

CHAPTER 4

Curbing Corruption in Public Procurement

- A. Reforming Public Procurement
- B. Analyzing the Public Procurement Process to Identify and Eliminate Risks of Corruption

A. Reforming Public Procurement

■ A. Michael Stevens

Principal Audit Specialist (Financial Investigator)
Asian Development Bank²¹

When the Asian Development Bank's auditors and investigators visit Asian and Pacific countries, they are often overwhelmed by accusations of fraud and corruption related to public procurement. Sometimes government officials and bureaucratic decision makers complain against contractors and consultants—the buyers against the suppliers. Other times, the reverse happens and the suppliers complain against the buyers. And sometimes, the buyers, suppliers or civil society organizations complain about a third party, often those institutions that have funded the procurement at stake.

Unfortunately, learning that public money is being siphoned off to private pockets is much easier than identifying the guilty and gathering sufficient evidence to bring the guilty to justice. Further, many legal systems are ineffective overall or make punishments trivial enough so that the expense of investigating and prosecuting corruption is not justifiable when weighed against a “greater public good”. Action should thus be taken to prevent corruption; procedures that assure transparency and foster integrity in public procurement constitute the pivotal instrument.

Past reforms of public procurement procedures

Corruption in public procurement is not endemic only to developing countries. In fact, it is arguable that the push for greater accountability and transparency in industrialized countries has caused the concerns over public procurement in the developing world. Claims for greater government accountability in industrialized countries have brought forth continuous efforts

²¹ The views expressed herein are those of the author and do not necessarily reflect the views or policies of the Asian Development Bank.

to review and reform procurement systems to ensure that the taxpayer “gets his money’s worth.” The United States (US), for instance, launched a program to “reinvent government” in 1994, and one of its top priorities was to reform the procurement system. This greatly increased efficiency in public procurement; besides, the removal of bureaucratic obstacles in public procurement reduced the opportunities for corrupt practices. The United Kingdom in 1998 launched a study on Efficiency in Civil Government, which resulted in several improvements in its procurement system. France, too, undertook procurement reforms.

Such self-examination led the industrialized countries to inspect their investments in developing countries through multilateral institutions. With the aim of rendering these investments more effective, they made financing conditional on procurement and administrative reform. This was not because of some unique concern over public procurement in the borrowing countries, but rather, because of the need to ensure their own taxpayers that projects in developing countries are sound investments with positive results.

Procurement reform on the buyers’ side

Public procurement is essentially a business process—with considerations of integrity; accountability and its twin, transparency; national interest; and effectiveness. This business process is also embedded in a political system; thus, without political support, it cannot be changed toward effectiveness and integrity. Simply blaming government officials on the buyer’s side for being corrupt is inadequate; lack of expertise contributes just as much to generating corruption in public procurement.

To provide such expertise, the United Nations Commission on International Trade Law developed a model law on procurement of goods and construction in 1993.²² The model law essentially strives to promote competition among suppliers of goods and construction and encourages bidders to participate regardless of their nationality.

The reason why a procurement law focuses on fostering competition as its key mechanism is simple: market-based systems exert constructive pressures on suppliers to constantly adjust and improve the pricing, quality and performance of a product or service. A supplier that arranges to minimize market pressures through undue influence or bribery loses the initiative to

²² The document is available at UNCITRAL’s Website: <http://www.uncitral.org/english/texts/procurement/proc93.htm>.

make his product more competitive, and the buyer is far more likely to receive substandard products and services.

Encouraging participation “regardless of nationality” is somewhat more controversial. While it is arguable that allowing foreign competitors to bid creates additional risks of corruption, those dealing with anti-corruption issues at international organizations certainly recognize the need to work in concert and share knowledge.

Previously, the practice was to ask each country to be responsible for the conduct of its nation’s companies. However, because the economic stakes were extremely high, many countries charged one another with failure to match their own efforts in this regard, by either putting a weak statute on the books or by neglecting enforcement. The US Foreign Corrupt Practices Act is a prime example: American companies complained bitterly of not having a level playing field, even though the law was only superficially enforced until the late 1990s.

The United Nations has recognized these points in its Convention Against Corruption. The Convention acknowledges “that corruption undermines the legitimacy of public institutions and strikes at society, ethical values and justice, as well as at the sustainable development of nations, and that the globalization of the world’s economies has led to a situation where corruption is no longer a local matter but a transnational phenomenon that affects all societies and economies, making international cooperation to prevent and control it essential.”

So, while acknowledging that eradication of corruption is a responsibility of states, the Convention recognizes that nations must cooperate with one another, with the support and involvement of civil society, if their efforts in this area are to be effective. Such cooperation is necessary not only to allow states to share information globally, but to ensure equitable competition among businesses. Even the International Chamber of Commerce, which welcomed the United Nations’ moves to create this Convention, emphasized that unless properly monitored, the Convention could create an uneven playing field for businesses.

But no matter how well all of these issues can be addressed, whether through individual or collective efforts, and no matter how well we try to preempt fraud and corruption, everyone knows it will occur, somehow, somewhere, to some degree.

Setting incentives for change on the suppliers’ side

Incentives for change in the suppliers’ business practices may fruitfully complement the mentioned legal and procedural reforms. Penalties for corrupt behavior serve as an essential and in fact ubiquitous deterrent; they can be

found in basically all countries' legal and judicial systems, and multilateral institutions, deprived of applying penal sanctions, make use of such administrative penalties as disqualification or ineligibility as penalties instead.

When strategically applied, administrative penalties can serve as an excellent incentive for changing business practices for the better. ADB's Anticorruption Unit's policy for dealing with contractors that violate the policy strives to exploit this potential: the company or individual is requested to explain its practices and what measures it plans to implement to avoid similar violations in the future; the proposed reforms are taken into consideration when ADB determines the penalty. This strategy has a two-fold advantage: it avoids harming the company and thus its employees, while promoting good practices and integrity. ADB has tried to balance carefully the need to punish with the better interest of reform.

Practical steps to resolve corruption in public procurement

Even though resolving corruption in public procurement cannot be accomplished by one best method, some general principles can certainly be followed. The first step when reforming the procurement system is to identify deficiencies. This review must evaluate the regulatory framework, monitor compliance with laws and regulations, measure performance and advise governments and civil society of successes and deficiencies. It must further ensure appropriate competition, take advantage of potential economies of scale and demonstrate professionalism and expertise. Only after all these means have failed may appropriate penalties be imposed.

Confidence in public procurement helps to attract more investment by lowering risk. A transparent system allows the private sector to assess the risk of doing business with governments and make more rational investment decisions, in line with good commercial practice and public accountability requirements. Development partner agencies also have an interest in transparent public procurement, since control of expenditures through accountability is essential to explain to their management and boards of directors that development assistance funds have been used in an appropriate manner.

B. Analyzing the Public Procurement Process to Identify and Eliminate Risks of Corruption

■ **Robert Jourdain**

Manager, Aid Monitoring Services
Société Générale de Surveillance, Geneva, Switzerland

Nadia Balgobin

Business and Public Ethics Consultant
Société Générale de Surveillance, Geneva, Switzerland

Eliminating risks of corruption in public procurement requires their prior identification. This again demands a precise understanding of the procurement process. With the ultimate aim of proposing a systemic approach to curbing corruption in public procurement, this document provides an overview of the key areas of concern in public procurement and how to address them.²³ It describes the predominant concepts and principles in public procurement, identifies the main parties intervening in this process and discusses actual instances of procurement malpractices. It also proposes three tools that are used by international financial institutions (IFIs) to detect corruption in public procurement, *inter alia* the Risk Profiling of Procurement Entities, a proactive and cost-efficient tool that the Asian Development Bank successfully employs.²⁴

²³ Full documentation on this workshop is available at <http://www1.oecd.org/daf/asiacom/KL.htm#documents>

²⁴ Office of the General Auditor, Anticorruption Unit.

Key concepts and principles in public procurement

Public procurement is usually defined as the acquisition of goods, works and services by a public administration. Contracts are signed mostly with the private sector and are expected to meet the user's requirements with the best value for money—defined as life-cost and quality. As such, public procurement must serve citizens' and taxpayers' interests. Public procurement represents an important part of governmental expenditures. In the European Union, for example, public procurement is estimated to cover about 15% to 20% of gross domestic product; in 1998 alone, 73,000 invitations were issued for a total value of EUR1,000 billion. Given the weight of public procurement in a national economy, it is clear that good procurement practices are essential ingredients of good governance.

Procurement activities can basically be categorized as “poor” and “good” practices: Poor practices either entail waste and delays because of inefficiencies or stifle competition because of unfairness or corruption. Both such practices impede economic growth and affect public trust. Good practices achieve the forecast results in a timely fashion while ensuring cost-effectiveness. Good procurement promotes four key principles: transparency, economy, efficiency and fairness.

- *Transparency* is defined as an objective (neutral) and public (visible) mastering of the whole process from call for tender to contract award and management. An important indicator is the “public advertisement,” which must be adequate and prompt and provide identical responses to all requests for clarification.
- *Economy* can best be expressed through such criteria as
- Contract prices that are close to original estimates (although a price that is too close to the original one might indicate prior knowledge of the buyer's estimate),
- Unit rates that are comparable with similar conditions/price DB/indexes, and
- A number of bids that is sufficient to reach the best possible price.
- *Efficiency and timeliness* are achieved by comparing the planned with the actual procurement schedule, by avoiding any delay in public bid openings, and by measuring the length of time between evaluation and contract award—which normally should be reduced to the shortest possible.
- *Fairness and equity* in the procurement process are indicated by a low number of complaints received. Tender rejections for marginal reasons

and patterns of awarded contracts by the same institution are important criteria for verifying compliance with this exigency.

Failure to comply with these principles indicates corrupt or fraudulent practices, respectively defined as *the misuse of an individual's position for improper/unlawful enrichment*²⁵ or a *misrepresentation of facts*.²⁶ Such practices, including collusion, obviously diminish the benefits of free and open competition.

Six different procurement types can be distinguished: International competitive bidding, limited competitive bidding, national competitive bidding, shopping, direct contracting and force account. The following table outlines the specific features of each of these procurement types:

It is worth noting that efficient management of the procurement cycle, irrespective of the procurement method that is being used, requires several types and levels of documentation, such as guidelines and handbooks (for

Table 4.1. Features of Procurement Types

Procurement Type	Features
International Competitive Bidding (ICB)	<ul style="list-style-type: none"> • Widest range of choices • Gives adequate, fair and equal opportunities to bid
Limited International Bidding	<ul style="list-style-type: none"> • ICB by direct invitation, no advertisement • Limited number of suppliers
National Competitive Bidding	<ul style="list-style-type: none"> • Unlikely to attract international competition.
Shopping, National and International	<ul style="list-style-type: none"> • At least three price quotations from known/ predetermined suppliers
Direct Contracting, Single Source	<ul style="list-style-type: none"> • Extension of existing contract for goods/services of similar nature • Standardization of Equipment
Force Account	<ul style="list-style-type: none"> • Borrower's own personnel and equipment

²⁵ By offering, giving, receiving, or soliciting anything of value to influence a procurement process or a contract execution.

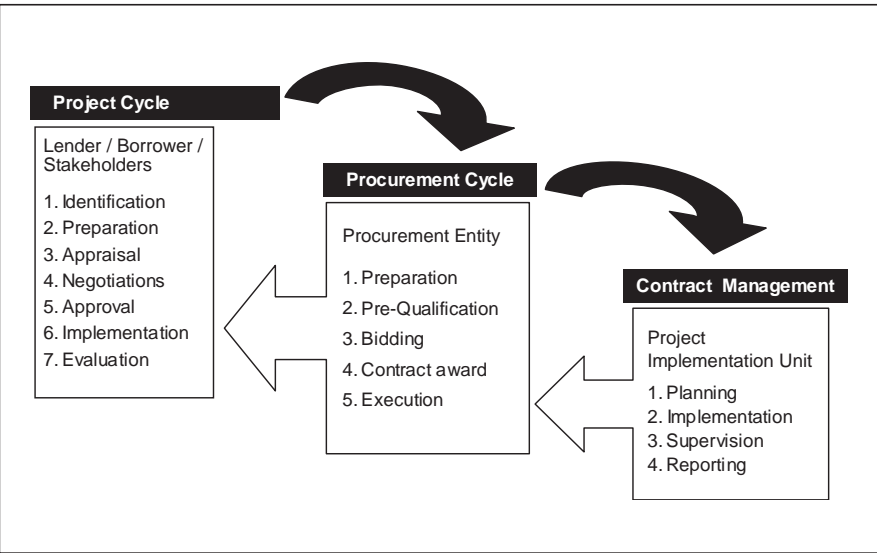
²⁶ In order to influence a procurement process or the execution of a contract.

procurement of goods and services and for the employment of consultants), standard documents and evaluation guides.²⁷ Considering this wide documentation, it is evident how complex procurement is and explains the difficulty of state administrations in coping with these difficulties efficiently.

Identifying corruption risks in public procurement

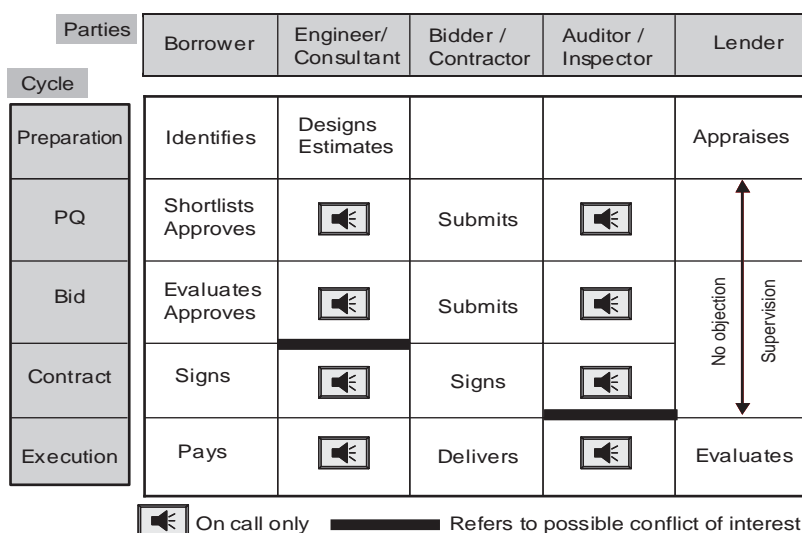
When trying to tackle corruption in public procurement, it is important to identify the stages most affected by corrupt practices. To this aim, the procurement cycle must be seen in its wider context, called “The Project Cycle” and outlined in the following diagram:

Figure 4.1. The Project Cycle



The following matrix takes in account the parties involved in each of these stages. This is important to identify actors that could prevent the risks and could take appropriate action.

²⁷ They are often complemented by more specific references such as the International Federation of Consulting Engineers Conditions of Contract, United Nations Commission on International Trade Law and World Trade Organization regulations, etc.



As the diagram outlines, only two parties are necessary to acquire goods, works, or services: the client (or “borrower” in lending operations of IFIs, in which case a lender will also have a supervisory role) and the contractor (lender). Depending on the nature and complexity of the process, an engineer/consultant might partake in the process (indicated by the “on call” symbol). An auditor, inspector or other independent third party with a supervisory role is also involved “on call” only—and such calls are too often made only when a problem has already occurred. Although experience clearly indicates that transparency and accountability are greatly enhanced with the involvement of such third parties, nothing in the bylaws or the procurement guidelines calls for any statutory auditors or inspectors.

Who among these involved parties can best address the risks of corrupt practices and take the corresponding preventive or corrective actions? The brief extract of the list of possible events that may occur in the preparation stage below allows the evaluation of how difficult effective prevention of corruption in procurement is:²⁸

²⁸ Other examples can be found in the workshop material at <http://www1.oecd.org/daf/asiacom/KL.htm#documents>

- Absence of project procurement plan (leading to absence of risks management),
- False/inflated current/future requirements (materials, cash, replacement...),
- Decision not to publicly advertise invitation to tender,
- Setting unrealistic price of tender documents,
- No written procedure on public tendering, and
- Procurement staff lacking basic training.

These examples also highlight the importance of a systemic approach to detecting corruption in public procurement.

Toward a systemic approach

A number of tools and instruments have been developed to address the above-mentioned risks of corruption in public procurement. The following section presents three of these tools that are used by IFIs to detect corruption in public procurement. For a better understanding of the rationale behind the three tools, the project cycle should be kept in mind, going from an *ex-post* (completed projects) situation to an on-going and finally an *ex-ante* (projects at the design stage) approach. This allows the evaluation and understanding of the potential behind each of these tools to enhance procurement effectiveness. Each tool description is followed by an assessment of its contribution toward achieving the key principles presented above, namely transparency, efficiency and effectiveness.

Tool 1: Independent procurement reviews

Financing institutions must ensure that the proceeds of their lending operations are used for the purposes they were granted for, with due attention to considerations of economy, efficiency and transparency. This verification serves to assess and qualify various aspects of the procurement management cycle. In particular it allows IFIs to

- verify compliance against procurement guidelines and procurement and contracting procedures and processes followed for each project, including the conformity verification of final contracts against the original bidding documents;
- assess technical compliance, physical completion and price competitiveness of each contract (usually selected through a representative sample);

- review contract administration and management issues as dealt with by implementing agencies;
- evaluate the capacity of implementing agencies to handle procurement efficiently; and
- identify improvements in the procurement process in the light of deficiencies.²⁹

This check is usually undertaken by independent third parties. It complies with the lender's fiduciary responsibility and is usually considered as a "stock-taking" exercise. However, since it is undertaken only after completion of a project, it comes too late to raise effectiveness issues for that particular project. The tool is thus most useful in a forward perspective, as it has a deterrent effect and allows for adjusting future project portfolios. Still, these advantages only become valuable if identified deficiencies are properly addressed before any new project in the same institutional setting is implemented.

Tool 2: Primary checks of procurement during project implementation

The second tool provides lending agencies with ongoing compliance checks of all documentary evidence supporting the procurement processes for goods, services and consultants undertaken by a borrower. The compliance is benchmarked against the relevant guidelines for procurement of goods and works and/or for employment of consultants.

The services assist the decision-making process of the lending agency (or procurement officers) by providing timely "primary check" reports about compliance at each and every step in the procurement processes undertaken by the borrower. These standardized reports contain a summary, an appropriateness analysis, and recommendations. The service also assures constant liaison with the lending agency for further clarification that might be requested, and provides the lending agency with regular analysis of patterns of non-conformities for any given portfolio of projects.

Such continuous identification of non-conformity, applied during project implementation, enables corrective actions to be taken before it may be too late. It also gives a broader view of a country's portfolio: it compares the performance of each borrower within the same country and thus identifies needs for support both in terms of management and capacity building.

²⁹ Implementation of such mandates is done by verifying a detailed list of about 70 criteria (from pre-qualification down to disbursements) for each and every selected contract, including no less important items than documentation management, borrower and lender supervision, timeliness, etc.

Tool 3: Risk profiling of procurement entities—implementing agencies

The third tool consists of a systemic and comprehensive assessment of procurement entities and implementing agencies considered within their institutional context.³⁰ Its overall objective is to enable the assessed bodies to eventually master the identified risks attached to their mandate’s undertaking as defined by the following “modules”: board of directors; institutional framework; integrity management; system and processes management; relations with stakeholders; human resources; financial processes and controls; procurement cycle management; contracts implementation; first, second and third-party audits; external and internal communication; outcomes; by-laws; regulations and voluntary accreditations.

These modules are first organized into a “cause-and-effect linkages” system. They are then defined by a series of “indicators of best practices,”³¹ also called “objectively verifiable indicators,” and finally each of these indicators is distributed amongst each of the three dimensions shown in Table 4.2:

Table 4.2. Cause-and-Effect Linkages for Procurement Assessment Modules

1. Contributors’ Expectations	Transparency, efficiency and effectiveness
2. Management Components	Operational systems and processes, programs and projects, human resources and finance
3. Improvement Cycle	The “plan, do, check, act” principle

³⁰ This assessment leans on some of the principles and dimensions laid down by management tools such as the Balance Scorecard, the Excellence Model, the Logical Framework and ISO Standards. However, it is important to note that ADB’s approach pays due attention to the intrinsic limitations of any model that is based on private business enabling contexts, presumably transferable to the public domain of socio-economic development; for example, customer satisfaction, partnerships, road maps, etc., cannot and should not be applied as such when dealing with the provision of public goods.

³¹ For example, the financial module contains indicators used by IFIs in their respective Country Financial Accountability Assessment, Country Procurement Assessment, Project Management Reports, Financial Accounting, Reporting and Auditing Handbooks, and Auditing Standards for non-commercial entities.

Each indicator is therefore assigned to one module, one dimension and one component. All these elements are integrated into a dedicated software whose quantification and weighting features make it possible to provide a “performance assessment tool” whose ultimate purpose is to serve as a benchmarking, monitoring and evaluation system, as per the following sequence:

- Key strengths and weaknesses are measured, enabling the provision of a detailed and actual performance dashboard (t_0);
- The identified weaknesses are reorganized in several groups of Corrective and Preventive Actions Programs ($t_1 - t_n$); and finally
- They serve as a logical framework for a focused but comprehensive monitoring and evaluation system ($t_{n, n+1}$ against t_0).

While this tool is best used as early as possible in the project cycle, it can also be applied during project implementation. The key interest of this tool is that it provides a systemic assessment of a procurement entity (or an implementing agency) against an integrated set of dimensions within a “cause-and-effect linkages” system rather than isolated ones³².

Who and how to implement an anti-corruption program?

A successful fight against corruption depends on many factors; the questions “*who* initiates the fight within the organization” and “*how* is it rolled out” are the most critical ones. As concerns the “*who*”, in the public sector the accountability mechanism is in the hands of the policy body and the senior management, i.e., the government and the public administration. To get started properly, commitment has to be secured from the very top.

The following case study demonstrates how an anti-corruption program could be implemented. It is based on an alleged corruption scandal that the Société Générale de Surveillance (SGS) itself had encountered, and to which both its board and top management reacted.³³ This case triggered the SGS Global Ethics Program, launched in 140 countries and involving more than 30,000 employees.

³² As is often the case for “modules” such as finance, procurement cycle management, integrity management, etc.

³³ This case is documented by Jean-François Arvis and Ronald E. Berenbeim in “Fighting Corruption in East Asia: solutions from the Private Sector,” The World Bank, 2003. Part II: Case Studies: Société Générale de Surveillance, pages 194 and ff.

The scandal led to the development and implementation of the following action plan:

Table 4.3. Société Générale de Surveillance Action Plan

SGS Action Plan	Conceptual/Managerial Reference
1. Introduction and dissemination of the Code of Ethics	Integrity framework
2. Establishment of a compliance office Focal point	
3. Inclusion of an ethical clause in the employee's contract	Legal framework
4. Establish an ethics committee.	Leadership
5. Annual senior management reporting.	Management Accountability
6. Develop training components with employees.	Ownership
7. Maintain awareness on ethical commitment (e.g. posters).	Communication
8. Establish a direct channel to Compliance Office.	Reporting
9. Embed ethics standards in management policy and procedures.	System alignment
10. Integrated compliance in terms of reference of internal and external audit.	Control

This action plan was developed for a private sector undertaking. Its ten pillars can also be applied in a public setting, however. To give just one example: if any given public sector were to consider an anti-corruption program to make procurement more transparent, a Public Ethics Infrastructure is a point to start with—just as in the private sector. Concerning public procurement more particularly, a Public Ethics Infrastructure that would meet good governance principles would have to comprise the following features:

Table 4.4. Features of Public Ethics Infrastructure

Legal/Institutional Framework	Systems and Mechanisms
Procurement Law and Regulations Code of Conduct and Anti-Corruption Act	Oversight body Training Communication Reporting Controlling Investigation
People's Commitment	Values
Government and Public Administration Declaration of Compliance Employees Statement of Compliance	Leadership Accountability Ownership

The following diagram synthesizes the major concepts and principles. It is within this framework that the tools and techniques for detecting corruption in public procurement presented above could best be applied.

Figure 2.2 Major Concepts and Principles of a Public Ethics Infrastructure

