

## **BUYING POWER: AID, GOVERNANCE AND PUBLIC PROCUREMENT**

### **SYNOPSIS**

This South Centre Analytical Note looks at the donor-driven agenda in the reform of public procurement – the rules that guide government purchasing of goods, works and services – as one of major components in the good governance agenda being incorporated by donors into their aid programmes. This Analytical Note stresses that such an agenda vis-à-vis government procurement not only restricts the flexibility of developing country governments to use public procurement as a policy tool for development, but also has significant consequences for local firms that rely on government contracts. It stresses that aid-driven reforms in public procurement must be linked to the broader aid effectiveness and development discourse, and that such discourse must result in enabling aid receiving developing countries to move out of aid dependence.

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## **BUYING POWER: AID, GOVERNANCE AND PUBLIC PROCUREMENT**

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## EXECUTIVE SUMMARY

It sounds very administrative and technical, but reform of government procurement – the rules that guide government purchasing of goods, works and services – is one of the most controversial aspects of the “good governance” agenda that is most often pushed by Northern donors and multilateral lending institutions (such as the World Bank). Donors have two goals: *greater accountability and transparency*, which is limited because of its reliance on a one-size-fits-all approach; and *greater efficiency*, which is narrowly defined as value for money to be secured through open competition. This not only restricts the flexibility of developing country governments to use public procurement as a policy tool for development, it can also have significant consequences for local firms that rely on government contracts.

### Government procurement matters

The rules guiding government purchasing and contracting need to be accountable and transparent. This is not only to limit corruption – a central concern with regard to public procurement – but to contribute to a more accountable relationship between a government and its citizens. It is also important because of the sums involved. In the Dominican Republic, 20 per cent of government expenditure is spent on procuring goods and services; in Malawi and Vietnam it is 40 per cent; and in Uganda as much as 70 per cent.\*

Government procurement accounts for approximately 4.5 per cent of developing countries’ gross domestic product (GDP) and governments tend to be the largest single consumers of goods and services in most countries. A government’s use of purchasing can thus be a very significant tool to achieve socio-economic objectives.

If public procurement reform is done accountably, with a view to achieving both cost-effectiveness and broader development goals, it can play a powerful role in poverty reduction.

Concern that aid money could be wasted or even fraudulently used is the primary concern for donor engagement in public procurement. This is increasingly the case as donors shift to using budget support, where aid is given centrally to fund a government’s entire development strategy

However, while pursuing public procurement reform through aid strategies, donor countries are also pursuing liberalisation of public procurement markets in trade negotiations\*\*. Globally, government procurement is big business, with government annual spending on tradable goods and services estimated at more than US\$2,000 billion. Government procurement is seen as the most significant trade sector excluded from multilateral processes.

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\* OECD, *Why is Procurement Important?: Factsheet*, December 2006

\*\* Note that the liberalization of public procurement markets in the WTO was rejected by developing countries at the Cancun Ministerial Conference of the WTO in 2003.

## Aid effectiveness and government procurement

It is timely to raise these issues now. Not only are trade agreements requiring substantial public procurement reforms currently being agreed, but in September 2008 a meeting of development ministers will take place in Accra, Ghana to review donor commitments to improve the effectiveness of aid.

One of the main aid-effectiveness commitments is to increase the use of country systems such as those used for government procurement. Donors have pledged to stop requiring recipient governments to use different public procurement procedures for each donor – this can be difficult for countries with weak administrative capacity.

However, donors' use of national public procurement systems is, in part, linked to the degree of liberalisation of those systems. Also, according to the Paris Declaration, should aid recipients' national public procurement systems not match up to the expected standard of "broadly accepted good practice,"<sup>\*\*\*</sup> the donors can demand that model public procurement procedures such as those developed by the World Bank be adopted. Furthermore, the United States takes the position that if the World Bank procedures are below US standards or are discriminatory against US companies, then it (the US) would not follow those procedures in relation to US aid.<sup>\*\*\*\*</sup>

Another serious flaw in the donors' own procurement systems which militates against strengthening the capacity of aid recipients' country systems is the donors' continuing failure to stop aid-tying, which allows them to ensure that their own domestic firms secure aid-funded contracts.

## Findings

This Analytical Note finds donor pressure- particularly from the World Bank – to place public procurement reform is succeeding in promoting public procurement systems that effectively increase market opportunities for foreign firms.

*Governance:* There is an important role for donors in supporting the development of more accountable and transparent public procurement. However, at present donors seem to prefer a quick fix, adopting a standard public procurement law and system rather than developing a reform that can be adapted to be appropriate to each country context.

This practice has undermined the governance goal. Following complex new public procurement rules has placed a heavy burden on governments, including the major

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<sup>\*\*\*</sup> This is defined in the Paris Declaration as the use of "mutually agreed standards and processes", with the processes developed by the joint OECD-DAC – World Bank Round Table on Strengthening Procurement Capacities in Developing Countries being identified as a prime example of such mutually agreed standards and processes.

<sup>\*\*\*\*</sup> See e.g. Roberto Bissio, Paris Declaration on Aid Effectiveness - Application of the criteria for periodic evaluation of global development partnerships – as defined in Millennium Development Goal 8 – from the right to development perspective: the Paris Declaration on Aid Effectiveness, paper submitted to the UN Human Rights Council Working Group on the Right to Development (UN Doc. No. A/HRC/8/WG.2/TF/CRP.7, 31 December 2007), at <http://www2.ohchr.org/english/issues/development/docs/A-HRC-8-WG.2-TF-CRP7.doc>

spending ministries. Local governments are particularly affected most directly because they do not have access to the professionals (such as engineers and public procurement consultants) required to make public procurement decisions. Greater forethought about the constraints of government – particularly local government – at the outset would help prevent this.

*Efficiency, development and open competition:* Efficiency is defined narrowly in terms of value for money – the best quality at the lowest cost. In this view, efficiency is best secured through open competition, so public procurement reform is seen as encouraging a more liberalised market-based public procurement system.

A broader definition of efficiency that considers development gains alongside cost and quality would ensure that public procurement plays more of a role for poverty reduction. Research findings indicate that the standard model favoured by donors actually reduces the ability of developing countries to do this.

There are very real consequences to opening up government procurement markets, particularly for local firms who previously relied on government contracts. Our research finds that the tools to mitigate these effects are not prioritised by donors sufficiently to counter the constraints facing local firms.

### Recommendations

Donors can play an important role by providing long-term support to developing countries to make the rules guiding government purchasing clearer, the process more transparent and government officials more accountable. It may be necessary to link aid – and budget support in particular – to improved public procurement systems. However, the decision of whether or not to allow foreign firms to compete for particular contracts must remain the decision of recipient governments.

Aid recipients must stress to donors, and the latter should accept, that aid-promoted improvements in public procurement systems in recipient countries should:

- be limited entirely to changes that improve the accountability and transparency of government public procurement to the country's own citizens rather than to external actors
- be tailored to each individual country context, taking government capacity and the workings of its political system into consideration
- provide long-term capacity development support to recipient governments, to enable them to move out of aid dependence and promote the development of domestic supply side capacity
- result in the removal of any requirement to partially or fully open up national public procurement markets to foreign firms in return for aid or debt relief if such opening up would result in decreasing the policy space of the recipient government to promote the development of domestic supply capacity

- recognise the effectiveness of linking public procurement to development objectives by positively supporting developing countries in using government procurement flexibly to support their own economic development objectives – whether that is, for example, by directly building up the competitiveness of local firms or bringing in foreign firms in joint ventures with local firms.

Furthermore, such reforms need to be linked to changes in the overall framework and approach being used by donors for the delivery of aid. Such changes should eventually enable aid recipients to exit from reliance on aid. This means that there must be a stronger correlation between aid and genuine development impacts in the recipient country.

# BUYING POWER: AID, GOVERNANCE AND PUBLIC PROCUREMENT\*

## I. INTRODUCTION

1. Public procurement reform is a standard element in the “good governance” reform agenda of developed countries, and is generally accompanied by reforms to the civil service; legal, judicial and security sectors; revenue and budget systems; and electoral, financial and administrative decentralisation. Good governance reforms have been a priority for Northern donors since the 1990s. The number of public sector governance conditions as a percentage of overall World Bank lending conditions has increased from 17 per cent in 1995-1999 to 50 per cent in 2007.<sup>1</sup>
2. A public procurement system is a set of rules that guide a government’s purchasing of goods, works and services, however big or small. Public procurement reform seeks to guide all purchases: from a new blackboard to textbooks for schools; from getting an engineer to mend a toilet to renovating an urban water system .
3. The drive to budget support has increased attention on government procurement – particularly because it represents a large part of government budgets. If there are no rules guiding this expenditure, there is a clear risk that money will be allocated inefficiently or inappropriately (see Box 1 for an example).
4. This paper assesses public procurement reform from two perspectives. Firstly, how effectively donor-driven public procurement reform achieves its governance goals of accountability, transparency and efficiency and secondly, the links between public procurement and economic policy and some of

### Box 1 Ghana’s 50<sup>th</sup> Anniversary

In January 2007, the Ghanaian government awarded the contract to produce cloth for its 50<sup>th</sup> anniversary cloth to a Chinese, rather than a Ghanaian, firm. The story was widely covered in the Ghanaian press including *Public Agenda*, a paper founded by Christian Aid partner organisation Integrated Social Development Centre (ISODEC), questioning the rationale behind this decision.

In response, the Ghanaian government claimed that it followed the procedures laid out in its new Public Procurement Act. According to the government, local firms simply lacked the capacity to produce the volume of cloth in the time required.

Abraham Koomson, secretary general of the Ghana Federation of Labour, argued that ‘if the government had approached local firms just three months earlier, they could have come together to produce all the cloth required’.<sup>1</sup> It is notable that, despite a concerted government strategy to get the textile industry on its feet, as it struggles against low-cost imports, smuggling and an influx of second-hand clothes, the labour force has declined from 25,000 in 1977 to 7,000 in 1995 and just 2,961 by 2005.<sup>2</sup>

<sup>1</sup> Interview with Abraham Koomson, 17 July 2007

<sup>2</sup> Peter Quartey, ‘The textiles and clothing industry in Ghana’ in Herbert Jauch and Rudolf Traub-Merz (eds) *The Future of the Textile and Clothing Industry in Sub-Saharan Africa*, Friedrich-Ebert-Stiftung, 2005, p 136

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- The South Centre acknowledges the contributions of Olivia MacDonald of Christian Aid to this Analytical Note. This paper draws on the Christian Aid report of the same title published in February 2008.
  - <sup>1</sup> World Bank, *World Bank Review of Conditionality*, 2005.

the impacts that public procurement reform is having on developing countries. It is based on desk research, interviews with public procurement experts and primary research in Ghana.

## II. PUBLIC PROCUREMENT REFORM AND BETTER GOVERNANCE

*'People do not develop systems and structures based on what is possible. They don't take into account existing capacity nor invest enough in capacity building.'* Siafa Kamara, director of Christian Aid partner Social Enterprise and Development Foundation (SEND), Ghana<sup>2</sup>

5. Academics Ha-Joon Chang and Dani Rodick have both emphasised the importance of institutional development, but question the effectiveness of imposing 'best practice' institutions, which according to Chang 'usually mean Anglo-American institutions'.<sup>3</sup> Reforms need to be realistic and appropriate to the country concerned and, according to Rodick, influenced by a more experimentalist approach, 'a process of discovery about local needs and capabilities'.<sup>4</sup>
6. However, public procurement reforms being implemented across many countries are remarkably similar. This is because donors have focused on getting countries to introduce a standard law developed by the United Nations Commission on International Trade Law (UNICTRAL) and meet the indicators set out by the OECD DAC-World Bank procurement round table initiative.<sup>5</sup>
7. This section questions how far this "best practice" model brings about better governance. Although rhetorically linked to the fight against corruption, the focus is really on efficiency, and reform is frequently hampered by the failure to adapt it to the practical realities of each country context.

### A. Efficiency and local government

8. Public procurement reform is very much driven by concerns about efficiency, that existing rules were not enabling governments to get the best-quality goods and services and the best price. However, efficiency can also be looked at from another angle – the simplicity of the rules, the ease of use and cost and time implications. In Ghana, before public procurement reform there were numerous different rules in place and government officials struggled to know which ones to follow. Having one set of rules to follow, at all levels of government, is a clear improvement.

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<sup>2</sup> Interview with Siafa Kamara, 20 July 2007.

<sup>3</sup> Ha-Joon Chang, *Kicking Away the Ladder: Policies and Institutions for Economic Development in Historical Perspective*, Anthem Press, 2002.

<sup>4</sup> Dani Rodick, *Institutions for High-Quality Growth: What They Are and How to Acquire Them*, paper prepared for IMF conference, 1999.

<sup>5</sup> OECD, *Methodology for Assessment of National Procurement Systems Version 4*, 17 July 2006.

9. However, Box 2 shows that the standard public procurement model is not efficient in supporting decentralised decision making because of lack of consideration about how reform will play out at local government.
10. The new rules are also very time-consuming. Lindsey Napier, a DFID-funded policy advisor based at Ghana's Ministry of Trade, described the 'laborious nature of the procurement process and the inherent capacity needs in government that are created by adopting such a comprehensive (and bureaucratic) system.'<sup>6</sup>
11. A lack of specialist training for staff in contracting government departments means that even major ministries are often unable to process all their public procurements, or that 'the time taken to do that procurement is unacceptably long (we're talking about awarding of contracts taking over a year or so in many cases).'<sup>7</sup>
12. Finally, when thinking about efficiency, the cost implications of new cadre of public procurement specialists needs to be taken into account.<sup>8</sup> This reliance on using public procurement experts not only increases the cost implications, but can further remove decision making from a local level.

**Box 2**  
**Local government and procurement reform in Ghana**

Siafa Kamara of SEND Foundation, another Ghanaian civil society organisation that supports community budget monitoring work, believes the law is a 'good thing' because it enables citizens' groups to see how far the rules are being followed when district councils purchase goods, works or services.

However, his concerns echo those of ISODEC - another Ghanaian organisation - that many district councils are not able to create tender committee boards or tender review boards because they cannot secure professional participants (such as lawyers, MPs, procurement professionals and engineers), particularly in rural areas. When this happens, decisions are pushed up to regional or national bodies, directly contravening the drive to decentralise government as outlined in the Ghanaian constitution.

Even where bodies have been properly constituted - in cities such as the capital, Accra - the relatively low threshold on contracts worth more than US\$100,000 for goods and US\$200,000 for works mean that district-level contract decisions often go to regional or even ministerial level for approval.

Kamara argues that the procurement law has 'strengthened the status quo', because the bodies below district and municipal level - unit committees and area councils - are not allowed to do any purchasing. Yet these are the governing bodies that hold the key to people's participation; as such, resources need to be allocated to and spent at this level.

<sup>1</sup> Republic of Ghana, *Public Procurement Law 2003*

<sup>6</sup> Personal communication with Lindsey Napier, 11 October 2007.

<sup>7</sup> Ibid.

<sup>8</sup> Ha-Joon Chang argues that this money could be better spent on 'training...school teachers or industrial engineers, which may be more necessary, given their stage of development.' Ha-Joon Chang, *Kicking Away the Ladder: Policies and Institutions for Economic Development in Historical Perspective*, Anthem Press, 2002.

13. Reform will always have time and cost implications, but it is odd that an area so focused on efficiency is not more focused on adaptation to the local context. The evidence above shows that successful public procurement reform needs to consider more the country's political context and administrative capacity. This could lead to reforms that are not only more practical, but also integrate better with other goals – particularly that of increased decision making by local governments.

#### B. Fair competition and corruption

14. Public procurement reform is seen as being a core part of the aid arsenal against government corruption. The existence of one set of rules that guide all purchasing is vital for accountability – particularly among civil servants, who know that they will be scrutinised and held to account on their adherence to those rules. In Ghana, there are already examples where these rules are helping people challenge parts of the government that have not been following the laws properly.

15. Box 3 presents a useful story that challenges some of the assumptions that underpin public procurement reform – namely that with more open competition, public procurement is better value, fairer and less corrupt. But this example also shows the flaw in assuming that the participation of international firms will bring about due process. Open competition is not a guarantor of greater integrity in the public procurement system: there is a need for clear, well-publicised guidelines and punitive action when the rules are not followed.

#### C. Conclusion

16. Public procurement reform currently focuses on getting countries to implement a standard public procurement law and system. This approach is not sufficiently country-specific; it can result in reforms that are ineffective in terms of cost and time; and undermines decentralised decision making. The introduction of clear rules definitely contributes to greater integrity for government officials, who know their compliance will be scrutinised. However, it is important to

#### **Box 3 On Ghana's Book Contracts**

In October 2006, Accra's High Court found that the government had not been complying with its own new law. The Ministry of Education and Sports (MOES) did not follow the Public Procurement Act when it single-sourced Macmillan Books to supply secondary school materials worth US\$28million, nor did the Public Procurement Board (PPB) when it approved this tender.

The Ghana Book Publishers' Association took the case to court after the MOES sole-sourced this contract. The publishers managed to pull together US\$20,000 to take their case to court and in October 2006, the High Court found that MOES did not comply with section 40 of the Public Procurement Act in sole-sourcing from Macmillan Books, and the PPB had contravened the same section of the Act in approving it. The tender was then revoked.

There has been no inference of corruption, rather one of misprocurement - not following the new rules. This is an example, then, that tighter rules can help reveal cases when officials fail to play by the rules. Such high-profile cases not only act as a disincentive to corruptly award contracts, but could be used by local firms as a tool to hold government to account when the rules are not followed.

<sup>1</sup> *Judgment for suit no AP 6/2006, 'The Republic versus Ministry of Education and Sports, the Public Procurement Boards, the Get Fund Board - ex-parte Ghana Book Publishers Association', Accra High Court, 18 October 2006*

disentangle this from an assumption that participation of foreign firms brings with it greater integrity and less corruption. The next section looks at the implications of the drive for greater openness.

### III. PUBLIC PROCUREMENT REFORM AND ECONOMIC DEVELOPMENT

17. This section examines the goals that guide donors in relation to public procurement and economic development. The main stated goal is to secure greater efficiency, narrowly defined as value for money. Public procurement can be an important policy tool that governments can harness for economic development. However, the space to do so is limited, not only by trade agreements, but also through reforms driven by aid donors. This current bias can have negative consequences for local industry. Donors should instead support developing-country governments by gauging public procurement efficiency according to its development impact.

#### A. Aid and public procurement liberalisation

18. The OECD-World Bank round-table has developed indicators that guide Northern donors in their support to public procurement reform. These indicators reward non-discriminatory public procurement systems with higher scores, which in turn increase the likelihood of their receiving budget support. The sub-indicator on participation rules argues that 'as a general principle, firms, including qualified firms, should not be excluded from participating in a tendering process for reasons other than lack of qualifications', as these exclusions 'may arbitrarily limit competition and may result in inefficient procurement and higher prices.'<sup>9</sup>

19. Furthermore, the indicators reward policies that do not require foreign firms to associate with local firms or establish subsidiaries. An annexed document entitled *Good practice for national competitive bidding*, claims that it is good practice if 'any firm, national or foreign, can participate in the tendering process except if the firms are excluded by legal provisions [including convictions or UN sanctions].'<sup>10</sup>

20. They do, however, recognise potential impacts on local industry, allowing price preferences, as long as they are kept 'reasonable', at around 15 per cent. Governments are also required to assess systematic constraints that may inhibit local private-sector access to the public procurement market – such as access to credit, contracting provisions that fairly distribute risk and fair-payment provisions.

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<sup>9</sup> OECD, *Methodology for Assessment of National Procurement Systems*, Version 4, 17 July 2006.

<sup>10</sup> Ibid.

21. The World Bank used to compare national public procurement policies to its own policy (which prohibits restrictions on eligibility according to nationality amongst others) but is now working with the agreed public procurement indicators.<sup>11</sup> Because it allows for price preferences for local companies, the World Bank has not promoted complete liberalisation in public procurement. However, it has a clear bias towards open competitive tendering and bidding in national public procurement (including the participation of international tenderers or bidders as potential suppliers).<sup>12</sup>
22. However, under pressure from the World Bank, aid recipient countries remove domestic preference conditions from their public procurement processes. In Ghana, for example, the government wanted to restrict smaller projects to local firms. The World Bank asked it to omit this requirement, because limiting participation by nationality 'undermines the principle of transparency and equal opportunity and may be a cause of abuse.'<sup>13</sup> The government agreed, and national competitive bidding (advertised nationally but open to all) is now used for tenders worth more than US\$20,000 for goods and technical services and US\$50,000 for works. The 2003 Public Procurement Act in Ghana does not reflect complete liberalisation of its public procurement market even if, under this law, competitive tendering is the general rule. The law does allow for only competitive tendering only by domestic providers, with international competitive tendering to take place only under certain circumstances. Furthermore, procurement entities may call for and assess tenders based on industrial policy objectives (such as local employment generation, technology transfer and local access).

## B. Government procurement and economic policy

23. Current policy and practice around public procurement reform is focused on the goal of maximising greater efficiency – often narrowly defined, it is argued, as value for money. In this view, more competitors bring better value, hence allowing foreign firms to tender increases competition and thus brings greater efficiency. However, this is not the only way to assess effective public procurement.

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<sup>11</sup> For World Bank policy on assessing public procurement systems, visit <http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/PROCUREMENT/0,,contentMDK:20105527~menuPK:84285~pagePK:84269~piPK:60001558~theSitePK:84266,00.html>

<sup>12</sup> World Bank, *Afghanistan: Managing Public Finances for Development*, Main report, Vol I, 22 December 2005

<sup>13</sup> World Bank Aide aide-memoir to Ghana Attorney General 2003 – in World Bank *Ghana Country Procurement Assessment Report: Main Report Volume 2* 2003, p 20

24. Facilitating the development of more competitive national businesses and small- and medium-sized enterprises (SMEs) in particular helps create jobs and reduce poverty. Because SMEs account on average for 50-60 per cent of employment at a national level,<sup>14</sup> consolidating and strengthening the sector is often recognised as an important economic development goal. As a result, various developed countries have linked public procurement policy to this objective in their own development. Examples include:

- the **US's** 1933 Buy American Act, which remains in place today requires preferences for local producers for small contracts
- **France** allows preferences for workers', artisans' and artists' cooperatives, and for groups of agricultural producers
- from 1976, **Germany** allowed SMEs to 'step in' and secure a contract if they could meet the terms and conditions of the cheapest bid
- In the 1950s **Greece** used price preferences to favour firms from outside Athens
- in the 1960s and 1980s, public procurement in the **UK** was directed to stimulate technological innovation.<sup>15</sup>

25. Public procurement, however, can and has been used to further socio-economic objectives. Examples where this has been done include:

- targeted public procurement in South Africa has allowed the government to particularly support local black businesses<sup>16</sup>
- in its trade agreement with the Dominican Republic and Central America, the US negotiated an exemption in the public procurement chapter to allow it to provide preferences to minority and small businesses

**Box 4**  
**Malaysia: public procurement and the Bumiputera**

Since the 1960s, the Malaysian government used public procurement preferences for both Bumiputera businesses and other domestic providers as one aspect of a strategy to generate investment-led economic growth, which together with redistribution secured racial stability. Linking preferences to growth ensured that the Bumiputera businesses could be strengthened without squeezing out those belonging to Indian and Chinese minorities.

Janis van der Westhuizen, a southeast Asia expert, claims that without this policy 'Malaysia's adaptation to the competition state model would have been even more difficult, complex and unstable'.

Malaysia has been at the forefront of developing country attempts to prevent an agreement on transparency in government procurement at the WTO. According to Christopher McCrudden, an expert on human rights and procurement law, 'Malaysia regarded elements of the proposed agreement... as tantamount to stripping it of its ability to use procurement as part of its development agenda, particularly in the context of redistributive policies directed at increasing the economic empowerment of... Bumiputera (sic)'

1 Taken from Christopher McCrudden, *Buying Social Justice: Equality, Government Procurement and Legal Change*, Oxford University Press, September 2007

<sup>14</sup> W Luetkenhorst, 'Corporate social responsibility and the development agenda: the case for actively involving small and medium enterprises', *Intereconomics*, May/June 2004.

<sup>15</sup> All examples from McCrudden *Buying Social Justice: Equality, Government Procurement and Legal Change*, Oxford University Press, September 2007.

<sup>16</sup> *Ibid.*

- countries like the UK are increasingly setting environmental guidelines for governmental purchasing.<sup>17</sup>

### C. The impact of open public procurement on domestic firms

26. The goal of value for money through more open competition has very real implications in countries reforming their public procurement systems. Domestic firms, particularly those that previously relied on government contracts under pressure from donors – such as the construction industry – often struggle to compete when public procurement markets are opened up.
27. To mitigate the impact of open public procurement on domestic firms, governments are able to offer them price preferences and training in the tendering process. However, an analysis of the structural constraints facing firms in Ghana raises some questions on how far the margin of preference will help local firms facing competition from abroad. Even if consistently applied, Cletus J Kosiba, executive director of Association of Ghanaian Industries believes that it is not in itself sufficient: ‘It’s just one ingredient. It probably addresses the cost differentials but there are other challenges that our industries face.’<sup>18</sup> Similarly, training in how to tender for government contracts will not in itself overcome the obstacles faced by firms in Ghana.
28. As in most developing countries, the high tax burden on local producers can undermine their competitiveness. In 2003, the World Bank’s Country Procurement Assessment Report (CPAR) for Ghana recognised this issue, stating that the ‘tax on raw materials renders local manufacturers uncompetitive against foreign competition.’<sup>19</sup> International firms are also frequently offered tax breaks by host governments and use a range of sophisticated accountancy practices that most developing country tax authorities are ill-equipped to address – for example, transfer pricing to help them avoid (and sometimes evade) the taxes they do face.<sup>20</sup>
29. Lobbying by local industry has managed to sometimes overcome this. Local firms can now claim back VAT on textbooks (as well as pharmaceuticals and agricultural machinery, inputs and tools), but this is still a cost as local firms obviously have to administer this process and it does not extend to all sectors.<sup>21</sup>
30. Local businesses quoted other major obstacles – such as labour costs, fuel costs, access to credit and delays in payment – which substantially reduce their competitiveness to foreign firms.

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<sup>17</sup> ‘UK government to set green procurement example’, *Green Biz*, 11 October 2004.

<sup>18</sup> Interview with Cletus J Kosiba, 14 August 2007.

<sup>19</sup> World Bank, *Ghana Country Procurement Assessment Report*, 2003.

<sup>20</sup> This is demonstrated by various Christian Aid reports, including *The Shirts off their Backs; A Rich Seam*; and *Haemorrhaging Money*

<sup>21</sup> Interview with William Turkson, 25 July 2007. Information in table is based on information provided during the interview.

## D. Conclusion

31. There is clearly an important role for donors here, in supporting governments to use public procurement processes, policies and practices to achieve broader development goals and consider the trade-offs of doing so. However, donors are not playing this role well because they are too focused on securing efficiency, narrowly defined as greater value for money through open competition. Yet this focus is to the detriment of overall economic development – which could be achieved through more strategic public procurement – and to domestic firms in particular.

## IV. RECOMMENDATIONS

32. In most developing countries, the government is the largest consumer. The impact of changes in public procurement on local industry can therefore be substantial – a fact that the international best practice law favoured by donors is not necessarily blind to, allowing as it does countries to implement a margin of preference for local firms. In Ghana donors have required the government to provide capacity building for local firms, particularly targeting actions at the construction industry, which in many developing countries relies on government contracts. However, it is not clear that these approaches, when fully implemented, would address the systemic constraints faced by local industries when competing against firms from elsewhere.
33. Public procurement needs to be recognised as the important *economic development policy* tool that it is. This is not a demand for blanket protectionism, but rather for developing countries to be able to decide how to use this tool to secure their development objectives. There are pros and cons to allowing the participation of foreign firms: it can bring in much-needed goods at lower cost and technology transfer, but it can also undercut local producers and hamper the development of local supply side capacity
34. Unfortunately there seems to be a trend in public procurement reform to mixing up the *process* (i.e. the way in which public procurement policies and decisions are made, monitored and challenged) with the *policy* (e.g. the extent of participation in domestic public procurement by foreign firms). It is important to separate the two and focus entirely on the *process*, or *administrative aspects* of reform, and help make them transparent and accountable to citizens.
35. When placed in the context of the current initiatives on aid effectiveness being undertaken by the Northern donor community and the World Bank, such as the Paris Declaration on Aid Effectiveness, the donor-driven agenda to reform aid recipients' public procurement policies and systems in order to promote "good governance" effectively becomes yet another tool through which developing countries may be required to conform to one-size-fits-all approaches that reflect

the donors' worldview of what constitutes "development" rather than the developing country's own view of what "development" should be about.

36. To prevent this situation, aid recipients must stress to donors, and the latter should accept, that aid-promoted improvements in public procurement systems in recipient countries should: :
- be limited entirely to changes that improve the accountability and transparency of government public procurement to the country's own citizens rather than to external actors
  - be tailored to each individual country context, taking government capacity and the workings of its political system into consideration
  - provide long-term capacity development support to recipient governments, to enable them to move out of aid dependence and promote the development of domestic supply side capacity
  - result in the removal any requirement to partially or fully open up national public procurement markets to foreign firms in return for aid or debt relief if such opening up would result in decreasing the policy space of the recipient government to promote the development of domestic supply capacity
  - recognise the effectiveness of linking public procurement to development objectives by positively supporting developing countries in using government procurement flexibly to support their own economic development objectives – whether that is, for example, by directly building up the competitiveness of local firms or bringing in the expertise of foreign firms.
37. Aid will not and cannot be effective in delivering on development if there are conditionalities that themselves negate the establishment of self-reliant and robust administrative structures, communities and bureaucracies in recipient countries. Aid must be changed so that it focuses on establishing the conditions under which the aid recipient starts moving towards exiting from reliance on aid.
38. This means that there must be a prioritisation of the development of local supply capacity as the sine qua non objective of any changes in aid policies, structures and delivery mechanisms. Aid conditionalities that would require the conduct of internationally competitive tendering for public procurement should not be accepted. The idea of committing to opening up of additional market access opportunities for Northern firms in developing country markets by allowing them to compete for government contracts against domestic firms was firmly rejected by developing countries when they rejected the launch of negotiations on government procurement under the WTO.
39. There must be benchmark indicators that donors must meet in order to ensure that aid-promoted changes in developing country recipients' public procurement policies, procedures and practices support and enable an eventual aid exit by the recipient. These indicators would include:

- measurable improvements on the use of country systems and their support to public procurement reform in recipient countries that enhance domestic supply capacity to meet domestic public procurement demands
- ensuring that the criteria to evaluate country public procurement systems focus only on accountability and transparency
- having measurable targets on aid-untying to which donors can be held accountable
- having disaggregated data of each donor's use of country systems

40. Aid-driven public procurement reform must also be situated by both aid providers and recipients in the broader context of the international aid architecture and the broader development debate. It cannot be dealt with in isolation from the broader systemic issues that need to be addressed if aid – including aid-driven procurement reform – is to deliver on development.

41. The continued widening of the development gap, coupled with the spotty record of existing aid programmes in supporting the self-reliant development of aid receiving developing countries, means that there must be substantial changes to the entire policy approach and architecture of aid.

42. Simply increasing aid will not be the panacea or sole solution to the problem of inequitable development, low growth, or poverty in developing countries. The problem of development inequity is deeply rooted in the structural and systemic imbalances that are reflected in the current global economic system. These imbalances reflect historical patterns of colonial and post-colonial economic and political exploitation, including in the areas of trade, finance, debt, and natural resource access and control. Aid, by its very nature, will not be able to address these systemic imbalances alone.

43. Furthermore, new approaches to ODA should be made more coherent with other policies that can enhance development policy space for developing countries, including the creation of new economic structures and policies designed to enhance South-South cooperation, integration, and self-reliance.

## V. CONCLUSION

44. The above recommendations are aimed at building national supply capacity, national procurement and accountability procedures and systems, and national institutions as the only basis for promoting endogenous development, and the only way to achieve the Millennium Development Goals and other internationally agreed development goals.
45. Governments of countries in the South must create conditions (such as provision of credit, tax breaks, skills training, etc.) to enable domestic suppliers (especially at local and municipality levels) to have a margin of preference over foreign firms while at the same time putting in place a rigorous system of public accountability to their citizens and national institutions.
46. For aid to be part of the development solution, the starting point will have to be for the main aid providers – i.e. developed countries – to deliver on their past aid commitments. They will also need to ensure that, among other things, aid delivery effectively helps developing countries meet their own development priorities and the MDGs and eventually result in aid recipient countries no longer requiring aid.
47. But more aid, in itself, will not guarantee developmental outcomes. There must also be a new and improved architecture that renders aid “more accountable to developing country governments and their citizens” as “more aid delivered through current aid structures will yield suboptimal results.”<sup>22</sup> Aid should be aligned to developing countries’ development strategies, help build up their institutional capacities, reduce transaction costs and eliminate bureaucratic procedures, be untied, enhance the absorptive capacity and financial management of recipient countries, and be focused on achieving development results – i.e. creating a situation where the aid recipient will eventually exit from aid dependence.

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<sup>22</sup> UNDP, Human Development Report 2005, p. 76.

## APPENDIX: USEFUL DEFINITIONS

Public procurement is a very technical business, so an initial understanding of the different systems of public procurement is helpful at the outset:

- **National competitive bidding:** the potential buyer invites tenders from as many suppliers as possible and awards contracts based on cost, quality or a mixture of the two. Invitations to tender are advertised in-country, and can be, but are not automatically, exclusive to national firms.
- **International competitive bidding:** as above, but advertised internationally to secure bids from foreign as well as local firms.
- **Sole sourcing:** the practice of using one supply source without a competitive bidding process for a justifiable reason.
- **Selective tendering:** when the buyer invites tenders from a few favoured suppliers only.
- **Price preferences:** when a government entity is able to select a higher-cost tender due to social, economic or environmental considerations. An additional percentage (normally 15 percent or so) is effectively added to the bid of non-preferred bidders allowing the purchaser to accept bid on preferred bidder (if it falls within that margin of adjustment)
- **Local content:** conditions on purchases to ensure that a certain degree of employment, goods and/or services for a specific contract come from the purchasing country.

## ACRONYMS AND ABBREVIATIONS

CPAR	Country Procurement Assessment Reports
DFID	Department for International Development (UK)
GDP	gross domestic product
ISODEC	Integrated Social Development Centre (Christian Aid partner)
MOES	Ministry of Education and Sport
OECD	Organisation for Economic Co-operation and Development
OECD DAC	OECD's Development Assistance Centre
PPB	Public Procurement Board
SEND	Social Enterprise and Development Foundation (Christian Aid partner)
SME	small- and medium-sized enterprise
UNICTRAL	United Nations Commission on International Trade Law

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