

PUBLIC PROCUREMENT – EFFECTS OF INTEGRATION OF POLITICAL GOALS

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Abstract

There is a tendency to include more and more political goals in European and national jurisdiction for public procurement. The consequences for the goal of getting the best value for taxpayers' money of these actions are seldom presented. This research is an attempt to systematize and present reasons for including political goals in public procurement as well as for the outcomes and consequences for both the buyers and suppliers.

Even though the inclusion of political goals can be described as an effort to achieve a better society, it can easily create new risks, uncertainties and problems like conflict of interest between different political goals. In general, the procurement process becomes more complicated, which by itself tends to increase various costs like monitoring the adherence to the political goals. Further it may reduce competition since fewer suppliers are able or willing to take part in the public procurement.

Keywords:

Public procurement, Value for Money, political goals integrated in public procurement

BACKGROUND

Public procurement includes purchasing, hiring, leasing and any contractual means of engaging suppliers in the provisions of public services. Public procurement has great importance for the economy of any country. For the European Union, it accounts *for almost one-third of government expenditure. In 2009, it amounted to 19.4% of GDP – or 2.2 trillion EURO – of all the income generated in the EU* (European Commission, 2010). Being such a big part of any country's economy and within the public administration's sphere of power, it is natural to use the

opportunities that public procurement presents not only to get the best deal for taxpayers' money in each specific procurement but also as a vehicle to attain more long terms political goals.

One example of how to motivate the use of public procurement for better environment is that... *If all public authorities across the EU demanded green electricity, this would save the equivalent of 60 million tonnes of CO₂, Which is equivalent to 18% of the EU's greenhouse gas reduction commitment under the Kyoto Protocol.* (Kahlenborn et al., 2011)

Another example of the motivation for strategic use of public procurement is its influence on the market. Public agencies buy goods and/or services from virtually every sector of the economy. Public procurement can have a great impact on the whole economy when the public sector acts as an *intelligent purchaser* (Aho et al, 2006).

The EU directives on public procurement, hence, also the national procurement laws among EU member states implementing these directives, are based on the Treaty of Rome and its political goal to establish the common European market. The main principles of the Treaty transformed into the public procurement directives for the EU states are:

1. To increase transparency of procurement procedures and practices throughout the community
2. To allow the free movement of goods, services, capital and people between member states
3. To develop effective competition for public contracts
4. To standardize specifications
5. To provide advance information of procurement needs to the market

Public procurement has a broad and diverse spectrum of stakeholders such as: politicians on central, regional and local levels, procuring public agency with its organizational structure, suppliers, agency's financiers – taxpayers and its “customers” – citizens and businesses. They can to various degree influence or be influenced by the outcome of a specific procurement.

Public procurement is considered to have some inherent problems such as the risks of

- Corruption
- Protectionism
- Discrimination

Corruption is a serious problem in many developing countries. It is generally considered to be less frequent in developed countries.

One of the leading ideas behind the EU directives and national public procurement laws is to avoid corruption, protectionism and discrimination. The problems' gravity varies among European member states.

Raymond (2008) considers that: *Ethics is another, after value for money, important principle of government procurement. Purchasing professionals are held to higher standards of ethical conduct than people in other professions, yet some do not even know what is expected of them.*

The three main political goals to be achieved through public procurement that currently are discussed in the EU are:

- Environment – Green Public Procurement (GPP)
- Social Responsibility – Socially Responsible Public Procurement (SRPP)
- Innovation – Public Procurement Promoting Innovation (PPPI)

Other discussed political goals are for example bigger participation of SMEs, harmonization of requirements or electronic public procurement.

The environmental and social considerations were included already in the 2004 EU directives for public procurement. They are implemented in most of the EU states' public procurement jurisdiction.

Despite the widespread discussions, declarations and political will as well as agreement on the importance of using public procurement as a driver for political goals, the report on strategic use of public procurement shows that ... *Current data on budget volumes for GPP (and even more so for SRPP and PPPI) are scarce and difficult to compare.* (Kahlenborn et al., 2011) In addition, McCrudden (2004) states that... *The use of public procurement to achieve social outcomes is widespread, but detailed information about how it operates is often sketchy and difficult to find.*

The European Commission's area of Internal Market and Services for the Public Procurement part has a subtitle – "better value for taxpayers' money". At the same time, the commissioner responsible for Internal Market and Services, Mr Michel Barnier, without mentioning anything about the Value for Money, states his mission for the public sector's purchasing activities: *I aim for better use of 2.2 trillion EURO worth of public spending, through public procurement that helps to improve the environment, social integration and innovation* (European Commission, 2010).

There is virtually no discussion how these political goals included in public procurement influence the outcome of different purchasing situations for the public procurement's stakeholders in general and from the Value for Money point of view.

The latest Swedish governmental report on public procurement (SOU 2013:12) points out the need to increase competence in the public procurement area. The report also shows that education at the academic level is mainly concentrated on law courses and lacks a broader approach including economy, technique, environmental and social responsibility. The explanation for this insufficient approach given in the report is difficulties to obtain relevant

statistics and that analysis and research activities in the public procurement domain have not been much demanded. Many questions have been raised but the few efforts that have been undertaken have not been followed up with more in depth research activities.

PURPOSE

The purpose of this explorative paper is an attempt to investigate reasons for and consequences of incorporating political goals such as environmental, social and innovation requirements in public sector purchasing activities for procuring organizations as well as suppliers and other stakeholders. This investigation is limited to the EU member states.

METHODOLOGY

This explorative investigation is mainly based on secondary written sources such as the European Commission's and national reports and official websites on the subject of public procurement and political goals, and earlier studies on public procurement and their outcomes.

PUBLIC PROCUREMENT AND CURRENT POLITICAL GOALS

The whole approach towards public procurement already from the beginning can be described as an important tool to achieve the political goal of an established and well-functioning common market.

The three political goals currently in focus for public procurement are:

- Promoting environmental aspects

Green Public Procurement – GPP

The purchasing activities where environmental goals are taken into account in Request for Proposal (RfP) are defined by the European Commission (2010 b) as *Green public procurement is a process whereby public authorities take environmental concerns into account in their tendering for goods, works and services.*

The EU motivates the use of GPP that public procurement can shape production and consumption trends. A significant demand from public authorities for “greener” goods will create or enlarge markets for environmentally friendly products and services... *By doing so, it will also provide incentives for companies to develop environmental technologies.* (European Commission, 2007)

The basic concept of GPP relies on having clear and ambitious environmental criteria for products and services that can be verified in the public procurement process. Some national criteria and national approaches to GPP have been developed.

- Adherence to certain social and ethical standards

Socially Responsible Public Procurement – SRPP

The purchasing activities where societal aspects and ethical standards are taken into account in RfP are defined by the European Commission (2008) as *Socially responsible public procurement refers to procurement operations that take into consideration the promotion of employment opportunities, decent work, social inclusion and social economy, SMEs, accessibility and design for all, fair and ethical trade issues, wider voluntary adherence to CSR, while respecting the principles of the EU treaty and of EU public procurement Directives*

The report on the strategic use of public procurement (Kahlenborn et al., 2011) states that *The SRPP criteria most commonly adopted ...include: ILO core labour standards, reservations for social enterprises or workshops employing the disabled, social inclusion and equal opportunities, reservations for SMEs and fair trade standards.*

In the same way as GPP, the SRPP presupposes clear, progressive and verifiable criteria for products and services.

- The promotion of innovative goods, services or works

Public Procurement promoting Innovation – PPPI

The purchasing activities with requirements on innovation in RfP are defined in the report on strategic use of public procurement as...

Public procurement promoting innovation is an approach to stimulating innovation on the supplier side. This can be either through pre-commercial procurement, which concerns the R&D phase before commercialization of new products and/or services, or through regular procurement, specifying user needs in such a way that suppliers are stimulated to come forward with innovative products and/or services. (Kahlenborn et al., 2011)

In the case of PPPI, there is an inherent conflict since the very nature of innovation makes it impossible to specify detailed and/or strict requirements. Such requirements would not give space for innovative solutions at the same time as no requirements may permanent the existing ones.

Often the environmental and societal goals are combined to lead to so called sustainable public procurement. United Nations (2005) in the brief on sustainable development discuss the reasons behind this approach. Sustainable Public Procurement (SPP) in political reasoning is ... *a powerful way to stimulate more sustainable consumption and production patters for society in large. (ref)*

There are many reasons behind SPP including:

- *Cost effectiveness of 'greener' products and services*
- *Governments' importance as customers in some markets, can make a difference in environmentally friendly options*
- *Governments can use their market power to influence producers to shift more rapidly to cleaner technologies*
- *Public demands for more sustainable produced goods and services can also have desirable indirect effects, such as raising consumer awareness about environmental and social implications associated with different purchases.*

Innovation is seen as one of the most important drivers for the development and governments' interest in the use of public demand as a driver of innovation has become mainstream in innovation policy debates, a process encouraged by the recommendations of a number of inquiries, reports and policy documents (Uyarra et al., 2010).

PPPI often is associated with GPP as a means to achieve environmental goals. Another important association with PPPI is that it promotes the participation of SMEs.

This development is underlined by ...*the Kok Report, reviewing progress on the Lisbon strategy, and the Aho Group Report "Creating an Innovative Europe"* (Aho et al., 2006) as well as by EC the Lead Market Initiative (European Commission, 2007), which considers public authorities and public procurement as one of the key policy instruments to achieve these goals.

There are no clear definitions of "innovation", "innovative" procurement and procurement of "innovation" despite extensive usage of them globally, and on the European and national levels. The report to the European Commission on Strategic Use of Public Procurement observed that... *innovation itself is often named as a criterion for procurement, along with quality and effectiveness. In most countries specific PPPI criteria are non-existent; rather, broad considerations are recommended to promote innovation in procurement, often with a focus on the promotion of SMEs. In a number of countries PPPI is promoted through specific methods of procuring innovation, such as public-private partnerships...* (Kahlenborn et al., 2011)

PUBLIC PROCUREMENT AND VALUE FOR MONEY (VfM)

There are several definitions of "Value for money" that can be summarized as the cost of a product or service against the quality of provision. *Value for Money is based not only on the minimum purchase price (economy) but also on the maximum efficiency and effectiveness of the purchase.* (www.businessdictionary.com).

Erlendsson (2002) concludes - *Value for Money is a term used to assess whether or not an organisation has obtained the maximum benefit from the goods and services it both acquires and provides, within the resources available to it.*

Harvey & Green (1933) consider VfM as a definition of quality - *Quality as value for money sees quality in terms of return on investment. If the same outcome can be achieved at a lower cost, or a better outcome can be achieved at the same cost, then the 'customer' has a quality product or service.*

Raymond (2008) sees VfM as the core principle governing public procurement, and is supported by the underpinning principles of efficiency and effectiveness, competition, accountability and transparency, ethics and industry development.

Value for Money is seldom monitored or measured despite the declaration that VfM is a core principle for public procurement and public service agencies' ambition to maximize overall "value for money" for citizens. Kahlenborn et al. (2011) points out:

Monitoring public procurement and related expenditures remains in general weakly developed and comparatively inconsistent through Europe... monitoring and reporting are strongest for GPP.

For SRPP, hardly any such specific monitoring or reporting lines exist... No systematic monitoring and reporting of PPPI is undertaken in any Member States, although here the need to do so is broadly recognized.

According to Kahlenborn et al (2011) *only 24.8% of the respondents indicated that they monitor the environmental performance of suppliers. For SRPP and PPPI the figures are even lower... Of the interviewed procuring agents, 68.2% stated that their organization does not have a system in place to monitor compliance in any of the three categories...*

EFFECTS ON PUBLIC PROCUREMENT OF INTEGRATING POLICY GOALS IN PUBLIC PROCUREMENT

Public procurement is seen by politicians as an instrument to achieve specific political outcomes. At the same time it is difficult to find more in depth analysis of the effects of this policy on public procurement's results and on stakeholders. In the debates several aspects of public procurement are downplayed, especially regarding innovation. The main areas not fully taken into account are (ref)

- That public procurement deals with a wide range of goods, services and works
- Risks involved with including political goals in public procurement
- Diverse nature of innovation

Buyer's perspective

The most extensive investigation on the strategic use of public procurement in EU (Kahlenborn et al., 2011) showed quite significant uncertainty. *For the GPP most of the respondents the cost effect is higher or the same with more the ¼ of answers no opinion. For the SRPP almost half of the respondents have no opinion and the rest considers that the cost is higher or the same.* (Kahlenborn et al., 2011)

There are several aspects that can have considerable impact on the costs such as:

Cost of certification - This is especially valid for GPP since environmental requirements must be verified.

Reduced competition - This can take place in all three types of procurement but is especially valid for innovative procurement. A number of suppliers will struggle to comply with new requirements based on GPP/SRPP/PPPI, thus, reduced competition. Another aspect is the risk for the public sector not to get from the value-for-money point of view the best offers if suppliers consider that the fulfillment of the requirements will not produce more contracts inside and outside of the public sector.

Need of training and instruction - In order to obtain positive results of GPP and PPPI new, earlier unknown types of solutions, technologies or procedures have to be implemented and it can be necessary with extra training activities for the staff.

Unwillingness to innovate - It can be difficult to persuade suppliers to give up their established range of offers and implement the innovative solutions required.

More complex tendering procedures – *The procurement process is lengthened as specifications for the requirements have to be determined. Additionally, the offers have to be compared and evaluated according to the specifications. The more requirements are considered in calls for tenders, the more time is consumed in the selection and awarding processes.* (Kahlenborn et al., 2011)

Monitoring – If public procurers do not rely on self-declarations by suppliers or accept the variety of existing certificates at face value in order to ascertain compliance with their respective GPP/SRPP/PPPI standards, the procuring agency requires extensive capacities in verifying and monitoring compliance. Monitoring efforts are complicated if global sourcing strategies (e.g. sub-suppliers from China) are involved, as this implies monitoring at places under foreign authority and operating under different legal conditions.

Several reasons are provided for the generally low monitoring rates. They include lack of resources and/or political support as well as insufficient know-how in establishing a monitoring scheme. A further challenge is posed by the difficulties of verifying compliance. This is even more difficult when suppliers (as many of them do) have a long

supply chain that is often located abroad. It is difficult to verify the environmental performances of suppliers in these cases. As an alternative strategy, contracting agencies are increasingly relying on suppliers to present proof of compliance with certain criteria, which is mostly done in the form of third-party verified audits. This presents a new set of challenges for suppliers, who have to carry the costs for these activities – a problem particularly for SMEs.

Appeals - possibility for legal protests against any single requirement including GPP/SRPP/PPPI in RfP that can result in appeals.

Lack of knowledge – GPP/SRPP/PPPI requires a broad understanding and need for professionalism

In addition procuring organizations can find themselves in uncertain situations. Uruya et al. (2010) argue that *..., the scope for public procurement to stimulate innovation has to be considered in a context of often conflicting policy objectives. Procurement practitioners are thus faced with a wide range of demands placed upon them to simultaneously achieve multiple goals beyond the proximate goals behind the procurement itself.*

McCrudden (2004) finds that *... We often think about government as regulating market participants, sometimes encouraging markets through competition law, or restraining them through minimum wages laws. But governments increasingly play a role as active participants in the market itself, purchasing public works, supplies, and services.... How government attempts to combine two functions: participating in the market as purchaser and at the same time regulating through the use of its purchasing power to advance conceptions of social justice.*

Hettne (2013) points out that *...the general EU legal framework provides a fairly large space for social and environmental considerations....But it is important that the contracting authority makes sure that integration of environmental and social considerations is not done in isolation from objectives stemming from the Union law in general.*

Suppliers' perspective

On the positive side, to be exposed and respond to new requirements, which coincide with the political goals, may strengthen and differentiate the company's image and perception as environmentally and socially responsible, and innovative. However, negative aspects may very well dominate, such as:

The lowest price approach - Suppliers have been used to the public sector's value for money approach as procurers aim to buy at the lowest price. However, GPP/SRPP/PPPI exposes the suppliers to new demands with varying and broad implications. Thus, the preparation of an offer consumes more time than usual and causes longer procedures.

Administrative approach - According to Kahlenborn et al. (2011) the biggest challenge is an increase in the administrative requirements resulting from integration of other objectives in the procurement process. With the proliferation of GPP/SRPP/PPPI criteria in the public tenders, both the bidding process for a tender and the actual implementation of a contract demand demonstration of compliance with new requirements. In particular, the administrative work necessary to participate in tender bidding processes imposes a particular burden on many suppliers. *...a significant increase in demands for labels, third-part audits, verification of the supply chain, and general paperwork documenting production processes. The winning supplier also faces a substantial amount of new requirements to comply with.* (Kahlenborn et al., 2011) The result may be that getting a contract puts the winning supplier in the winner's curse (Thaler, 1998) situation.

Risks - To participate in bidding and respond to RfP that include GPP/SRPP/PPPI requirements can produce risks as the efforts to prepare an offer with considerable costs without winning the contract mean lost human resources and time invested in the process that can hardly be recovered. The most affected parties are SMEs for whom the upfront investments to participate in tenders represent a noticeable share of their profits.

Heterogeneity – An additional challenge for suppliers is the diversity in integrating and incorporating GPP/SRPP/PPPI requirements. As different procuring bodies can decide on its procurement practices, suppliers are faced with a myriad of different procedures and requirements. For relatively low quantities demanded, a supplier has to develop a series of distinct applications for the same product. Hence, the administrative work increases.

Lack of consistency – If there is no long term strategy and the procuring body changes its requirements and standards frequently, it becomes difficult for the company to adapt. With inconsistent policy directions, standards and criteria change relatively fast. Hence, investments in certain technologies or procedures may not pay off in the medium or long run.

CONCLUSIONS

There is a tendency to include more and more political goals in public procurement. The three most important ones are environmental, social and innovation. However, the effects of their incorporation on the Request for Proposal, effectiveness and Value for Money have not been fully investigated.

The few reports that have been done on the subject show that inclusion of requirements based on political goals mean new challenges for both buyers and suppliers. It is likely to give rise to

additional costs e.g. for monitoring and a more complex process in general for the public agency as well as for suppliers' administration and preparation.

Since there are several diverse stakeholders, Value for Money for public procurement that includes requirements based on political goals typically differ for different stakeholders as well as for different political goals.

Inclusion of several diverse political goals on public procurements may result in new conflicts of interest between different goals. One example is the ambition to include small and medium sized enterprises (SME) at the same time as the bidding process becomes more complicated in particular for SMEs.

The time perspective is also important and should be investigated as the Value for Money of incorporation of political goals can change from time to time.

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