



How to Implement Economic Reforms

How to Fight Corruption Effectively in Public Procurement in SEE Countries

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Foreword

At a meeting in Paris on 02 April 2007, the governments of South East Europe (SEE) launched the SEE Investment Committee (SEE IC) to help design and implement priority reforms to improve the business climate in the region. Based on the results of the Investment Reform Index 2006, SEE governments agreed to launch four Working Groups:

- *Investment Promotion (Chair: Bulgaria)*
- *Human Capital (Chair: Croatia)*
- *Anti-Corruption (Chair: Romania)*
- *Regulatory Reform (Chair: Serbia)*

Each Working Group has a mandate to elaborate “how to” guidelines for implementation of reform in the targeted priority areas.

In preparation for the 1st meeting of the Working Group on Public Procurement to be held on 11 September 2007 in Bucharest, the following concept paper outlines an approach on how to fight corruption in public procurement.

1. Introduction

Public procurement plays a major role in the world’s economic activities. It accounts for 15% of GDP in OECD countries, and in many non-OECD member countries this percentage is even higher.¹ Contracts for public works can comprise large and long-term infrastructure contracts, such as building utilities, roads and facilities in the health sector, but also smaller and shorter contracts such as supplying public institutions with goods and materials. Given the extent and complexity of public procurement, the sector is particularly vulnerable to corruption.

2. The link between public procurement and corruption

A transparent and effective public procurement system is important to combat bribery and corruption. Malpractices and fraud in public procurement deter both domestic and foreign investors. Clear rules and practices need to be established and communicated to all stakeholders. These rules then need to be enforced. However, public procurement systems are not designed per se to fight corruption. In addition, bribery in public procurement may be hard to detect due to the size, number and complexity of transactions. Therefore, in addition to an effective and transparent

¹ OECD (2007), *Bribery in Public Procurement: Methods, Actors and Counter-Measures*, Paris.

system, special tools and mechanisms need to be established to fight corrupt behaviour in public procurement.

The link between public procurement and corruption has already been extensively researched by international, regional and non-governmental organisations. The OECD recently published *Fighting Corruption and Promoting Integrity in Public Procurement* (2006)² and *Integrity in Public Procurement, Good Practice from A to Z* (2007).³ Other OECD studies include *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Procurement: Possibilities and Limitations*, which seeks to identify the way in which opportunities for corruption arise in the context of procurement, and *Good Governance for Public Procurement: Linking Islands of Integrity* which attempts to present the arguments and the methods for procurement control at the institutional design and legislative levels.

The OECD Anti-corruption division (Directorate for Financial and Enterprise Affairs) has also published extensively on the link between corruption and public procurement. For example, *Bribery in Public Procurement: Methods, Actors and Counter-Measures* offers insights into the prevention, detection and sanctioning of bribery. *Curbing Corruption in Public Procurement in Asia and the Pacific*, conducted in collaboration with the Asian Development bank, includes country assessments and an inventory of measures for curbing corruption in public procurement.

Other international organisations such as the World Bank and GRECO have also reviewed and assessed public procurement systems and corruption. Non-governmental organisations, notably of Transparency International (TI), have also been active. TI publishes a Handbook on Curbing Corruption in Public Procurement. Public procurement systems as a whole have also been extensively reviewed by the OECD and other organisations.⁴

Despite the literature linking public procurement to corruption, the policy recommendations from existing publications have not always been adapted to the varying situations of target countries. For example, some countries might be missing important pieces of legislation related to sanctions and penalties while others may have a sound legal and institutional framework but lack the control systems and trained personnel to effectively detect corruption. Furthermore, generic good practices to fight corruption in public procurement could, through inputs from local experts, be adapted to the specific regional and cultural context of different countries.

² In 2004, the OECD organised the Global Forum “Governance, Fighting Corruption and Promoting Integrity in Public Procurement”. In 2006, it organised the symposium “Mapping Out Good Practices for Integrity and Corruption Resistance in Public Procurement”.

³ This study is based on the information collected at the above mentioned symposium and maps out successful measures for enhancing integrity in public procurement.

⁴ For example, SIGMA (Support for Improvement in Governance and Management) has conducted various assessments of public procurement systems of South East European countries and has in addition analysed the review and remedy systems in the European Union: SIGMA (2007), *Public Procurement Review and Remedies Systems in the European Union*, SIGMA Working Paper No. 41, Paris; The OECD Development Assistance Committee has, in collaboration with the World Bank, developed guidelines on strengthening procurement capacities in developing countries: OECD (2005), DAC Guidelines and Reference Series, *Harmonising Donor Practices for Effective Aid Delivery, Volume 3: Strengthening Procurement Practices in Developing Countries*, Paris.

3. Objectives

The objective of this concept paper is to outline a set of practical guidelines for policy makers on how to implement anti-corruption measures in the most vulnerable areas of public procurement. The proposed guidelines will offer policy makers practical advice adapted to the specific context of SEE countries.

Responding to a specific request from SEE countries made through the SEE IC, the guidelines will:

- *Be user-friendly* - They will be based on a practical step-by-step approach adapted to officials with still limited experience.
- *Incorporate strong input from the region* - They will be developed in close co-operation with experts from the region to ensure maximum relevance and impact. Development in a regional context ensures that lessons learned from countries with similar historical and regional experience are distilled to the benefit of all participants.
- *Build capacity progressively* - They will ensure a progressive transfer of expertise to support the implementation of recommended measures.
- *Respond to a specific request for practical support* - SEE countries have expressed a need for practical guidelines on how to implement specific policy priorities

4. Key success factors

Several key success factors are required to fight corruption in public procurement. The OECD's *Bribery in Public Procurement: Methods, Actors and Counter-Measures* highlights three factors in particular.

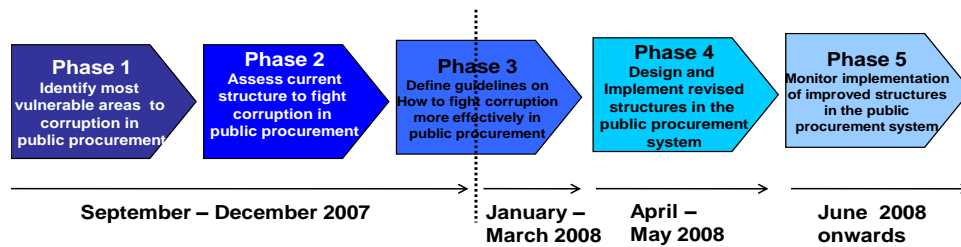
1. Design and implement the right procurement and anti-corruption legislations. To enhance enforcement, clear rules on sanctions and penalties are crucial.
2. Develop networks of experts with judicial and technical skills to improve prevention and detection within public procurement administration.
3. Generate awareness building among staff of procurement administrations and society (private sector) of the effects of bribery and how to apply procurement rules and control mechanisms.

In addition, transparency, accountability, control and professionalism are key factors in promoting integrity and fight corruption in public procurement.

5. Approach

The design and implementation of a policy to detect and prevent corruption in public procurement can be structured around five phases.

Figure 1 - Five phases of setting up structures to fight corruption in public procurement

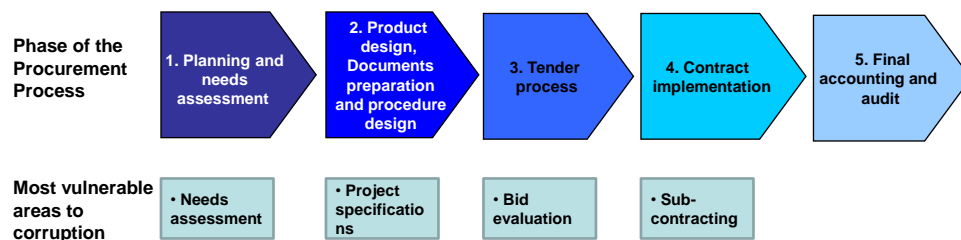


Phase 1: Identify the most vulnerable areas to corruption in public procurement and review good practice cases⁵

Procurement process and areas of risk

The procurement process can be divided in the five following phases: (i) procurement planning and needs assessment, (ii) product design and document preparation, (iii) tender process (including advertising, invitation to bid, prequalification, bid evaluation, post qualification), (iv) contract award and implementation, and (v) final accounting and audit. The risk of corruption exists at every stage of the process.

Figure 2 - Phases of public procurement process and vulnerable areas to corruption



The major risk of corruption comes from a lack of transparency, limited access to information and lack of accountability and control at each stage of the procurement process. Collusion is frequent during the phases of procurement planning and document preparation, when investigations are most difficult. Conversely, corruption is most easily detected and investigated during the phase of contract implementation. An area with particular high risk for corruption is sub-contracting

⁵ This section is based on: OECD (2007), *Bribery in Public Procurement: Methods, Actors and Counter-Measures*, Paris; OECD (2007), *Integrity in Public Procurement, Good Practice from A to Z*, Paris; OECD (2005), *Fighting Corruption and Promoting Integrity in Public Procurement*, Paris; Transparency International (2006), *Handbook for Curbing Corruption in Public Procurement*, Berlin; OECD Global Forum on Governance: *Fighting Corruption and Promoting Integrity in Public Procurement*, November 2004; OECD Symposium on Mapping Out Good Practices for Integrity and Corruption Resistance in Public Procurement, November 2006.

during contract execution. Other vulnerable areas to corruption are the phases of needs assessment, project specifications and bid evaluation.⁶

Examples of typical corruption risks at each stage of the public procurement process are listed below.⁷

1. Planning and needs assessment

- The project/purchase is not necessary or is unjustified.
- Manipulation of needs assessment (e.g. investment is unnecessary, goods and services are overestimated).
- Exchanges between project designers and intermediaries can lead to the disclosure of confidential information and the introduction of false or policy and technical requirements that are not needed.

2. Product design, documents preparation and process design

- Manipulation of terms of reference and technical specifications to favour a particular supplier.
- Unnecessarily complicated tender documents to hide corruption.
- Abuse of exceptions to open and competitive bidding procedures.

3. Tender process

- Lack of competition or collusive bidding.
- Conflict of interest situation at the evaluation process.
- Design and application of selection criteria to evaluate tenders (e.g. they are not made public or are designed to favour a certain bidder).
- Inconsistent access to information for bidders in the invitation to bid.
- Dissemination of confidential information before the submission of the bid.

4. Contract implementation.

- Performance of contract is not within the scope of the public procurement procedure.
- Lack of supervision of contract execution which can lead to change of orders, substitution of products or false accounting among others.
- Officials monitoring the contract are not independent.
- Lack of accountability of sub-contractors.

5. Final accounting and audit.

⁶ See for example OECD (2007), *Integrity in Public Procurement*, pp. 21-27; TI (2006), *Handbook*, pp. 17-20; Sacerdoti, G. (2005), "Main Findings of the Forum Workshop 'Identifying Risks in the Bidding Process to Prevent and Sanction Corruption in Public Procurement'", *Fighting Corruption and Promoting Integrity in Public Procurement*, OECD, Paris, pp. 155-156.

⁷ For a more exhaustive list please see OECD (2007), *Integrity in Public Procurement, Good Practice from A to Z*, Paris; Transparency International (2006), *Handbook for Curbing Corruption in Public Procurement*, Berlin.

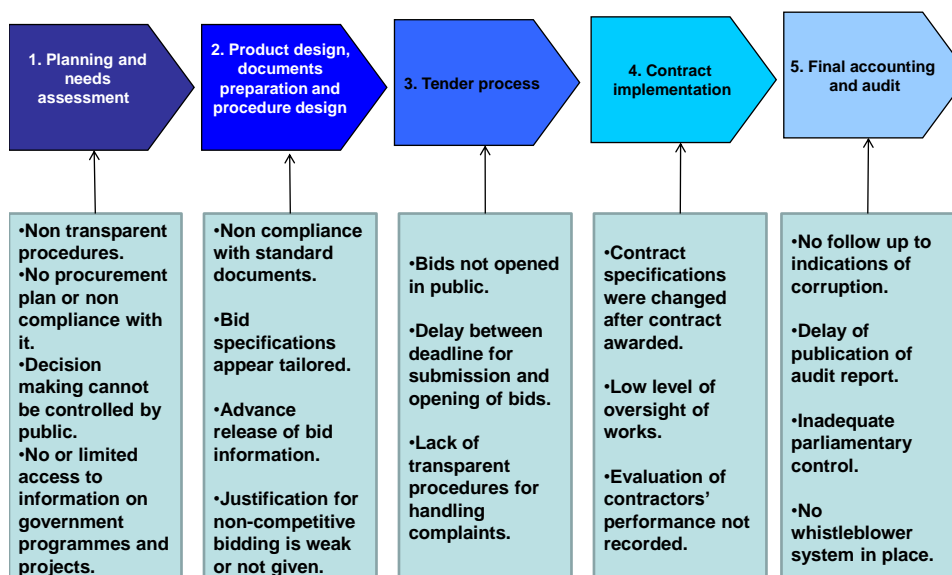
- Audits are not regularly and systematically performed which makes it harder to detect corruption.
- Structures for audit are not independent and reporting mechanisms are not clear.
- Lack of co-operation with other relevant agencies and institutions to ensure transparent and effective flow of information necessary for the audit.

These different risks of corruption in public procurement can be difficult to detect. Corruption indicators, or so called “red flags”, can function as warning signals of corruption.

Red flag indicators

Red flag indicators help to identify corruption by focusing on weaknesses embedded in the procurement system that can be easily identified. For example, no procurement plan in stage 1 (Planning and needs assessment) is a first red flag to look for. Other red flag examples include the advance release of bid information and the absence of a whistleblower system.

Figure 5. Typical red flag indicators at each stage of procurement⁸



Good practice cases

Good practice cases on fighting corruption in public procurement will be presented at the first meeting of the Working Group. Based on these presentations and other examples, good practices for fighting corruption in public procurement will be developed. SEE countries' current structure of public procurement systems to fight corruption will be reviewed in light of those best practices.

Policy response⁹

⁸ For a more exhaustive list see Transparency International (2006), *Handbook for Curbing Corruption in Public Procurement*, Berlin.

Policy makers can respond to risks of corruption in general by ensuring a good public procurement system (see Annex). A good public procurement system that can effectively prevent corruption needs to be transparent and provide for accountability and integrity. In addition, it needs to ensure effective control and complaints and review mechanisms, to ensure that decisions conform to procedures and laws. Moreover, a number of integrity and anti-corruption measures and provisions specifically aiming to detect and prevent corruption, and which can serve as useful tools to fight corruption along the whole procurement process, should be embedded in the public procurement system.

Sound legal and institutional framework

A comprehensive legal framework covering the whole public procurement process and all entities involved in procurement, is a precondition for transparent public procurement. Secondary legislation and regulations should define standard tender documents and guide contracting authorities in applying the assessment and in completing and processing tender documents. Furthermore, anti-corruption provisions in the public procurement law (e.g. blacklisting of companies previously involved in corruption) contribute to enhance the transparency and integrity of public procurement. Conflict of interest provisions for civil servants in the public procurement law or other legislation related to public administration and public service are also important measures to detect and prevent corruption. In addition, a sound institutional framework is important, providing for a well functioning public procurement office with clear responsibilities.

Control systems¹⁰

Control systems play an important role in enhancing the accountability and transparency of a public procurement system and hence in detecting and preventing corruption. They should include adequate independent internal and external control and audit with a clear coordination of all control mechanisms. Internal control comprises the organisational structure on one side and the verification of the procurement process on the other. Control mechanisms can include internal audits, financial risk analysis, management control systems and performance audit and external financial audits.

Complaints and review mechanisms

Complaints and appeal mechanisms give companies the chance to protest in case of violations. However, these mechanisms can be misused by suppliers simply filing complaints to distort the process. Therefore, clear rules on the effect of filing a protest should be defined. Effective control and review systems and measures increase transparency and play an important role in preventing corruption.

Sanctions

Warning systems and effective sanctioning systems should be included in a good public procurement system that effectively fights corruption.

⁹ For a more extensive inventory of measures to fight corruption, see ADB/OECD (2006), *Curbing Corruption in Public Procurement in Asia and the Pacific*, Manila.

¹⁰ See OECD (2007), *Bribery in Public Procurement*, chapter 7 and Sacerdoti, G. (2005), “Main Findings of the Forum Workshop ‘Identifying Risks in the Bidding Process to Prevent and Sanction Corruption in Public Procurement’”, *Fighting Corruption and Promoting Integrity in Public Procurement*, OECD, Paris, pp. 153- 160.

Professionalism/Training

The training of public procurement officials and other stakeholders is fundamental. Training should not only include the correct application of rules and procedures, but also obligations, awareness raising on how to identify corruption risks, and means to enhance integrity and effectiveness. In addition, a code of standards for public servants and suppliers/contractors, and reporting obligations of alleged misdeed by public officials, should be made standard.

E-procurement

Public procurement via the internet has been adopted by an increasing number of countries in recent years. E-procurement increases transparency, efficiency and lowers costs. E-procurement also increases competition by simplifying access to information and to the bidding process, which is especially important for SMEs. Reduced personal contact between public procurement officials and bidders also contributes to preventing corrupt behavior.

Table 1 - Policy responses at each public procurement phase¹¹

Public Procurement Phases	Broad policy responses	Specific policy responses
Planning and needs assessment phase	<ul style="list-style-type: none">• Annual needs identification and assessment• Annual procurement plan	<ul style="list-style-type: none">• Civil society participation at stage of planning through public hearings• If applicable, only independent consultants and hired in transparent manner to prepare needs assessment
Product design, documents preparation and procedure design	<ul style="list-style-type: none">• Clear and reliable regulations and proceedings regarding civil servants• Oversight mechanisms	<ul style="list-style-type: none">• Public hearings to discuss the design of the project• Conflict of interest register for officials to manage possible conflicts of interest• Competitive bidding• Standard tender documents• Specific anti-corruption clauses in tender documents• Financial disclosures requirements for procurement officers
Tender process	<ul style="list-style-type: none">• Secure, accessible and confidential system for reporting frauds, corruption or unethical behaviour• E-procurement system if necessary infrastructure and regulatory framework are given	<ul style="list-style-type: none">• Provision of anti-corruption proofs for companies, e.g. due diligence and/or compliance structures inside their corporate structures, declaration of integrity and refusal to use corrupt methods, declaration to extend its anti-corruption provisions to its suppliers• Comprehensive procurement

¹¹ For a more exhaustive list see OECD (2007), *Bribery in Public Procurement*; OECD (2007), *Integrity in Public Procurement*; Transparency International (2006).

	<ul style="list-style-type: none"> • Complaints and review system and mechanisms 	<p>manuals for suppliers and procurement officers</p> <ul style="list-style-type: none"> • Easy access to information for all bidders (questions and answers) during the bidding clarification phase • Public opening of bids and immediate registration of content • Dispersing authorities, e.g. establishing of tender committees to evaluate tenders and make award decision • Staff rotation in key positions • “Four-eyes” principle • Documentation of tendering process • Publication of evaluation criteria, evaluation process and award decision
Contract implementation	<ul style="list-style-type: none"> • Clear and pre-established limits for contract change orders • Independent monitoring system to check contract implementation 	<ul style="list-style-type: none"> • Use of standard contract specifications and conditions • Random-on-site checks of works
Final auditing and accounting	<ul style="list-style-type: none"> • Internal (including financial and operational audit) and • external audit (including performance audit) 	<ul style="list-style-type: none"> • Internal control report drafted by a controller • Internal audit and control manual • Publication of external audit reports • Co-operation of external auditor with other relevant agencies to ensure effectiveness and exchange of information • Clear reporting channels

Table 2 - Policy responses along the whole public procurement process

	Planning and needs assessment phase	Product design, documents preparation and procedure design	Tender process	Contract implementation	Final auditing and accounting
Policy responses	<ul style="list-style-type: none"> • Internal control (e.g. management control system which can be ex post evaluation but also ex ante) • External control through public oversight bodies, parliamentary controls, direct social controls (NGOs) • Separation of functions to avoid multiple performance of decisions/tasks by the same officials • Training of staff • Sanctions systems (e.g. liability for legal persons) • Whistleblower mechanism • Hotline to report violation of laws • Ombudsman 				

Phase 2: Assess structure to fight corruption in public procurement¹²

Following Phase 1, each SEE country will assess its current system of fighting corruption in public procurement.

Phase 3: Define guidelines on how to fight corruption more effectively in public procurement

Based on the two previous phases, Phase 3 will develop practical guidelines on how to implement effective measures to prevent and fight corruption in SEE countries.

Phase 4: Design and implement revised structures adapted to the specific country context

Once the practical guidelines to fight corruption in public procurement have been published, each country can adapt the guidelines to its specific context. The Working Group experts will define an action plan for each country.

Phase 5: Monitor implementation of improved structures and provisions in public procurement system

- Monitor and review the revised structures and provisions to fight corruption based on indicators defined in the “how to” guidelines in Phase 3.
- Improve the system on a continuing basis through periodic monitoring and feedback reports.

¹² The assessment will be conducted based on the excellent work done by SIGMA of public procurement systems assessment in South East European countries.

Annex

The five levels of a successful public procurement system¹³

A good public procurement system, which is the precondition to fighting corruption, comprises five levels.

1. Public Procurement Law

- Compliance with international standards (UNCITRAL Model, WTO Government Procurement Agreement (GPA), European Directives)
- Conflict of Interest provision
For example: 1. The definition of a conflict of interest is in line with OECD Guidelines. 2. Civil Servants are required to make decisions without regard to their personal interest. 3. They must declare all relevant private interests that potentially conflict with official duty when they take office. 4. They must subsequently notify the appropriate body when any changes lead to a new emergent conflict of interest situation.
- Secondary legislation/regulations define standard tender documents and guide contracting authorities in applying the assessment and in completing and processing tender documents (operational guidance)

2. Public Procurement Office and Practice

- Location of the office in the government system, its accountability and structure; rights, resources and tasks
- Public notice and transparency

3. Accountability and control mechanisms in the public procurement office and in procuring agencies

- Internal audit
- Internal control mechanisms
- External audit
- Other external controls: public oversight bodies; parliamentary controls
- Mechanisms to control: who is controlling the procurement procedures and how? What is the mechanism to control post-bidding stages and due diligence in the execution of public contracts?

4. Complaints review process

- Complaints review office (independent/separate from PPO)
- Complaints process and sanctions

5. Training

- Training (availability, frequency)
- Content of training (are procurement officials being taught their obligations, the corruption risks and means to enhance integrity and effectiveness of procurement)
- Target groups of training

¹³ This structure is based on the various publications cited throughout this paper and input from the Anti-corruption Division of the OECD Directorate for Financial and Enterprise Affairs.

Figure 1 - Elements of a good public procurement system to promote integrity and support fighting corruption

