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CONFLICTS IN PUBLIC PROCUREMENT

During the last couple of years, there has been a tendency to include more and more political goals into public procurements, such as environmental and societal considerations. This can result in higher prices paid by the public sector compared with similar procurements in the private sector. The decision makers at local level are elected and should represent the interest of their communities and voters, which includes promoting regional/local companies and economic development. This task can sometimes get into conflict with public procurement law or the political goals of a central government.

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1. Introduction

A considerable proportion of all purchasing activities on any national market is due to public procurement and has great importance for the economy of any country. As 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 € – of all the income generated in the EU. (http://ec.europa.eu/internal_market/publications/docs/public-procurement_en.pdf) Administration at all levels – national, regional or local – purchases goods, works or services in order to deliver public facilities. Government purchasing through public contracts is known as public procurement. It is of huge importance to the economy. (http://ec.europa.eu/internal_market/publications/docs/public-procurement_en.pdf). Also *at the local/regional level public procurement can easily reach double that in terms of percentage of public expenditure. For example, a study*

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of public procurement across Baltic city metropolises(3) shows that public procurement accounts for 40% of the city budget in Helsinki and 30% in Stockholm.*

Public procurement not only meets purely utilitarian and economic goals, but also political goals that can involve societal, environmental or other political issues. Examples of such goals are new EU directives that impose a procuring organization to specify and take into consideration environmental and social requirements that are harsher than the national law which private companies follow. Furthermore, deregulation of previous monopolies has a considerable impact on public procurements [6]. Arrow-smith and Hartley [2] argue that despite the scale and complexity of government purchases, the field of public procurement has remained a relatively under-researched area amongst economists, lawyers and other social scientists.

The purpose of this paper is to investigate and discuss conflicts of interest in public procurement, the sources of such conflicts and their consequences.

2. Public procurement in Europe

Public procurement is one of the most frequent types of transactions between organizations, in this case between public and private ones. All types of transactions follow specific laws that regulate the rights and obligations of all parties involved. All parties involved in public procurement have to adhere to national public procurement law, which in the case of the European Union member states is based on the European Union directives for public procurement. The decision making process and the number of stakeholders, as well as their specific goals in public procurement, differ from those of purchasing processes between private organizations.

Public procurement in the European Union countries is based on the principles from the Treaty of Rome regarding the free market within the EU. It has to follow five fundamental principles:

- Non-discrimination – all discrimination based on nationality or by giving preferences to local companies is prohibited.
- Equal treatment – all suppliers involved in a procurement procedure must be treated equally.
- Transparency – the procurement process must be characterized by predictability and openness.
- Proportionality – the means of assessing offers must have a natural relation to the supplies, services or works that are being procured.

*CORDIS – Community Research and Development of Information Service, <<http://cordis.europa.eu/fp7/ict/pcp/key_en.html>>.

- Mutual recognition – the documents and certificates issued by the appropriate authority in a member state must be accepted in the other member states.

The national public procurement laws of European Union member states have to follow the directives for public procurement (the latest is from 2004). These directives are based on these five fundamental principles. The main reason for these principles was to create a common European market and increase competition. They do not directly deal with the interests of each member state, including public agencies that often are cautious and much more eager to avoid being taken to court or bad press than to achieve the best possible deals. These principles protect the companies that participate in tendering, especially against corruption and favouring of specific companies. The public procurement directives based on these five principles are quite detailed, often making the public procurement process tedious and bureaucratic compared with similar purchasing situations in the private sector.

The EU directives do not deal with the economic outcome of specific deals. To put more and more political goals in public procurement is quite natural from the EU point of view. From the member states' point of view, the incorporation of such requirements can result in considerable additional costs.

3. Stakeholders in public procurement

Following Lindskog [6], the main stakeholders in public procurements are:

Politicians. Politicians are elected by citizens and responsible to them for their decisions and initiatives. Their voters evaluate politicians' achievements in the next election. Their political decisions depend on their party's current policy.

Central government. They formulate visions and take overall responsibility for the whole country. The execution of policy is delegated to authorities.

Local government. They are responsible for a local authority, community or region. Additionally, they are responsible for a geographically bounded area including support for local companies that provide employment for their voters, who make up the tax base for local governments, which in their turn deliver services to citizens and local businesses.

Public agency. The authority's overall goal is to deliver the best possible service at the lowest cost.

Public agency management. Management is responsible for the running and administration of an agency and its decision making.

Procurement department. The procurement department is responsible for the purchasing activities of an agency.

End-users/employees. End-users are employees that will use the specific function, service or equipment that is procured.

Citizens and businesses. The general public, citizens and businesses are the agencies' "customers".

Companies participating in the tendering process. Companies that respond to the Request for Proposals and prepare offers.

In addition to the stakeholders that are more or less directly involved in the public procurement process or influenced by its outcome, the EU through its public procurement directives has a big impact on the public procurement process, procedures and results.

4. Incorporation of political goals versus costs

Possibly, the most important source of conflict in the public procurement arena arises from following policies and promoting political goals rather than minimizing the costs of such transactions. Typical examples of these political goals include environmental and social requirements, as well as support for disadvantaged social groups, such as minorities or disabled persons.

There are currently three main areas of interest when using public procurement to achieve political goals:

- environmental protection through green public procurement,
- social responsibility through socially responsible procurement,
- innovation through Public Procurement Promoting Innovation.

Following Arrowsmith [1], there are two main ways to approach policies of realizing political goals through public procurement:

- policies can be
 - limited to securing compliance with legal requirements,
 - those that go beyond;
- policies applied
 - only to the contract awarded and
 - those that go beyond.

4.1. Policies and requirements

4.1.1. Policies limited to securing compliance with legal requirements

The main reason for the government to use requirements that merely reflect the existing legal norms could be:

- To avoid associating the government with unlawful behavior, both to set an example and to avoid public criticism.

- To provide additional enforcement tools for securing compliance with the general law and/or punish violations, and to reduce the risk of violations of the general law during the realization of a contract.

- To ensure a level-playing-field and to avoid unfair competition. Firms that do not comply with their legal obligations to pay taxes and observe labour laws etc. enjoy an unfair competitive advantage and may drive legitimate operators out of the market.

- To avoid using government contracts as a means for criminal activities or terrorism.

One example of a way to adopt such a policy is exclusion due to corruption or criminal convictions. The risks involved in implementing such a policy include the additional administrative burden of controlling and punishing the contractor, when required.

4.1.2. Policies that go beyond compliance with legal requirements

One example of a policy that goes beyond the current legal requirements could be to demand that of those engaged on a contract a certain proportion are to be disabled persons. Other examples include:

- promotion of gender and racial equality,
- precursor of future legislation, when it is difficult to get it through the parliamentary route,
- highest possible standards – the government sets an example – which may encourage wider acceptance of the standards and avoid public criticism,
- effectiveness – procurement can be a more effective policy instrument than alternatives. (Swedish examples: procurement by the STATTEL delegation of telephone services in order to speed up the liberalization of the telecom market by introducing more competitors, as well as procurement by the central government authority, Statskontoret, of PC screens with specified low radiation).

The risks involved in this kind of procedure is a reduced number of suppliers, thus, lower competition as well as additional costs for companies that may be transferred to the procuring public organizations.

4.2. How the policies are applied

4.2.1. Policies applied to the contract awarded

Policies related to a contract may seek merely to ensure compliance with the law, for example health and safety laws. They can also go beyond those provided by the law, such as the employment of disabled people, that IT equipment in offices and libraries should be accessible to disabled users, electricity from renewable sources, etc.

The risks include the impact on the production of goods supplied to the government. The goods supplied may even have to be tailor-made and changes implemented

in a factory or business as a whole, which may therefore deter participation, competition and raise prices.

4.2.2. Policies applied beyond the contract awarded

Policies applied beyond the contract awarded can regulate contractors' behavior across their business activities as a whole, for example companies should not deal with undesirable countries. Another way could be to award preferences or set-asides to assist SMEs and/or those owned by disadvantaged social groups, support workshops providing employment, minority-owned businesses, etc.

This often imposes a greater burden on contractors than other policies and, as a result, greater costs in the procurement process. Higher costs for compliance with the requirements reduce the pool of contractors, as they have, for example, to change production methods. It may be difficult to apply the required changes only to workers on government contracts or apply different pay and conditions for similar work within the organization, since the same staff can work on contracts both with the government and private companies.

Costs must be weighed against benefits ([9], p. 594–617). Policies often involve paying higher prices and/or involve some adverse impact on other features of a supplier's offer, such as service quality. The benefits from social and environmental requirements raise prices and reduce competition, since some firms refrain from participation. In addition, there are costs of ensuring compliance with the contractual requirements. In general, additional costs may arise both because of the extra costs for firms of meeting these requirements and because some firms cannot meet the requirements and so cannot participate at all, which limits competition.

5. European Union and central government versus local government

The European Union and central government can have different priorities than local authorities. Local governments are squeezed between responsibilities to voters, who live and vote in their region or community, as well as for local development, and at the same time they have to comply with EU and central government policies that do not always correspond to specific local community interests.

The EU directives for public procurement based on the Treaty of Rome have, as a leading idea, a common European market. Sometimes, these policies can be difficult to carry out without hurting some, especially small, local suppliers when competition can come from international companies from any part of the EU. Even if the price and quality of the purchased goods or services is better than from the local supplier, it can result in a loss of jobs locally or even to bankruptcy. That can be a real blow to local politicians.

The increased usage of political goals included in public procurements can often result in additional administrative burden, thus, costs for the local authorities. One result could be that local procuring organizations put requirements on paper without controlling whether suppliers de facto comply with them.

The central government can use framework contracts in order to achieve a bigger impact from using public procurement for political goals. In this case, the designated central authority procures goods and services on behalf of other authorities. Local authorities and local governments can decide whether to take part in such a framework contract and just state their needs from the already procured preconditions of this contract. Sometimes it can be difficult to find the conditions that correspond to authority-specific needs. In the case of goods from rapidly advancing technologies such as mobile phones and laptops, or markets characterized by fierce competition such as the telecom market, it can sometimes be more favorable to buy from a local supplier when the need for such goods or services occurs, since new models, technical features or prices can change very rapidly and make the conditions of the framework contract obsolete.

6. Conclusions

The basis for the EU directives for public procurement can be a source of conflict in itself, as the EU directives are derived from the five pillars of the Rome Treatise. These pillars are the basis for the EU common market and none of them directly deals with public procurement. The EU directives, and hence also national public procurement laws, are there in order to fulfill the political goals of the common European market, which can be in conflict with the economic and/or political responsibilities of local authorities in member states.

There is a tendency to include more and more political goals in public procurement directives, as well as in national laws. This can be beneficial on some levels and for specifically favored groups. However, at the same time, it can create conflicts of interests with other levels, as in the case of procurement by specific agencies.

In general, each new goal carries extra costs and may limit competition which can raise prices. As a result, public agencies can get less favorable deals compared with the private sector.

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