td>
</tr>
<tr>
<td>National Development and Reform Commission</td>
<td>115</td>
<td>314</td>
<td>113</td>
<td>542</td>
</tr>
<tr>
<td>Ministry of Housing and Urban-Rural Development</td>
<td>1,195</td>
<td>2,500</td>
<td>2,000</td>
<td>5,695</td>
</tr>
<tr>
<td>Ministry of Finance</td>
<td>643</td>
<td>2,000</td>
<td></td>
<td>2,643</td>
</tr>
<tr>
<td><strong>V. Total</strong></td>
<td>2,058</td>
<td>4,840</td>
<td>2,190</td>
<td>9,088</td>
</tr>
</tbody>
</table>

Note: Some large-scale procurement agents can have more than one certification.


On the other hand, the procurement agent is generally not responsible for the following:

(i) preproject research,
(ii) feasibility studies,
(iii) design,
(iv) bid confirmation and decision making,
(v) contract signing,
(vi) project supervision and management, and
(vii) contract performance and acceptance of work. (footnote 15)

As an independent service agency, a procurement agent is not a subordinate of the public agency, nor can it provide consultancy services to the bidders. Nevertheless, a procurement agency is answerable to various parties: (i) the administrative departments under the PRC’s State Council and the local government concerned, which exercise administrative supervision over procurement agents under Article 14 of the Tendering and Bidding Law; (ii) the PRC’s judicial organs, which handle and resolve related cases submitted to them (this is called judicial supervision); (iii) the employer and the bidders who participate in the bidding activities; and (iv) the general public (i.e., society at large and the media).16 Relatedly, the NDRC established the China Tendering and Bidding Association (CTBA) on 10 September 2005 as a self-regulating body for the procurement agent industry. The CTBA is a nonprofit social organization, membership of which is voluntary. It charges the following annual fees: CNY3,000 for ordinary membership, CNY5,000 for membership in the CTBA council, and CNY8,000 for standing membership in the CTBA council. It has a varied membership, including procurement agents (which comprise 60% of the membership), state-owned enterprises, and contractors. The following are some of its achievements: (i) in May 2010, it drafted the “procurement agent sector operations specifications” to standardize procurement agent operations; (ii) in 2009, it launched an “honesty and optimum activity,” where it started to evaluate the performance of procurement agents; and (iii) in 2006, it called for procurement agents and members to sign honesty and self-restriction commitment letters to fight fraud and corruption, which, by 3 September 2008, had been signed by 804 firms.17

B. Accreditation of Procurement Agents in the People’s Republic of China

The procurement agent system in the PRC features strong government administration and supervision, and this may be viewed within the context that the PRC used to have a planned economy where government played a significant role in controlling the market. The government controls the marketplace through the accreditation process, whereby qualification certificates serve as entry requirements for a procurement agent to actively participate. Five procurement agent certifications are currently issued by different ministries:

(i) The MOC certifies procurement agents for ICB procurement of mechanical and electrical products. This is the oldest type of procurement agent certification in the PRC, and has existed since 1984.
(ii) The NDRC certifies procurement agents for central government investment projects.
(iii) The Ministry of Housing and Urban-Rural Development certifies procurement agents for the procurement of civil works.
(iv) The Ministry of Finance certifies procurement agents for government procurement.

17 For more information, visit http://www.ctba.gov.cn
The Ministry of Industry and Information Technology certifies procurement agents for construction of communication projects.

Table 2 shows the number of procurement agent certifications issued by the MOC, NDRF, Ministry of Housing and Urban-Rural Development, and Ministry of Finance as of 2010.

Procurement agent certification is considered essential in the PRC for the following reasons:18

(i) It safeguards the publicity, equality, and impartiality of the tendered projects. Since the procurement agent is carrying out a legal and regulated act that results in a binding contract with the government and links the government and the market, it needs to conform to professional norms that are supposed to be embodied in the certification process.

(ii) It ensures the ability of procurement agents to provide professional services. Government projects such as railways, communications, power, oil, urban construction, health, and environmental protection significantly affect public safety, security, and national interests. Therefore, procurement agents need to have the required expertise and knowledge to provide services that meet reasonable high standards.

(iii) It ensures the professional capacity of the procurement agent’s team of experts. For a procurement agent to deliver successful results, it needs a multidisciplinary team of experts who have adequate experience and knowledge in the legal, technological, economic, and management aspects of the project, as well as foreign language competency.

(iv) It strengthens executive supervision. The accreditation of procurement agents helps control the size of the market, strengthens management capacity, improves service levels, and enables timely suspension of disqualified procurement agents.

To meet these objectives, the procurement agent certification system looks at the legal and financial status of procurement agents. It also considers the office sites, working conditions, organizational structure, and international management system of a procurement agent, as well as its pool of experts. Compliance with criminal and other laws is also checked. Certification for central government investment projects is divided into three levels: (i) class A, which allows procurement agents to engage in all central government investment projects; (ii) class B, which allows procurement agents to engage in central government investment projects with a value of up to CNY500 million; and (iii) class B-2 (temporary), which allows procurement agents to engage in central government investment projects with a value of up to CNY200 million (footnote 18).

C. Analysis: Advantages and Challenges of the People’s Republic of China Model

Through performance of their services, the following advantages of procurement agents have been reported in the PRC:

(i) Procurement agents minimize information asymmetry. In an arena where suppliers and contractors normally possess more information than executing agencies and thus have significant advantage over such agencies, procurement agents can provide the necessary leverage for executing agencies through their expertise, knowledge of the

The Regulated Market-Based System in the People's Republic of China

rules, familiarity with the process, integrated information channels, and in-depth knowledge of the markets. By the nature of their business, effective procurement agents should have accumulated valuable information about the national and international markets and actual prices of equipment and materials, and should be familiar with developing trends in the industry and related technologies. By maintaining a balance in the acquisition of information, procurement agents help to avoid disruptive price distortions.

(ii) Procurement agents reduce legal risks. The rights and responsibilities of both the buyer and supplier in a public procurement activity are heavily regulated by PRC law, and strict penalties apply to any infringement. This increases the relevance of procurement agents in the PRC, because experienced procurement agents will be familiar with the relevant laws and regulations and can safely ensure that the procurement activity will comply with all the legal requirements. It should be noted that the procurement agent not only safeguards the rights and interests of the executing agency but also those of the bidders by ensuring that the procurement is conducted fairly and justly.

(iii) Procurement agents provide professionalism. The bidding system is being widely used in all areas of the PRC’s national economy, whether for nationally or internationally financed projects, and different projects involve different types of requirements, specifications, capital sources, trade practices, and procedures. With their accumulated experience, procurement agents provide specialized knowledge and expertise that will help executing agencies navigate through these numerous variables. In fact, with the development of the industry, procurement agents have begun to focus on improving their service levels. For example, some companies have already passed the requirements under the ISO9001 quality management system, which provides more assurance on service delivery, and have further standardized procedures and developed institutional capacities.

(iv) Procurement agents contribute to advancement of new approaches and international practices. Since procurement agents continuously deal with projects financed by development partners, they are exposed to international good practices and innovations in public procurement. In turn, in the course of their work and through capacity development programs, procurement agents transfer the knowledge and experience they gain to their executing agency counterparts. (footnote 16)

There is no question that the market for procurement agents in the PRC is huge. As pointed out earlier, the procurement agent industry in the PRC grew substantially in the 1990s, and, by 2000, this had transformed the market from a monopolistic environment where only a handful of procurement agents controlled the supply side, to a highly competitive environment.

---

Outsourcing Procurement in the Public Sector

maintain the annual growth momentum of the country's tendering and procurement market (footnote 19). It was also reported that the CTBA estimated the national tender value passing through procurement agents was CNY13.9 trillion ($2.2 trillion) in 2009, which translates to 62% of the total amount of fixed investment assets indicated above for the same year (footnote 14).

Paradoxically, despite these figures, it appears that the procurement agent industry in the PRC has generally been reporting low profit margins in recent years. For example, the statistical data of the Ministry of Housing and Urban-Rural Development show that the annual business revenue of project procurement agents for 2010 was CNY127 billion ($20 billion), but that total operating costs were CNY109 billion ($17 billion), total liabilities were CNY506 billion ($80 billion), and total gross profit was only CNY15 billion ($2 billion), or 11% of annual business revenue (footnote 14). According to a representative from a PRC tendering agency (Guoxin Tendering Group), the general calculation rule of the national industry would show that, if the gross profit rate is below 30%, then the net profit rate can be expected to be below 7% (footnote 14). The same representative blamed this on vicious competition and the low agency fees imposed by the government.

Yong Zhao from the Institute of Public Market and Government Procurement at the University of International Relations in the PRC supports this view. According to him, when the Tendering and Bidding Law opened the doors of the procurement agent industry in 2000, and with the increase in the number of procurement agent accreditation departments and the reduction of entry barriers, the market entered into a growth period and expanded rapidly.20 Certainly this initially broke the high degree of market concentration among the few procurement agents that controlled the supply side for more than a decade since the 1980s,21 but with the floodgates open, companies poured into the local industry faster than the growth of market demand. Moreover, while during the early years of limited competition the service fees of procurement agents were determined through negotiation, this practice was gradually replaced by a competitive selection process in the 1990s. This caused fees to fall further to extremely low levels which were sometimes hardly sufficient to cover basic services. On the other hand, as government agencies continued to develop their knowledge and capacity to handle procurement, some of them have actually begun to handle this function themselves, an alternative that is still allowed by Article 12 of the Tendering and Bidding Law. These, coupled with the fact that service fees are capped by the government, appear to be major reasons for the declining profit margins of national procurement agents in the PRC.

While procurement agents are legally defined as “social intermediaries,” and may be viewed in the PRC as organizations that should not pursue individual gain at the cost of national or social interests (footnote 18), some consideration also needs to be given to the fact that markets need conducive environments to develop in a robust manner. As noted by the eminent economist and former World Bank senior vice-president Joseph Stiglitz, “[W]hile markets are at the center of any successful economy, government has to create a climate that allows...
business to thrive and create jobs." 22 Indeed, Li Xiaolin, deputy secretary-general of the CTBA, expressed the need to establish the appropriate legal and external conditions to allow the industry to maximize its full potential. According to him, “[T]he tendering agent[s] have been deprived of the awareness and motivation to improve their service levels…Meanwhile, the [supervising] institute[s] and tenderer[s] [misunderstand and are] disappointed at the tendering agent. In this context, such practices as [the] draw[ing] [of] lots and malignant commission[s] [in] competition occur, and conflicts between [the] tendering company and agent are greatly correlated to such inappropriate positioning.” 23

Also, according to Yuan Bingyu, chief executive officer of the Guoxin Tendering Group, under the pressure of vicious competition, some procurement agents actually end up illegally charging below the standard rates, just to undercut competitors (footnote 14). The opposite is also reportedly being practiced, in that procurement agents have been resorting to illegal practices to increase their prices beyond the government ceilings. In a 2009 report published by the Chinese Academy of Social Sciences, entitled Corruption Situation and Countermeasures Research of Social Intermediary Organizations, it was mentioned that procurement agents that are facing survival pressures are often becoming agents for illegal profiteering activities. 24

While this paper will not consider the broad debate between market and regulated systems, it is worth pointing out that any government looking at the market-based approach needs to consider the benefits, costs, disadvantages, and applicability of the PRC’s model, particularly with respect to the use of accreditation and the standardization of service fees. There are always different and opposing views to consider in any situation. For example, while accreditation may curtail competition, especially when the financial and experience requirements are set too high, the PRC’s experience has shown that it was crucial in the development of the procurement agent industry in at least three ways: (i) by breaking the monopoly of the few procurement agents that existed during the early years of the system and opening the doors to new players, (ii) by providing some level of quality control as the market opened and matured, and (iii) by segregating the market and allowing procurement agents to specialize in key sectors.

With respect to the service fees, even if these are generally charged to the winning bidders, the government ends up shouldering the costs because the bidders simply include these in their bid prices. Therefore, one may understand the motivation of the Government of the PRC to regulate the allowable rates. Nevertheless, it is also important to balance this concern with measures to ensure that the market operates efficiently and effectively. If the standardized rates do not accurately reflect or consider the actual costs and profit margins in the industry, then these may end up curtailing the growth, competitiveness, and professionalism of the market. In particular, since the procurement agent service fee in the PRC is simply a percentage of the awarded price, it is necessarily based on the prices of the goods to be procured or the construction of the works, rather than on reimbursable costs and remuneration rates for actual staff inputs that consider staff time and staff rates, plus overheads, social costs, tax, and profit. The bottom line is that the market should provide incentives for growth, and firms exist because some transactions internal to them are less costly than similar transactions carried out in the markets,

24 Cited by Zhao (footnote 20).
so that the limits of a firm depend on cost comparisons at these margins. As such, any effort to regulate procurement agent service fees should not impede this basic principle.

One should also not discount the advantages of a professional association to ensure effective self-regulation and continuous development of the industry. In the PRC, the CTBA is performing the role and function of the self-governing body. However, in setting up such an association, two things are worth considering: (i) whether it should be established under the auspices of a government agency, as in the case of the CTBA, or as a fully independent private sector association; and (ii) whether membership will be limited to procurement agents or if it will be open to all players in the market (i.e., procurement agents, procuring entities, and bidders). With respect to (ii), while an association comprising procurement agents, procuring entities, and bidders may provide the venue for constructive dialogue among the key players in the market, it may also create an environment that is conducive to conflicts of interest and may hinder open discussions among procurement agents for fear that sensitive information may be shared with other players.

Finally, it is also interesting to note that some procurement agents in the PRC have recently begun to broaden and diversify their activities. While most procurement agents still regard the bidding activity as a core service, some are looking at expanding into corporate and project management consulting services, contract management, and supply chain management (footnote 23). This appears to be a natural progression as the experience and capabilities of procurement agents continue to improve (footnote 20), and as competition in the traditional core functions constantly increases. Therefore, it is important to see how the PRC’s legal, regulatory, and institutional frameworks further evolve to both regulate and motivate these innovations, because these will certainly serve as future lessons for other DMCs that may adopt a market-based system.

While most procurement agents still regard the bidding activity as a core service, some are looking at expanding into corporate and project management consulting services, contract management, and supply chain management.

---

IV. The Centralized Procurement Agency Model

In the private sector, since the marketplace can be fragmented, buyers recognize the value of outsourcing the procurement function to a third-party service provider that has the ability to force many suppliers that offer similar products to compete against each other. Such an approach can significantly reduce costs, especially when the procurement function involves complex and costly processes that require specialized expertise. Several organizations in the private sector have also concentrated the purchasing function in a capable centralized department to leverage their purchasing power and achieve economies of scale. According to Lysons and Farrington, the benefits of centralized purchasing are as follows:

(i) Forecasts of the total quantities of items likely to be required by the whole organization for a specified period can be prepared.

(ii) Consolidation of quantities can form the basis for negotiating quantity discounts, rebates, or learning curve reductions.

(iii) Suppliers dealing with a centralized purchasing department have an incentive to compete for preferred-supplier status, or garner the whole or a substantial proportion of the undertaking’s requirements.

(iv) Suppliers may be able to reduce prices by spreading overhead over longer production runs.

(v) The supplier base may be reduced by the award of preferred-supplier status to one or two providers.

(vi) Centralization (a) permits the employment of purchasing professionals in a way that is not possible with diversified purchasing, (b) helps identify who can become experts in the procurement of special classes of materials or

---

products following market trends, and (c) permits the development of reliable and economic supply sources or of import and expert procedures where there is substantial global sourcing.

(vii) Centralized purchasing tends to have a greater strategic focus than divisionalized purchasing, because of proximity to major organizational decision makers.

(viii) Uniform policies can be adopted.

(ix) Competitive or “maverick” buying between functions is eliminated.

(footnote 1, 168)

In the public sector, the approaches of both outsourcing and centralization are also being practiced by some governments through the creation of a centralized procurement agency. Since such a centralized procurement agency consolidates the requirements of several public agencies across the bureaucracy, it can be regarded as performing the same function as that of a centralized purchasing department in the private sector, albeit with a much larger budget. On the other hand, although the government in a country can be regarded as one entire bureaucracy that is subject to a single administrative system, each agency at the national and local level, and every state-owned enterprise, would normally have its own budget and procurement requirements—as in the case of individual organizations in the private sector—and so the consolidation of all their requirements in a separate centralized agency could also easily fall within the concept of outsourcing to a third-party specialized provider in the private sector. In any case, the benefits of centralizing procurement in the private sector may also apply to the public sector, except that the legal framework in some jurisdictions may actually limit flexibility in some areas. For example, preferred-supplier status may run counter to strict requirements in the procurement laws of some countries (nevertheless, this may be similar to the approach of using framework agreements, if so provided in the legal framework).

A. Case Studies

The following case studies show how governments have been able to achieve substantial savings in their overall procurement budgets by establishing centralized procurement agencies and consolidating procurement requirements.

1. Consip and Bulk Purchasing in Italy

The story behind the establishment of Consip in Italy presents an interesting case of how a government successfully shifted from a decentralized approach with more than 50,000 purchasing agents in the public sector to a centralized agency model for widely used goods and services. Consip is a stock company that is entirely owned by the Ministry of the Economy and Finance and, since it operates with exclusive public resources, its activities are subject to the control of the Court of Audits. It was created in 1997 in what was then the Ministry of the Treasury, Budget and Economic Planning, and was originally entrusted with the information technology activities of the state administration, particularly in the areas of finance and accounting (footnote 28). Three years later, Consip was entrusted with the task of implementing the Program for the Rationalization of Public Administration Purchase, and through the 2000 Budget Law and Ministerial Decree dated 24 February 2000, the Ministry of the Economy and Finance identified Consip as the agency responsible for provision of goods and services on behalf of public agencies (footnote 28).

Consip is one of the most-cited centralized procurement agency models worldwide because it was a key component of the Government of Italy’s successful program

---

28 The original name of Consip was CON.S.I.P., which was an acronym for Concessionaria Servizi Informativi Pubblici.

to reduce public expenditure for goods and services and actually helped to reduce public debt. As explained by Bandiera, Prat, and Valletti in their oft-cited paper, the rationale behind Consip is twofold: (i) since contracts, tender documents, and eventual litigation are centralized, Consip can save on transaction costs; and (ii) compared to individual procuring agencies, Consip has more buying power that can be exploited to obtain lower prices.29 This is reminiscent of the points made by Boddy, Harries, and Vlietstra on the cost benefits of using procurement agents, cited earlier. In fact, in line with Vlietstra’s argument on the benefits of using framework agreements, it is interesting to note that Consip actually procures its goods and services through such types of agreements, whereby public agencies can opt to buy the goods and services indicated in the contract at the terms and conditions provided, within a specified period.

The impact of Consip in terms of increased efficiencies in the procurement cycle becomes more apparent if it is juxtaposed with the findings of Bandiera, Prat, and Valletti that, on average, at least 82% of documented waste in Italian contracting is passive waste, which is defined as waste that does not benefit the public decision maker, such as inefficiency due to red tape (footnote 29: 1, 2, 36). They further point out that the total purchases from the Consip catalogue was €14 billion ($18 billion), or 12% of total procurement expenditures in 2005, while the value of purchases of the same products and services from other sources was €6 billion ($34 billion), or 22% of total procurement expenditure in 2005, and that public agencies that switch to Consip save 28% of the purchase price (footnote 29; 9, 10, 37). Based on their findings and analyses, plus the fact that the cost of running Consip is not high (with only around 160 employees in the procurement department), Bandiera, Prat, and Valletti conclude that agencies like Consip can produce considerable public savings. To put this into perspective, one should note that, in 2006, public spending for goods and services in Italy accounted for about 8% of GDP, or €125 billion ($162 billion), a figure that is in line with other countries in the Organisation for Economic Cooperation and Development (OECD). Of this, 40% is spent on generic goods such as desktop computers, paper, and telephones (footnote 29). Appendix 2 presents a more detailed account by Varley on Consip as a success story, as reported by Thai and Roman.

2. Republic of Korea’s Public Procurement Service

The Public Procurement Service (PPS) of the Republic of Korea was created on 17 January 1949, soon after the establishment of the Government of the Republic of Korea. At that time, it was named the Provisional Office of Foreign Supply under the Prime Minister’s Office, and was responsible for managing foreign aid supplies.30 It was then consolidated with the Office of Foreign Procurement and was renamed the Office of Foreign Supply. On 2 October 1961, it was expanded to include domestic procurement and civil works contracts and became a central procuring agency. In 1967, the PPS’s functions were further expanded to include the stabilization of supply and demand and prices for major foreign raw materials and basic necessities (footnote 30). The PPS is perhaps more known worldwide for the Korea On-line E-Procurement System (KONEPS), which it established in 2002. This system has been benchmarked by the international community, including the United Nations and the World Bank, having garnered the United Nations’ Public Service award in June 2003 for its innovations on transparency and efficiency, and having been selected by the United Nations as the Best Practice Model in terms of e-procurement in November


Outsourcing Procurement in the Public Sector

2004, among others (footnote 30). Currently, the PPS is an executive agency under the Ministry of Strategy and Finance.

According to its website, the PPS performs the following roles and responsibilities:

(i) **Domestic and foreign procurement for public institutions.** More specifically, it purchases and supplies goods worth $14 billion, which is approximately 46% of total public purchases.

(ii) **Contracts for the government’s major construction projects.** Its contract volume stands at $14 billion, which is approximately 39% of the entire public civil works spending. The PPS also reviews designs of construction projects and provides construction management services for public institutions that lack professional engineers.

(iii) **Stockpile and supply of raw materials.** The PPS stockpiles major raw materials such as aluminum, copper, lead, zinc, tin, and construction materials. It also makes them available with the short- and long-term supply and demand for goods in mind, as well as stabilization of consumer prices.

(iv) **Coordination and audit of government property matters.** The PPS manages approximately 12 million units of government property, which was $7.8 billion as of 2007. It is in charge of matters pertaining to the management of government property.

(v) **Management and operation of KONEPS.** Through KONEPS, the PPS conducts the entire procurement process, from the issuance of the invitation for bids, bidding, and contracting, to online contractor payment for public entities. (footnote 30)

All national and local government entities are required to procure all goods and services worth more than $100,000 and all civil works worth more than $3 million through the PPS. A total of 43,000 public entities and 223,000 suppliers currently use the services of the PPS.31 Procurements falling below the thresholds set for goods, services, and civil works may be procured independently by the agencies. In 2011, out of a total public procurement budget of $100 billion (10% of the Republic of Korea’s GDP), $33 billion (33% of the total public procurement budget) passed through the PPS as the centralized procurement agency (Figure 3).

In terms of capacity development, the PPS also has the Public Procurement Education Institute that offers in-class procurement training curricula for procurement officials across the public sector, manages third-party professional training programs for PPS professionals, and administers the Public Contracting Officers’ Certification program.32 The institute has trained around 900 procurement officials from the PPS, 160,000 staff from other public entities, and 300,000 suppliers.

Hee Seok Byeon, director-general of the Construction Works Bureau at the PPS, reports the following advantages and disadvantages of the centralized and decentralized approaches (Table 3). According to Byeon, the disadvantages of centralized procurement indicated in Table 3 can be mitigated if the centralized procurement agency model is complemented by an e-procurement program that (i) reduces the procurement lead time through e-processing, and (ii) provides e-ordering for commercial goods (footnote 32). With respect to (ii), it is interesting to note that KONEPS

---


Figure 3  Total Value of Public Procurement in the Republic of Korea and the Percentage of Public Procurement Service Pass-Through, 2011

- Centralized: $33 billion
- Decentralized: $67 billion


Table 3  Advantages and Disadvantage of the Centralized and Decentralized Procurement Models

<table>
<thead>
<tr>
<th>Model</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Centralized Procurement</td>
<td>• Economies of scale&lt;br&gt;• Accumulated expertise and data&lt;br&gt;• Focused monitoring for transparency and traceability&lt;br&gt;• Effective use of government procurement as economic policy tool</td>
<td>• Complex and longer procurement processes&lt;br&gt;• Limited choices for the procuring entity</td>
</tr>
<tr>
<td>Decentralized Procurement</td>
<td>• Freer choices for the procuring entity&lt;br&gt;• Shorter process time</td>
<td>• Lower professionalization&lt;br&gt;• Less standardization&lt;br&gt;• Loose monitoring, risk of moral hazard</td>
</tr>
</tbody>
</table>


Currently has 320,000 products available for e-shopping (footnote 32). Moreover, the PPS observed that efficiency and cost effectiveness in the procurement cycle are enhanced further through centralization because (i) accumulated and concentrated expertise arises from the specialized work and experiences; (ii) price transparency from the accumulated data and market surveys reduces information asymmetry between the suppliers and the public buyers; (iii) the economies of scale increase bargaining leverage; (iv) processes, forms, and specifications are standardized; and (v) reduced administrative costs arising out of the concentration of the procurement workforce (footnote 32). The PPS analyzes the procurement budget to ensure that it reflects competitive market prices before

---

33 Based on the following formula: administrative cost per contract = (labor cost + operational cost) / number of contracts.
it is reflected in the bidding and awarding of the contract. The analysis is conducted by procurement specialists through market surveys and accumulated data from past transactions. According to Byeon, in 2009, PPS price analysis reduced the procurement budget by 13.9% for goods and services, and 6.4% for civil works, and, while these are not savings in themselves, possible budget waste is prevented by screening excessive cost estimates and setting more competitive reference prices for bidding (Figure 4).

The PPS also uses a type of contracting that is similar to framework contracts, which it refers to as multiple award schedule (MAS) contracts, for frequently purchased commercial products. Once contracted by the PPS, products covered by the MAS will be available to all public agencies through e-ordering. The MAS generates savings from economies of scale, because suppliers tend to quote favorable prices in consideration of the opportunity to sell to all public agencies. The PPS reports that, in 2011, public purchases from the PPS Online Shopping Mall was $11.3 billion for 327,000 products, and that a survey conducted in the same year on six sample MAS-contracted products showed significantly lower prices (ranging from 9.1% to 31.7%) compared to the average market prices for similar products (Figure 5).

3. The Philippines’ Decentralized and Centralized Procurement Agency Systems

According to Janet Abuel, assistant secretary of the Philippines’ Department of Budget and Management (DBM), the legal framework in the Philippines allows the following types of procurement servicing for government agencies:

![Figure 4](Reduction_of_the_Procurement_Budget_in_the_Public_Procurement_Service_through_Price_Analysis.png)

**Figure 4** Reduction of the Procurement Budget in the Public Procurement Service through Price Analysis ($ million)

<table>
<thead>
<tr>
<th></th>
<th>Total Budget for PPS Conducted Procurement</th>
<th>Total Estimated Price after PPS Review</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods and Services</td>
<td>7,090</td>
<td>6,102</td>
</tr>
<tr>
<td></td>
<td></td>
<td>13.9%</td>
</tr>
<tr>
<td>Construction Works</td>
<td>12,021</td>
<td>11,250</td>
</tr>
<tr>
<td></td>
<td></td>
<td>6.4%</td>
</tr>
</tbody>
</table>

Reference year: 2011  
Unit: $ Million

PPS = Public Procurement Service.

(i) Agency-to-agency, such as when government agencies procure their commonly used supplies from the Procurement Service of DBM (PS-DBM), which is the Government of the Philippines' centralized procurement agent.

(ii) Outsourced procurement of non-commonly used goods and works through procurement agents, either through public or private agents. The former case occurs when the procurement function is transferred from the requisitioning agency that has weak capacity or that regards procurement as a noncore activity, to another public agency that specializes in the type of procurement concerned or that has extensive procurement capabilities. An example of this type of arrangement is when local governments or the Department of Education requests the Department of Public Works and Highways to conduct the procurement of their civil works contracts. As another example, the PS-DBM also conducts the public bidding activities for government agencies that prefer to outsource this function to it, and for which the PS-DBM charges a service fee amounting to 4% of the contract cost. Another government agency has also been performing a similar function as the PS-DBM (i.e., the Philippine International Trading Corporation, which competes with the PS-DBM as a procurement agent for the procurement of noncommonly used goods, and which charges a lower service fee of 2% of the contract cost). With respect to the use of private procurement agents, the implementing rules and regulations of the Philippines' public procurement law, Republic Act No. 9184, allows agencies to recruit the services of a procurement agent, and Abuel mentioned that the government will soon develop the guidelines to implement this provision. Section 53.6 of the implementing rules and regulations provides as follows:

In order to hasten project implementation, Procuring...
Entities which may not have the proficiency or capability to undertake a particular procurement, as determined by the Head of the Procuring Entity concerned, may request other GOP [Government of the Philippines] agencies to undertake such procurement for them, or at their option, recruit and hire consultants or procurement agents to assist them directly and/or train their staff in the management of the procurement function. The GPPB (Government Procurement Policy Board) shall issue guidelines to implement this provision.

(iii) Procurement management, where government agencies engage consultants to directly assist in the procurement function or train in-house staff.34

In 1975, a major procurement scam in the Philippines led to the creation of a study team composed of the heads of the Budget Commission (presently the DBM), the Department of Finance, the Commission on Audit, and the University of the Philippines, which was tasked to streamline and improve all existing procurement systems in the country. The team identified policy and procedural improvements that became the basis for a pilot on the operation of a centralized procurement system of commonly used supplies, materials, and equipment. This eventually led to establishment of the PS-DBM through Letter of Instruction No. 755, dated 18 October 1978. The PS-DBM was previously attached to the Ministry of the Budget (now the DBM) for administrative supervision purposes. Its creation was considered to be consistent with adoption of a policy that focused on procuring supplies and materials in the most economical and efficient manner by (i) purchasing directly from reliable sources in economic lot sizes, (ii) observing optimum specifications, and (iii) making prompt payments.35 With the issuance of Executive Order No. 285 on 25 July 1987, the General Services Administration, along with its Building Services and Real Property Management Office and Supply Coordination Office, was abolished, and its functions of operating a government-wide procurement system for commonly used office supplies and monitoring prices were absorbed by the PS-DBM. On 2 June 1989, Executive Order No. 359 was issued to (i) reiterate the policies expressed in Letter of Instruction No. 755 and Executive Order No. 285, (ii) prescribe the guidelines and procedures for operation of the PS-DBM, and (iii) provide for establishment of regional depots as part of the PS-DBM’s organizational structure (footnote 35).

Republic Act No. 9184, which was issued on 26 January 2003 to provide a single omnibus law on public procurement in the Philippines, reiterated the role of the PS-DBM in Letter of Instruction No. 755 and Executive Order No. 359 (1989) as the centralized procurement agency for all commonly used goods of the government. In light of the foregoing, the PS-DBM operates a government-wide procurement system from which all national government agencies, state colleges, local government units, and government corporations are required to procure their commonly used supplies, materials, and equipment.36

The PS-DBM is also studying the possibility of procuring and stocking construction materials and supplies, so that the benefits of economies of scale may also be applied to the government’s civil works contracts. The PS-DBM also conducts price monitoring and currently operates the Philippines Government E-Procurement System. This system is the Philippines’ electronic system for government procurement, which serves the following functions: (i) as a single centralized electronic portal to be

The Centralized Procurement Agency Model

used by all government agencies in the procurement of commonly used goods; and (ii) as a primary source of information on the procurement of other goods and general support services, civil works, and consulting services, including policies, regulations, issuances, and contract awards (footnote 36).

To bring its services closer to its clients, the PS-DBM currently maintains 13 regional depots and 12 regional subdepos throughout the country, which are being operated in collaboration with DBM regional offices and, in some instances, local governments. These depots are operating under a common information technology-enabled database system that was designed to speed up daily operations such as issuance of delivery receipts, preparation of price quotations, monitoring of stock availability and out-of-stock items, and issuance of official receipts (footnote 35). The PS-DBM currently outsources its long-distance forwarding requirements. According to Estanislao Granados, Jr., executive director of the PS-DBM, this generates more savings for the PS-DBM because it only costs around 3%–7% of the value of the goods (depending on the location of the delivery), which is much lower than the additional costs charged by suppliers when these services are included in their contracts. Granados observes that suppliers can charge as much as 85%–100% of the cost of goods for freight and handling (footnote 37). The PS-DBM is currently considering outsourcing more of its functions, such as distribution services within Metro Manila and warehousing. It is currently not fully using framework contracts but it maintains a few ordering agreements with a 1-year term for consumables such as ink, as well as Microsoft software products (footnote 37). Executive Order No. 359 (1989) allows the PS-DBM to charge service fees of up to 5% of the value of supplies, materials, and equipment procured and supplied. However, as mentioned earlier, it keeps a rate of 4% for the services it offers, whether as a procurement agent for noncommonly used goods or as the central supplier of commonly used goods.

A number of interesting factors provide a more or less effective system of checks and balances within the PS-DBM. First of all, Section 5 of Letter of Instruction 755 provides that the PS-DBM “shall not have any permanent employees.” This means that all 160 employees of the PS-DBM—from the drivers and stockers to the executive director—are contractual employees who are engaged for a term of 1 year, with the option for renewal every year. This also means that, even if all PS-DBM employees receive the same benefits as regular staff, it is not administratively difficult to terminate someone for cause, such as for poor performance or integrity issues. Secondly, since the prices of commonly used goods supplied by the PS-DBM are available online through its “virtual store,” these may be easily compared with market prices. Thirdly, government agencies tend to be very exacting with respect to the goods they procure through the PS-DBM, as they are themselves the end users. According to Granados, these serve as natural deterrents against integrity risks within the PS-DBM, because any indiscretion that will tend to lower the competitiveness of its prices and the quality of its goods will immediately be obvious to all its end users and the general public. Fourthly, the PS-DBM checks 2% of all deliveries, and any lot with a defective product is rejected in its entirety. Finally, the PS-DBM generally checks its estimated costs against market prices before any public bidding is conducted, to ensure that such estimates are realistic.

Although the PS-DBM has its share of complaints on the quality and availability of some of its stocks, it still manages to achieve considerable savings for the

---

37 Interview with Estanislao Granados, Jr., executive director of the PS-DBM, Government of the Philippines (11 October 2012).

38 The PS-DBM also has around 160 workers who are recruited on a “job order” basis to handle administrative requirements, mostly in the regional and subregional depots.
government. In 2011, the Philippines secretary of budget and management, Florencio Abad, reported that the Government of the Philippines is able to save around 35% of its total expenditure on common supplies through the centralized purchasing conducted by the PS-DBM. The significance of savings becomes apparent if one considers that, during 2007–2010, government procurement accounted for an average of 3.86% of GDP and 21.20% of the total government budget, which was estimated to be around P308 billion in 2011 ($7 billion).39 In an interview, Abad provided the following insights:

On average, you save 35% if you buy from our Procurement Service. And you know, right now, our turnover is about P1.5 billion. The total expenditure of government on common supplies like bond paper, pencils, ballpens and ink is about P19.5 billion [$471 million]. So, if the full P19.5 billion will [be used to] buy from Procurement Service, [and] we multiply that by 35%, [then] that’s about a little less than P6 billion [$145 million] (in savings).40

Data from the PS-DBM that compares the prices of aggregated and stocked items against retail prices support Abad’s claims. In other words, savings of around 30% can be achieved by agencies that procure their commonly used supply requirements from the PS-DBM rather than from retail shops (Figure 6). According to Granados, three factors have been contributing to the realization of such savings in the PS-DBM:

(i) **The aggregation of requirements and bulk purchasing.** By aggregating its procurement requirements, the government is

---

able to attract principal suppliers and manufacturers rather than retailers and distributors, and thus save on the commissions and profit margins that these retailers and distributors normally charge. Moreover, the volume of its requirements also encourages more competitive proposals from the private sector.

(ii) **Quick payment of suppliers.** In Section 4 of Executive Order No. 359 (1989), “[T]he agencies shall remit to the Procurement Service the funds needed to service their requirements for supplies, materials and equipment, as reflected in [the] Work and Financial Plan.” In this regard, since agencies need to transfer their budget allocations to the PS-DBM for the goods to be procured, the PS-DBM is able to release payment to suppliers within 2 weeks of receipt of the billing statement. This is quick compared to the average 45 days it takes government agencies to pay suppliers. This also lowers the cost that suppliers tend to include in their prices to account for delays in payment whenever they deal with the government.

(iii) **Principal suppliers and manufacturers offer lower prices than retailers and distributors.** Retailers and distributors can add as much as 40%–50% to the original cost of goods, whereas principal suppliers and manufacturers generally charge around 3% for profit. However, Granados observes that, since the passage of R. A. No. 9184 in 2003 and the introduction of more stringent bidding requirements, it seems that more retailers and distributors have been winning contracts, while fewer principal suppliers and manufacturers have shown interest in bidding for the commonly used requirements of the PS-DBM (footnote 37).

The World Bank’s 2003 country procurement assessment report for the Philippines recognized the importance and professionalism of the PS-DBM but, nevertheless, recommended a study to propose the needed steps towards its conversion into an independent and corporatized entity in order to ensure independence and accountability (footnote 36). The Government of the Philippines has also been considering reorganizing the PS-DBM into a corporate entity but it was only recently that serious steps were taken towards this objective. It is believed that corporatization of the PS-DBM will not only ensure its sustainability and independence from the government budget but it will also allow more flexibility in the management of its resources. Another effect will be greater security of tenure for PS-DBM employees and possible salary increases, since they will then be covered by the national labor laws and will no longer be contractual employees under the government’s administrative laws (along with its salary standardization scheme). Corporatization will also have the effect of expanding the role of the PS-DBM, because additional responsibilities will be given to the new corporate entity, such as importation, exportation, and logistics. There is also a plan for the new entity to acquire the Philippine International Trading Corporation. Figure 7 illustrates the expanded responsibilities of the new organization.
Figure 7  Planned Responsibilities for the New Procurement Service of the Department of Budget and Management Corporate Entity

- Centralized procurement agent for commonly used goods
- New Corporate PS-DBM
- Outsourced procurement (non-commonly used goods and works)
- PhilGEPS (E-Procurement)
- Logistics
- Import and Export

PS-DBM = Procurement Service of the Department of Budget and Management.
Source: Interview with Estanislao Granados, Jr., executive director of the PS-DBM, Government of the Philippines (11 October 2012).
V. Conclusion: Basic Considerations for the Future

Based on the country examples provided in this paper, it can be seen that public procurement constitutes a significant part of a country’s economy—around 8.00% of GDP (2006) and 15.00% of total public spending in Italy (2000), around 10.00% of the Republic of Korea’s GDP (2011), and around 3.86% of GDP and 21.20% of the total government budget (both figures averaged from 2007–2010) in the Philippines. The percentages in other regions can be even higher. Thai and Roman provide the following additional interesting insights on the scale of public procurement:

In all countries the sizeable share of government purchases makes governments the most significant economic actors. Within the European Union, the share of governmental procurement expenditure ranges between 10% to 15% of the gross domestic product (GDP), and as high as 30% of total public expenditure; in Latin America the share of governmental procurement can reach 20% of GDP (Morand 2003). The share of governmental procurement expenditure is about 35% of GDP in the United States, about 30% of GDP in Canada, and between 20% and 40% of GDP in Asia (Morand 2003), and about 20% of GDP in the Organisation for Economic Development and Cooperation countries (OECD 2000).

By some accounts, the procurement of sub-central governments is larger than procurement at the central level of governments by as much as three times (OECD 2000, United Nations 1997). At the state and local levels, governments spend on average up to 40% of their budgets for purchases (Kelman 2002).41

Public procurement constitutes a significant part of a country’s economy—around 8.00% of GDP (2006) and 15.00% of total public spending in Italy (2000), around 10.00% of the Republic of Korea’s GDP (2011), and around 3.86% of GDP and 21.20% of the total government budget (both figures averaged from 2007–2010) in the Philippines.

In terms of actual amounts spent on public procurement, it has been reported that around €1.5 trillion ($1.9 trillion) is spent annually in the EU, and over $500 billion is spent in the United States at the federal level alone (footnote 5). As indicated earlier, in the PRC the total volume of investments in fixed assets was a staggering $4.4 trillion in 2010. On the other hand, leakages through fraud, abuse, waste, and corruption can take out as much as 50% of a government’s procurement budget, with World Bank and Organisation for Economic Co-operation and Development (OECD) estimates at 20%–70% of spending (footnote 5). Moreover, the 2009 Global Corruption Report published by Transparency International estimates that corruption increased public purchasing costs by approximately 10%, resulting in global losses of $300 billion–$500 billion (footnote 5).

These figures provide a compelling argument for countries to explore various options to ensure that public funds are effectively utilized, value for money is achieved, and intended development outcomes are realized. As this paper shows, procurement outsourcing may be an effective option if utilized properly and thoughtfully. For example, a procurement agent may help a public agency achieve more efficient and timely procurement, and attain competitive prices if it (i) possesses specialized experience on the relevant procurement rules and procedures, (ii) has a deep understanding of the relevant sector, and (iii) knows the capacities of the national and international markets for the given sector. In turn, the increased efficiencies and lower costs that the public agency is able to achieve with the assistance of a procurement agent can lead to improved operational quality, portfolio performance, and finance mobilization.

The issue of procurement outsourcing in the public sector is one that spans at least three levels: (i) development of policies and frameworks at the national policy level, (ii) implementation at the project management and administration level, and (iii) organizational decisions at the procuring agency level. The basic considerations and options that are open to a decision maker will depend on the level at which she or he operates. However, all these levels are inevitably intertwined. For instance, the decision to outsource procurement at the project and organizational levels will depend heavily on the enabling environment that is established at the national level, in that a decision to outsource can only be implemented if the law or relevant regulation allows it and if the appropriate institutional arrangements exist. Moreover, even if the regulatory and institutional frameworks have already been established in a country, the agency needs to be able to tap an industry that is sufficiently developed, to the extent that service providers are not only able to provide the expertise required but are also adequately immersed in the relevant markets and sectors.

A. Developing the Legal, Regulatory, and Institutional Frameworks

77. For a procurement agent system to operate effectively, it is important to develop the appropriate legal and regulatory frameworks that will allow agencies to outsource the procurement function, either to the private sector or to specialized government instrumentalities. Although it was already pointed out that multilateral and bilateral development partners allow procurement outsourcing in their guidelines for projects they finance, and that some have actually indicated this as the default approach, looking beyond ODA projects, national rules and laws need to be recalibrated for the benefits to truly take hold in a country’s economy. In terms of broad strokes, several governments have actually hurdled the so-called “first generation” set of reforms in the field of public procurement through the passage of new laws, and some have taken further steps to establish procurement regulatory bodies and
e-procurement systems. Nevertheless, most legal frameworks still do not recognize the option of procurement outsourcing and the potential benefits it may provide. Moreover, even if some of these laws open the doors to varying forms of procurement agent systems, only a few jurisdictions have managed to successfully integrate such an approach into actual operations so that broader development impacts are realized.

This paper discussed four examples of national policies that cover variations of two diverse approaches—the PRC’s regulated market-based approach, the centralized models in Italy and the Republic of Korea, and a blended approach in the Philippines. But, as the PRC experience shows, the process of developing and implementing a policy is expected to be lengthy because both the public and private sectors need time to get acquainted with the system. The national government also needs room to correct mistakes and introduce adjustments to improve the model and address difficulties. As Abuel mentioned, several concerns have led the Government of the Philippines to take a slow and considered approach towards implementing the legal framework for a market-based approach, giving consideration to (i) the readiness and maturity of the market; (ii) the comfort level of the public agencies to entrust a role that they have traditionally held; (iii) fear of abuse, graft, and corruption; (iv) the national government’s level of preparation to address all policy requirements to set the stage for such an innovation; and (v) the country’s overall sense of preparedness to shift paradigms (footnote 34). Indeed, before a full roll-out can be considered, a government needs to adopt a phased approach that allows for some pilot cases and development of key supporting institutions.

The PRC’s case shows that, even when national laws have already been adjusted to allow for a market-based procurement agent system, the implementation of such a policy continues to improve after almost 2 decades. It is important to point out that numerous issues also have to be considered, such as

(i) the need to ensure that the market develops at the right pace, and that competition is neither too concentrated, which leads to monopolistic behavior, nor too crowded, which encourages vicious competition;

(ii) establishment of an accreditation system that provides quality control and allows for specialization;

(iii) creation of a professional association to ensure effective self-regulation and continuous development of the industry, and the need to determine (a) whether it should be a fully independent body or a government instrumentality, and (b) whether or not the membership should be exclusive to procurement agents; and

(iv) the question of control through the standardization of service fees.

When the Philippines issued its omnibus procurement law in 2003, it also had to specifically allow public agencies to outsource the procurement function—whether to other specialized government agencies or to the private sector—even though it already had a centralized procurement agency system in place since 1978. Nevertheless, the government acknowledged that it still needs to study the subject thoroughly and issue further guidelines to ensure that such a market-based approach functions properly.

Actual savings generated by the market-based approach may be difficult to establish because procuring agencies may not keep a comparative record of actual project costs against market prices, and it may not be easy to ascertain the accuracy or comparability of the cost estimates, especially for civil works contracts. In this sense, it is easier to establish the gains achieved in the areas of capacity development and efficiency. For example, as indicated earlier, ADB statistics on all contracts greater than $10 million for 2011 show that the average bid evaluation

Most legal frameworks still do not recognize the option of procurement outsourcing and the potential benefits it may provide.
period was much shorter in the region that used procurement agents in most procurements than in other regions, a finding that augurs well for outsourcing and capacity development.

On the other hand, it is easier to establish the savings generated by a centralized procurement agency approach. These central agencies aggregate demand for goods that are commonly or widely used (and thus easily available in the market), and they normally conduct regular market analyses for such goods. Indeed, data analyzed from Italy, the Republic of Korea, and the Philippines show that the centralized procurement agencies in these countries have consistently been reporting savings that can reach 20%–30% for selected items, when their aggregated prices are compared with market prices obtained from retail shops. Considering the experiences in these countries, it appears that the centralized procurement agency model can potentially provide substantial benefits in terms of savings and efficiency if the central agency

(i) has the authority to aggregate the requisitions for commonly used goods and services (and even works) across the government's bureaucracy, and procure these in bulk;
(ii) has the capability of conducting price analyses through market surveys;
(iii) is able to successfully apply framework contracts; and
(iv) is able to maximize its position to aggregate demand by successfully using an e-procurement system that automates the business process and increases transparency.

It appears that the Republic of Korea has been successfully meeting all these conditions, and has thus been enjoying substantial savings, not only for goods and services but also for civil works contracts. The impact of such success on the government's procurement budget is not miniscule, if one considers the potential scale that can be aggregated. Italy’s success with Consip indicates that around 22% of the total government expenditure for goods and services could be aggregated, while the Republic of Korea's Public Procurement Service reports that 33% of the government's total public procurement budget passed through it. In the Philippines, the figures reported in this paper show that the total expenditure of government on commonly used supplies can account for around 6% of the total government's procurement budget.

B. Outsourcing Procurement at the Project and Agency Levels

As with most reforms, while development of the legal and institutional frameworks for procurement outsourcing is an important task, it is just a preliminary step. The greater challenge lies in ensuring that the system is actually used effectively by public agencies. Indeed, it may not be difficult to adjust the legal framework to accommodate procurement outsourcing, but then a government needs to set this initiative into motion, develop and sustain the relevant institutions and systems, ensure that the desired objectives are obtained

(i) has the authority to aggregate the requisitions for commonly used goods and services (and even works) across the government’s bureaucracy, and procure these in bulk;
(ii) has the capability of conducting price analyses through market surveys;
(iii) is able to successfully apply framework contracts; and
(iv) is able to maximize its position to aggregate demand by successfully using an e-procurement system that automates the business process and increases transparency.

It appears that the Republic of Korea has been successfully meeting all these conditions, and has thus been enjoying substantial savings, not only for goods and services but also for civil works contracts. The impact of such success on the government's procurement budget is not miniscule, if one considers the potential scale that can be aggregated. Italy’s success with Consip indicates that around 22% of the total government expenditure for goods and services could be aggregated, while the Republic of Korea’s Public Procurement Service reports that 33% of the government's total public procurement budget passed through it. In the Philippines, the figures reported in this paper show that the total expenditure of government on commonly used supplies can account for around 6% of the total government’s procurement budget.

B. Outsourcing Procurement at the Project and Agency Levels

As with most reforms, while development of the legal and institutional frameworks for procurement outsourcing is an important task, it is just a preliminary step. The greater challenge lies in ensuring that the system is actually used effectively by public agencies. Indeed, it may not be difficult to adjust the legal framework to accommodate procurement outsourcing, but then a government needs to set this initiative into motion, develop and sustain the relevant institutions and systems, ensure that the desired objectives are obtained. These demand a thorough understanding of several issues, such as the scale of a country’s public procurement budget at both the national and local levels, the various categories of a government’s total budget for public goods and services, the capacity of both the local and international markets to meet the government’s requirements, and the appetite of both the public and private sectors for procurement agents. All of the expected benefits and potential risks of such an initiative also need to be carefully analyzed, especially in terms of transparency, competition, efficiency, and economy.

The objectives for recruiting procurement agents may vary; for example, the primary consideration for recruiting the IPA in the Cambodia case study differs from that of a public agency in the PRC that recruits a national tendering agent to handle its bidding activities. In any case,
Boddy summarized the general benefits that a client can achieve by recruiting a procurement agent, which apply whether the consideration is for a national or international procurement agent, or whether the need is for a traditional procurement agent or an IPA:

(i) **Protection.** A procurement agent acts for, and on behalf of, its clients and is responsible for representing the best interests of its clients through all stages of the procurement process. Thus, a client can be assured when using a procurement agent that it has an experienced and professional organization working on its behalf and protecting its interests.

(ii) **Efficiency.** A procurement agent can assure greater efficiency through established procurement systems, resources, and expertise. Also, when a procurement agent is appointed to act as a centralized procurement unit for a number of procuring agencies, there can be significant efficiency savings through economies of scale. A procurement agent also provides a central point of contact and a one-stop shop that covers the complete procurement and supply chain process.

(iii) **Probity.** The use of a procurement agent can give an assurance to government, development partners, suppliers, and contractors that the procurement processes are transparent and free from corruption, and can ensure that activities are undertaken in full consideration of applicable laws, rules, and regulations.

(iv) **Value for money.** A procurement agent can maximize value for money for a client, in that the procurement agent can secure a more favorable response from the global supply community because of its position in the marketplace, and can thus keep transaction costs down through the use of well-established systems and procedures. Of course, savings can be direct or indirect. Examples of indirect savings include those garnered through more efficient delivery times or those achieved through improved specifications that encourage better responses from the market.

(v) **Augmented procurement capacity.** There are many reasons why an organization may have limited procurement capacity. For example, (a) in a new operation or project, there may be weak procurement capacity in the start-up phase; (b) an organization may take over responsibility of a new major project, but does not have the necessary in-house procurement resources to handle the increased workload; or (c) the nature of the business activity leads to peaks and troughs of workload. In such circumstances, a procurement agent can provide essential support at crucial times. Also, a procurement agent can provide a client with access to professional procurement resources and expertise that it might not have within its own organization.

(vi) **Procurement capacity development.** While working for, and on behalf of, a client, a procurement agent can also fulfill a valuable capacity development role. The procurement agent is often in an ideal position to work alongside a client’s own procurement staff, providing on-the-job procurement training and capacity development.

(footnote 6)

Attainment of these benefits will not only depend heavily on the experience of the procurement agent and its capacity to access the relevant markets, but also on its reputation for transparency, fairness, and integrity. Based on the conclusions arising from the Cambodian IPA case study and Vlietstra’s analysis, discussed earlier, the costs for participating in public bidding and the overall reputation of a public agency are sufficient to make the private
sector wary of participating in a public bidding exercise. Therefore, a procurement agent that is able to lend its positive reputation to a procurement activity will go a long way in attracting and motivating potential bidders, and in increasing genuine competition. This is important because value for money will depend largely on the quality of competition generated by a public bidding exercise. In a similar manner, and especially for ODA projects, a renowned international procurement agent can be effective in attracting foreign bidders to participate in a major ICB contract because it can bolster the confidence of the international market.

Savings generated through a successful procurement exercise, whether with an experienced government agency or a procurement agent, will increase the impact of ODA projects. For example, data over the last decade from the National Audit Office of the United Kingdom show wide differences between the highest and lowest prices for the same goods purchased by 121 public agencies (Table 4). While some of these price differences may be justified by variances in the quality, location, and size of the purchases (which may, by themselves, make such goods likely candidates for aggregation), waste and inefficiency due to lack of capacity are also likely culprits.

<table>
<thead>
<tr>
<th>Item</th>
<th>Price Range (£)</th>
<th>Variation (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Toner cartridge (per cartridge)</td>
<td>41.00–89.00</td>
<td>117</td>
</tr>
<tr>
<td>Electricity (day rate kWh)</td>
<td>0.05–0.08</td>
<td>73</td>
</tr>
<tr>
<td>Box of 5x500 sheet A4 paper (80 gsm)</td>
<td>6.95–14.95</td>
<td>115</td>
</tr>
<tr>
<td>Post-it notes (pack of 12)</td>
<td>4.41–10.55</td>
<td>139</td>
</tr>
</tbody>
</table>

gsm = grams per square meter, kWh = kilowatt-hour.

Source: National Audit Office, United Kingdom.

In addition to the potential of procurement agents to generate savings for their clients, capacity development has constantly been appearing in the cases cited in this paper as another important benefit to consider. As pointed out by Bandiera, Prat, and Valletti, passive waste in the delivery of public services can derive from a variety of sources, one of which is that public officials simply do not possess the skills to minimize costs (footnote 29).

Capacity development may not be critical to agencies that do not have procurement as a core function, as the entire procurement responsibility can simply be outsourced. However, when project administration, management, and implementation are key aspects of an agency’s mandate—such as in civil works.
agencies—then the perennial lack of capacity may have serious consequences for the costs, efficiencies, and quality of projects and service deliveries. In the case of service delivery, while full and continuous outsourcing of the procurement function may not be advisable, it may be considered as an interim measure to help develop in-house capacity.

Regardless of all the advantages presented, the decision to outsource the procurement function ultimately resides with the public agency handling the procurement. As such, it needs to carefully consider the benefits and challenges of outsourcing, weigh these against its own internal strengths and weakness, and consider all external opportunities and threats that may bear upon its project. For example, an agency needs to look at the capacity of its staff in terms of experience and availability to undertake the tasks involved, records management resources, internal control measures and integrity issues, documentary resources, knowledge of the market, and access to information, as well as the level of interest of suppliers or contractors, the competitiveness of the industry, and prevailing conditions in the market to ensure that adequate competition exists in a level playing field. These considerations broadly fall within the basic process for strategic organizational make-or-buy decisions, which can be adapted to the public procurement environment (Figure 8).

Unless otherwise stated, a public agency will only seriously consider procurement outsourcing in light of its own needs, depending on how well it appreciates any potential benefit to be had. Eventually, even if the law requires all public agencies to adopt a procurement agent system (whether market-based or centralized), implementation will remain sketchy, at best, if these agencies do not buy into the system well enough to shift practices. Consider, for example, that the Government of the Philippines’ PS-DBM continually strives to improve its competitiveness and service standards, despite the clear legal provisions mandating a centralized procurement system. With this in mind, if a government seriously intends to pursue procurement outsourcing, it needs to ensure that any policy it adopts is not only compatible with its country’s political, cultural, and operating environments but is also practical and suitable to its national and local agencies.

If a government seriously intends to pursue procurement outsourcing, it needs to ensure that any policy it adopts is not only compatible with its country’s political, cultural, and operating environments but is also practical and suitable to its national and local agencies.

---

Figure 8 Decision Process for Make or Buy, Adapted to Public Procurement

Is procurement a core business of the agency?

Yes | No
---|---
In-house | In-house v. Outsource

Does the agency have the capacity to manage procurement?

Yes | No
---|---
In-house | In-house v. Outsource

Can the agency garner adequate competition?

Yes | No
---|---
In-house | In-house v. Outsource

Appendix 1

Case Studies on the Two Roles of Procurement Agents

A. The Ghana Example—A Traditional Procurement Agent’s Role

Charles Kendall and Partners (CKP) was appointed to act as a traditional procurement agent in 2006 for the Millennium Challenge Corporation (MCC) program in Ghana. This program was completed in 2012. Over the course of the program, goods, works, and services worth more than $500 million were procured on behalf of the Government of Ghana.

1. Challenges

   (i) Timing of appointment of the procurement agent. The procurement agent was appointed before the body responsible for managing the implementation of the MCC program in Ghana was established.

   (ii) Standard bidding documents. There were no standard bidding documents available and the procurement agent had to prepare these documents for initial procurement.

   (iii) Procurement planning. There was no effective procurement planning in the initial stages and the procurement agent had to work closely with the procuring entities to prepare initial procurement plans.

   (iv) Contract management. The client had little experience with contract management, and the procurement agent had to prepare suitable guidance and systems (i.e., a contract administrative system and a contract administration manual).

2. Successes

   (i) Compliance. Using the procurement agent ensured compliance with MCC procurement rules and procedures.

   (ii) Efficiency and value for money. More than 800 procurements valued at more than $500 million were managed effectively and efficiently through to successful completion.

   (iii) Capacity development. The procurement agent was able to transfer skills and knowledge to the client’s procurement department throughout implementation.

   (iv) Market development. The procurement agent was able to assist in the development of local and international supply markets by encouraging potential suppliers to respond to invitations to bid.

B. The Cambodia Example: Use of an Independent Procurement Agent

In 2009, CKP was appointed by the Ministry of Economy and Finance in Cambodia to act as an independent procurement agent (IPA) to undertake procurement of goods, works, and services for selected programs funded by the World Bank.
1. Challenges

(i) Change and the introduction of an independent procurement agent. Change is always difficult to manage, whatever the situation, and even more so when there is a system in place that most people in the country are satisfied with. There will be suspicion, resistance, and even hindrances. This has to be addressed quickly and diplomatically by building trust and creating a good relationship with all the stakeholders concerned, showing all parties the IPA's actual role, as well as the advantages of the new system. The IPA must establish a good working relationship with the client's procurement staff. The IPA has to convince its counterpart that it (the IPA) should not be viewed as an unwelcome imposition, but rather as a positive contribution and an initial step towards enhancement of the counterpart's capacity and responsibilities. The counterparts must sign up to the new system.

(ii) Bidder reluctance to participate. Three main reasons for bidder reluctance to participate in invitations to bid are as follows:

(a) **Historic.** Some bidders traditionally only work with certain procuring entities, and so the bidders’ perception is that, regardless of the merits of their bid, the contract award will only go to traditional suppliers and contractors.

(b) **Unnecessary complication.** Some bidders find the bidding documents of development partners too complicated and the qualifying requirements too demanding. Several bidders have placed weeks of work into a bid, only to be rejected at the preliminary examination stage because one form was not submitted in exactly the manner stipulated in the bidding documents. In contrast, the private sector offers plenty of other work that is easier to secure.

(c) **Suspicion.** The IPA is an unknown variable and people may tend to question its role and objectives.

(iii) **Bidder ignorance of bid requirements.** The bidding documents of development partners are complex in the eyes of laypersons. In countries such as Cambodia, for example, the market is relatively young, inexperienced, and limited in size. Nevertheless, although bidders are having difficulty understanding and interpreting complex bid requirements in a second language, the market has the capacity to construct roads and rural buildings. Pre-bid meetings and workshops have been used to mitigate this situation, and these have led to substantial improvements in submissions.

(iv) **Technical evaluation of bids.** When the technical specifications are complicated—such as those for complex information technology requirements, sophisticated medical equipment, and power generation equipment—specialist expertise will be needed during evaluation of bids. This is not an insurmountable challenge to the IPA but it poses cost and logistical challenges because the expertise has to be brought in for that particular procurement exercise.

(v) **Variation in the capacity of client procuring entities.** In any large organization, some departments will not be as proficient as others. Government is no different, especially when one is dealing with more than 20 different projects under various ministries. This disparity in experience, knowledge, and capacity affects the IPA in terms of timeliness, accuracy of estimates, and the adequacy of technical specifications. It can also cause delays and, in the extreme, rebiddings.

2. Successes

(i) **Greater procurement efficiency in terms of first-time no-objection letters.** Using an IPA improves the multilateral development bank approval rate of submissions dramatically, especially when there is a large number of disparate entities with
mixed abilities and capacities. Over time, the IPA gets to know the development partner, and vice versa, and a professional relationship is established. Needless to say, it is much more efficient to have one relationship than manage more than 20 relationships. The one-stop shop approach and the high approval rate have proven to be a success in Cambodia.

(ii) **Increased confidence of the development partner.** A more confident development partner leads to a better and more trusting development partner–project–IPA relationship. This leads to more cooperation, easier management, and a more efficient work flow.

(iii) **Quicker procurement cycles and increased disbursements.** The number of contracts issued and the level of disbursement have both reportedly increased in Cambodia during the tenure of CKP in Cambodia.

(iv) **Increased market participation and expertise in bids, leading to greater competition.** The lack of bidder participation is still a concern to a certain extent, but it is reportedly turning out to be a success story. At the beginning of CKP’s tenure in Cambodia, the bidders were reluctant to participate, especially for client procuring entities with which they had no previous track record. However, the situation continues to improve by word of mouth, evidence of contract awards to nontraditional contractors and suppliers, confidence building during pre-bid meetings, and the general dissemination of the new order of things. Not only are more bidders participating but their expertise in addressing the documentary requirements of the bidding documents has also radically improved.

Appendix 2
The Success Story of Consip, Italy

Italy's procurement program was born in 2000 as one of the myriad new belt-tightening programs intended to make good on Italy's promise to bring down public spending, reduce the public debt, and prove the critics wrong. By contrast to the country's big public finance controversies—e.g., its high tax rate, generous labor policies, and rapidly ballooning public pension system—the procurement program was a low-profile initiative adopted by the Government of Italy relatively quietly.

The Italian public sector's spending on goods and services, at all levels of government, accounted for about 15% of total public spending, or €85.7 billion in 2000. But in recent years, procurement spending has been increasing annually 5%–10% faster than the overall budget. This made it a problem area of the budget, but one that, analysts argued, had high potential for savings.

Under the Italian system, nearly all government revenue was collected centrally. Spending decisions, however, were widely dispersed among the central government ministries, the 21 regional governments, the 109 provincial governments, and the 8,101 municipalities, and purchasing decisions even more so. There were some 50,000 purchasing agents in the Italian public sector altogether, which meant tens of thousands of negotiations took place across the country for goods and services ranging from printer paper to telecommunications.

But suppose, government analysts suggested, that procurement of these widely used items were consolidated into huge national contracts. The central government could issue a single public tender for each good or service, award a winner, and set up a national frame contract, accessible to public agencies across the country. The chance to win such a major contract and the corresponding fear of losing it to a competitor would lead suppliers to offer significant price concessions, analysts believed. Eventually, about 40% of goods and services spending (€34.3 billion) could be aggregated in this manner, they calculated, perhaps generating billions of euros in savings. Best of all, the strategy did not require such unpopular actions as cutting back public services, pensions or other entitlements, or government jobs.

Public procurement also posed a great opportunity for process savings. Italy's 2000 Budget Law gave the Ministry of Economy and Finance responsibility for developing and managing it. The ministry immediately delegated this responsibility to a quasi-public entity called Consip. Consip had been created in 1997 as a private company, but one wholly owned by the ministry itself. As such, the ministry set its agenda but Consip was freed from many public sector constraints, especially with respect to hiring, and was thus able to hire ambitious young professionals with training and background well targeted to the needs of the company's projects. Initially created to handle the ministry’s in-house information technology needs, Consip was already a locus of technology expertise.

Over the next few years, the procurement program staff would increase to 170, but in the beginning Consip hired a small group, recruited primarily from large corporations, and set them the task of getting the program off the ground. This group identified the first experimental set of goods and services to put out for bid, choosing items they
believed especially well suited for standardization, such as telecommunications service, heating oil, photocopiers, and laptop computers. Once a good or service had been chosen, they developed a process for deciding what set of specifications would best serve the greatest number of agencies for the lowest cost. And they came up with ways to forecast public sector demand for the item so they could decide what volume to put out for bid, and how long the contract should remain in force. Once Consip had awarded a contract, the company monitored its successes and failures. When the contract expired, Consip put the item out for rebid, adjusting the new public tender to reflect the information learned in the previous round.

Consip’s public tender process allowed for virtually no discretion in selecting the winning bid. Suppliers had to be large enough to provide the volume set out in the public tender. Beyond that, the winner was decided by an impartial scoring system. In a reverse auction, the low bid won. In a most economically advantageous auction, price, technical characteristics, and service were weighed by an established formula. While the winning supplier would not be guaranteed a minimum sales volume, it would be able to count on a captive market. The 2000 Italian Budget Law required all central ministries and agencies to buy through Consip’s national frame contract.

For local and regional governments; national health service agencies, clinics, and hospitals; and universities, the use of the national frame contracts were optional. But if they opted not to use the contracts, they were required to use its quality–price ratio as a benchmark in their own competitive tenders.

In June 2000, Consip issued its first public tender, requesting bids for a huge contract for basic telecommunications landline service. No one was sure what kind of price drop to expect; this was uncharted territory. Although Italy had moved from a monopoly to a free market in telecommunications service in the previous few years, public agencies were uniformly buying service from the former monopoly provider, Telecom Italia. Fearful of losing the tender to an efficient upstart, Telecom Italia submitted a bid 58% below its own market rate. Consip was elated, the ministry was elated, Parliament was elated—the procurement program was off to a sensational start. Consip set up its first national frame contract for landline service in 2001.

Between 2001 and 2003, Consip concluded 61 national frame contracts. The amount of the price drop obtained for any particular good or service depended, first and foremost, on the actual profit margin in the industry. Thus, in 2001, mobile phone costs dropped 75%, laptop computers 35%, and photocopiers 32%. By contrast, the drop in fuel cost was only 10%, and for meal coupons 9%. The most dramatic price drops were expected to occur in the first one or two contract cycles. After that, with profit margins tightened, prices would necessarily even out. Overall, prices dropped 32.5% in 2001, 27.2% in 2002, and 21.3% in 2003.

Outsourcing Procurement in the Public Sector

This publication explores the option of outsourcing the procurement function to specialized agencies. Through selected case studies, it discusses the various benefits and issues surrounding two major approaches, namely a market-based system and a centralized procurement agency model. In analyzing these approaches, the report also looks at the broader issue of linkage with development impacts, particularly on the potential of procurement agents to improve project outcomes and overall development effectiveness. Finally, it discusses some basic considerations in successfully developing and implementing the legal, regulatory, and institutional frameworks for a procurement agent system.

About the Asian Development Bank

ADB’s vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region’s many successes, it remains home to two-thirds of the world’s poor: 1.7 billion people who live on less than $2 a day, with 828 million struggling on less than $1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.