

CORRUPTION IN PROCUREMENT

TERMPAPER

MCS 8303:Business Ethics and Governance

60473

Charity Wairimu Muriithi

4/6/2011

INTRODUCTION

An organization seeking to acquire goods and services for its day to day running is likely use a purchasing process that has end-to-end stages of the purchasing activity through its procurement department. The stages consist of defining requirements; specification; make or buy decisions; source identification; source selection; contracting; receipt and payment; contract management; consumption; and decomposition and disposal.

At the make or buy stage, a critical choice has to be made in regards to the competencies of the organization and the market. The 'make' decision involves the organization fulfilling the need internally while the 'buy' decision requires the organization to purchase from a third party.

If the organization chooses the 'buy' decision, it then goes to the source identification stage in order to identify suitable and appropriate sources of supply that will fulfill the acceptance criteria of the requirements. This may involve tendering, desk research, word of mouth and expression of interest in order to establish a body of competitive suppliers with which to create a competitive bidding.

This paper will focus mainly on the tendering process and on the ethical issues arising while procuring goods for institutions. For that purpose it is necessary to understand the tendering process.

The Tender Process

Some terms necessary to be understood in regard to this paper are:

Invitation to tender – this is a document or a set of documents that are sent to all firms selected to bid for a contract, or all firms replying to an open invitation. (Purchasing Context, 2006)

Tender – is the response from a supplier to an Invitation to Tender. (Purchasing Context, 2006)

The tender process begins with drawing up documentation that clarifies the requirements of the buyer.

Typically tender documents should include:

- The specification of materials, services or equipment required
- A description of the relationship expected with the supplier
- The proposed terms and conditions of the future contract
- A general description of the tender evaluation criteria
- Details of instructions, deadlines, the contact points and associated procedures that the tenderers must follow
- A request to confirm the tenderers' intention to tender.

Next, potential bidders are invited to submit an 'expression of interest' by advertising the opportunity. This enables the buyer to get a list of pre-qualified suppliers who will receive an invitation to tender. The invitation to tender will contain instructions to the tenderers about the procedures to be followed and the scope or specifications of the goods and services required.

During the tender period, sometimes further information may be made known to the tenderers to help them prepare their bids. New information should be sent to each tenderer in writing to avoid misunderstanding or misinterpretation and information should be sent at the same time to all tenderers to give equal consideration to all parties.

Once the tenders have been received, the buyer evaluates the tender submissions and ranks the bids. This is done in the presence of other business stakeholders and based on aspects that include cost, service, quality, delivery and innovation.

Top tenderers are then invited to discuss the bids and seek further clarification. Further negotiations can take place to change aspects of the supplier's bid. Finally, the contract is awarded either on the face value of the terms and conditions outlined in the suppliers tender or with amended documentation if any arose during the post-tender negotiations (PTN).

PROBLEM STATEMENT

Corruption is a rampant predicament facing Kenya as a country. It has and still is affecting most government institutions and large organizations at various levels of operations. One of the most affected areas is procurement. Institutions are meant to follow laid down procurement procedures in acquiring goods and services but they never completely follow them thus, they take unethical turns in their day to day running.

This paper will look into various stages in the tender procedure that provide leeway to corrupt circumstances to arise and the ethical problems that arise thereof.

PRESENTATION OF THE CASE

Early this year, a Kenyan parastatal was accused of having irregularities in their tender issue. It had inflated prices for goods and had awarded the contract to the highest bidder amongst other irregularities. (Daily Nation Newspaper, February 3 2011)

Last year, various cases arose in regards to sealing loopholes in the Public Procurement and Disposal Act 2005. The Act was termed a fallacy and heavily flawed and needs an open examination by patriotic Kenyans to seal all gaping corruption loopholes. (Daily Nation Newspaper, November 6 2010)

Also during the 23rd meeting of the National Economic and Social Council (NESC), it was brought out that the existing procurement rules and regulations had not been able to tackle corruption despite them being imposed on Kenya when corruption was at a high level. (Daily Nation Newspaper, November 19 2010)

All the above goes to illustrate that corruption in procurement is an existing issue that should be tackled.

ETHICAL PROBLEM

Corruption is defined as dishonest or fraudulent conduct by those in power, typically involving bribery. (Oxford dictionary)

Common Types of Public Procurement Corruption

Procurement corruption can take place at every stage in the contracting process. Corrupt agents can inflate demand or create artificial demand for goods and services. Agents may also distort the allocation of scarce budgetary resources for purchasing these goods or services.

At the tendering stage corruption can include tailoring specifications to restrict competition, restricted publicity, abuse of confidentiality, bid rigging, and rejection of bids on frivolous grounds.

At the post-tendering stage offers opportunities for abuse of authority for example the post-tender alteration of contract conditions, acceptance of inferior goods or services, and the waiver of penalties. In many cases, the supplier deliberately provides inferior-quality goods in order to offset the extra costs incurred due to bribery.

The types of corruption in procurement can be grouped as follows:

- i. Influence on tenders – here, strategies verge on corruption when representatives of the customers are offered benefits of significant personal value, such as business excursions and tickets to events to which job contacts are also invited. Also some firms are frequently asked to advise clients on technical aspects of tender specifications, even if they are among the competitors for the contract ending up benefiting the firm itself or one of its associates.
- ii. Predetermination of contracts – here contracts are designed to fit the offer of one specific tenderer. The technical tender procedure may appear correct on the surface even though the qualifications have been set to give an advantage to a particular company. This firm will thus offer the lowest price, and the formal procedures appear satisfactory. Such bid rigging will often affect the choice of technology, a choice that typically has more consequences the larger the project. The choice of technology will, for instance, often directly affect what subcontractors are used.

iii. Tender rules – it could be thought that tenders rules should be flawless in a bid to prevent instances of corruption but pre-selection and pre-tender contact cast doubt on the efficiency of tender rules in controlling corruption. Procurement rules are important, though not in itself a good anti-corruption tool. To some extent tender rules may function as an obstacle.

iv. Rules of communication – rules of communication are often neglected in tender procedures. Although access to information and transparency are important to ensuring fair competition, it is crucial to keep critical information about the bids as secret as possible. Communication rules are supposed to prevent the distribution of such critical information, which for obvious reasons is a frequent object of bribery.

A central element in most formal tender rules is the way the contact between client and bidders should take place once the tender process has started. At this stage, the rules often require that communication between one firm and the client is copied to all tenderers. These factors, however, will also make it easier to cover up corruption.

v. Diplomatic pressure – the tenders on big contracts is sometimes affected ‘from above’ by diplomatic pressure to the benefit of one specific firm, specifically when the client is a foreign government. The pressure may take the form of a subsidy, such as an export credit deal, aid to the buyer linked formally or informally to the purchase, commercial pricing issues, impediments to trade, or tied defense/arms deals. This kind of pressure may reduce the prospect of ending up with the most beneficial outcome to the host country’s citizens. The link to corruption becomes clear when the selected firm has paid its own government to put pressure on the client.

Quid pro quo is a different form of political pressure, still connected to big contracts, but now instigated by the client government. It refers to a reciprocal exchange in which the chosen firm provides benefits for local governments and their constituents. For example, a multinational firm may promise to build a school or infrastructure, or to use local human resources during their operations in the given country. Local content demands are clearly more common in tenders by

the large firms, compared to small- and middle-sized ones, and appears - from this material – more common in construction and oil, gas and power transmission than in other sectors.

Large firms unlike small firms are better able to influence tender specifications, are more likely to suspect tender results to be pre-determined, have a lower trust in procurement procedures' ability to prevent corruption, are more likely to find the competition in their own industry 'biased, more often believe that diplomatic pressure has an influence on the competition and are more often asked for quid pro quos.

ANALYSIS

Some principles of corporate governance are violated by institutions that carry out corruption in the procurement process. These principles are as follows:

Subsidiarity

The principle of subsidiarity holds that a larger and greater body should not exercise functions which can be carried out efficiently by one smaller and lesser, but rather the former should support the latter and help to coordinate its activity with the activities of the whole community. (Domènec, M.C., 2004)

From the definition of corruption, we see it as a dishonest or fraudulent conduct by those in power. Those in power will indulge in acts such as bribery in order to get what they desire irrespective of other individuals, or in this case, other businesses.

Between large and small organizations, it is obvious that the large organizations have power to manipulate decisions, tender wisely, than small organizations. That is the actual state in most institutions today. We see that large corporations are still those that are able to be awarded tenders since they are able to bribe and are able to manipulate tender requirements to fit themselves. These corporations end up getting opportunities to supply goods and services which a small organization is capable of supplying but is underpinned by its lack of 'power'.

If corruption was nonexistent in tendering, and the principle of subsidiarity was actualized, it is possible that small organizations would have a fair competing ground for business and would be able to win tenders. On the other hand, large corporations would also benefit since they would also get tenders that suit their large capability resulting in a win-win situation.

Virtues

Another area affected by the issue of corruption in procurement is virtues.

Virtue means behavior showing high moral standards. (Oxford Dictionary) Vice, the opposite of virtue, means an immoral or wicked characteristic. (Oxford Dictionary) Virtues and vices are habits, tendencies or dispositions to do good or bad.

From the definition of corruption, we see it as a dishonest and fraudulent action that qualifies as a vice since the acts that are done are bad.

Corporations should exercise virtues in their day to day running of the organization. One such value is prudence which is the right reason in action. An organization should exercise prudence by not accepting bribes of any form or going against procurement rules for their own personal gain. But the gain they should aim for is one that maximizes value for the shareholder.

Justice, being the constant will to give each one his or her fair due should also be exercised. When justice is done by the organization, this will mean that contracts will be awarded to deserving individuals or institutions. It will also mean that there will be no bribery, communication rules are followed giving all tender participants fair ground to win contracts.

Greed, defined as intense selfish desire for something, is an element that leads to corruption. Powerful organizations engage in corrupt acts in order to gain more for themselves instead of other organizations who want to achieve their goals in an honorable manner.

CONCLUSION

Collusion between an institution responsible for making a purchase decision and a supplier exists at every stage of contracting. In order to rid the process of corruption therefore, we should aim at controlling the behavior of the employees as well as the supplier firm.

First, we need to reduce rent seeking opportunities. Measures that can be undertaken include the creation of procurement legislation or rules, transparent procedures, and strong and independent audit institutions. Information irregularity can be reduced by strengthening oversight institutions, the media, and civil society. Additionally, the behavior of corrupt public servants can be controlled by strict enforcement of ethical codes of conduct and by criminal sanctions against bribe-taking.

A second measure involves controlling supply-side behavior. This approach includes enforcement methods like debarments, penalties, criminal sanctions on bribe payers, or by developing ethical codes of conduct and other self-regulation mechanisms. While these steps are often sufficient for combating corruption where both the purchaser and seller are from the same country, they typically fail when the buyer and supplier are from different countries.

With these measures in mind, some effort will be put into controlling corruption in procurement transactions.

REFERENCES

- Domènec, M.C. (2004), The principle of subsidiarity in organizations. A case study, IESE
- Erridge, A., & Nondi, R. (1994). Public procurement, competition and partnership. *European Journal of Purchasing & Supply Management*, 1(3), 169–179.
- Kenya Gazette Supplement No. 24The exchequer and audit (public procurement), regulations, 2001.* (2001). Government Printer.
- Kiplagat, S. (2009). *Grey areas dot the procurement act*. Nation Media Group.
- Menya, W. (2010, November 19). Raila wants procurement laws reviewed. *The Daily Nation*
- Ngirachu, J. (2011, February 3). Agency faults water board over tenders. *The Daily Nation*
- Ombaba, G. (2010, November 6). Seal loopholes in procurement rules to win war on corruption. *The Daily Nation*
- Oxford Dictionary
- Pidaparthy, V. R. S. (2005). Supply side issues in procurement corruption: is the developed world responding adequately to the needs of the developing world? *Journal of Development and Social Transformation*, 2, 109–116.
- Purchasing context, (1st Ed.). (2006).CIPS course book, CIPS
- S\oreide, T. (2005). Corruption in public procurement. *Fighting Corruption and Promoting Integrity in Public Procurement*.
- S\oreide, T. (2006). Procurement procedures and the size of firms in infrastructure contracts. *The World Bank Annual Conference on Development Economics, ABCDE, Tokyo* (p. 29–30).
- Smyth, H. (1999). Partnering: practical problems and conceptual limits to relationship marketing. *International Journal for Construction Marketing*, 1(2), 12–23.
- Soreide, T. (2006). Tender manipulation: large firms and infrastructure contracts. *Public Procurement Conference, Rome, September* (p. 22–24).

Strathmore University Library Catalog › Details for: The connected corporation: how leading companies win through customer-supplier alliances (n.d.) Retrieved March 16, 2011a, from <http://opac.library.strathmore.edu/cgi-bin/koha/opac-detail.pl?biblionumber=26870>

Strathmore University Library Catalog › Details for: The connected corporation: how leading companies win through customer-supplier alliances (n.d.) Retrieved March 16, 2011b, from <http://opac.library.strathmore.edu/cgi-bin/koha/opac-detail.pl?biblionumber=26870>

Walker, D. H. T. (2003). *Procurement strategies a relationship-based approach* /. Blackwell Science.