

CHAPTER 5

Contracting with the government

- ◆ Efficiency in public procurement ensures better use of taxpayer money.
- ◆ Awarding a simple contract for road maintenance takes as little as 161 days in the Republic of Korea or as long as 15 months in Chile.
- ◆ Resolving complaints raised during the award and execution of a contract takes 330 days in the Czech Republic or more than four years in the Dominican Republic.

In 2007 the Nigerian government awarded a contract for the rehabilitation of a local road. The works were slated to begin in 2009, but the project specifications had been designed six years before the contract was awarded. By the time the contractor started the works, the condition of the road had deteriorated significantly. The project was awarded at less than 60% of the cost required to execute it. At the expiration of the contract period in June 2012, the project was only 8% complete.¹ A decade after the contract award, rehabilitation works were still underway and a trip that would typically take one hour took four.²

Delays and cost overruns are not the only results of nonfunctioning public procurement. The waste of taxpayer money is the worst consequence. Bribes also abound. In Honduras, the now-defunct highway fund, Fondo Vial, awarded contracts to businesses run by a drug cartel to conduct road maintenance in exchange for bribes.³

The contracting with the government indicator set—*Doing Business's* latest area of research—benchmarks the efficiency of the entire public procurement life cycle, with a focus on the infrastructure sector.

Why does efficient public procurement matter?

Public procurement is the process by which governments purchase goods and services from private firms. In many sectors—for example, transport, infrastructure, and education—public authorities are the principal buyers. Worldwide, public procurement accounts for between 10% and 25% of GDP on average, and governments cumulatively spend \$10 trillion on public contracts each year.⁴ In OECD member economies, public procurement accounts for 12% of general government expenditures.⁵ At 15%, low-income economies' share of public procurement in GDP is the largest.⁶ Significant variation exists among economies: the ratio of government expenditure to GDP in Finland and the Netherlands is about 20%, whereas in Bahrain and Oman it is about 7%.⁷

Inefficient procurement regulation leads to substantial losses of public funds. Studies indicate that excess costs for a public procurement project are in the range of 25–50%.⁸ Research on the Democratic Republic of Congo, Indonesia, Japan, and Turkey shows that improved competition reduces prices.⁹ Similarly, a World Bank study finds that higher accountability leads to lower costs in road construction projects, as do transparency in advertising and tendering in Italy and the Slovak Republic.¹⁰ Competition also deters bribes. A study of 34,000 firms in 88 economies shows that, in economies with more transparent procurement law, firms report paying fewer and smaller bribes to public officials.¹¹

Losses from bribery (that is, when a firm bribes a public official to obtain a contracting advantage) represent on average between 4% and 10% of global procurement spending.¹² A new World Bank study shows that up to one-fifth of the value of government contracts may be lost to corruption.¹³ The indirect costs of corruption lead to distorted competition.

TABLE 5.1 Contracting with the government standardized case study assumptions

Procuring entity	<ul style="list-style-type: none"> – Is the agency in charge of procuring construction works for the authority that owns most of the roads comparable to the one described in the contract section – Is the sole funder of the works, has budget for the works, and is solvent
Bidding company	<ul style="list-style-type: none"> – Is a privately and domestically owned medium-size limited liability company – Operates in the economy's largest business city – Is up to date with all regulations and is in good standing with all relevant authorities, including those related to taxes – Has all licenses and permits needed to operate in this technical area – Has already responded to a public call for tender and is already registered with the procuring entity
Contract	<ul style="list-style-type: none"> – Entails resurfacing 20 kilometers of a flat, two-lane road (not a highway and not under concession), connecting the main business city to another city within the same state, region, or province if applicable, with an asphalt overlay – Is valued at \$2.5 million – Does not include any other work (such as site clearance, subsoil drainage, bridgework, or further routine maintenance)
Procurement process	<ul style="list-style-type: none"> – Is an open, unrestricted, and competitive public call for tender

The standardized case study

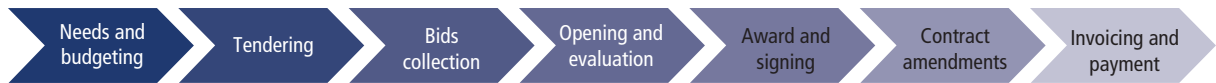
The contracting with the government indicators collect data through a hypothetical scenario. The standardized case study includes assumptions about the procuring entity, the bidding company, the contract, and the procurement process (table 5.1).

The construction sector was chosen because of its ubiquitous nature.¹⁴ Worldwide, construction is a \$2 trillion industry, representing between 5% and 7% of GDP in most economies.¹⁵ Government investment in road transport alone accounts for 2.0–3.5% of GDP.¹⁶ Because of construction's role in development (and its size), corruption in this sector is particularly harmful. The cost of collusion in the road sector is estimated at up to 60% of the contract value.¹⁷ Roads and other large infrastructure projects are consistently delivered over budget and over time.¹⁸ These overruns range from 20% above estimates in OECD member economies¹⁹ to 135% of initial funding authorizations in some developing economies.²⁰

What do the data show?

Three measures—the necessary procedures, the associated time, and the features regulated by the applicable laws—capture various aspects of each phase of the public procurement life cycle, from budgeting to payment (figure 5.1).

- The number of procedures describes a finite number of interactions between the contractor and various public agencies (the procuring entity, any governmental office issuing permits, a court, and so on).
- The number of days describes how long those interactions take.
- The legal index benchmarks which aspects of the public procurement process are regulated by law.

FIGURE 5.1 The public procurement life cycle

The data show vast differences in how efficient public procurement is worldwide. Sources of delay are found in every phase.

Needs and budgeting

If procuring entities do not begin the procurement cycle with a needs assessment, it is unlikely that the process will have a successful outcome. Overly optimistic budgets from faulty needs assessments result in projects delivered over budget and over time.²¹

The way the contract value is estimated varies greatly—from detailed fact-based analysis to an approximation left in the hands of public officials. In Hong Kong SAR, China, the procuring entity uses multiple instruments to value a contract, including market research to make informed decisions on design options, works implementation programs, cost estimates, and procurement method. The cost of materials is estimated through a price index established by the Civil Engineering Society, and similar projects from previous years inform other cost components. By contrast, procuring entities in Bolivia and Lebanon do not regulate which data should be used to estimate the contract value.

Another indication of planning adequacy is whether budget resources need to be secured before a procurement opportunity is advertised. In many economies, including Poland, a budget allocation is not required to proceed to the tender stage, suggesting that, when the time comes for the procuring entity to pay the contractor, funds might not be available. Others require a budget allocation that ensures that the necessary portion of the yearly budget is set aside for that particular procurement (as is the case in Canada and Slovenia, for example). Spain goes even further: in addition to requiring a budget allocation, the procuring entity must also include a document certifying the availability of funds in the tender documentation.

Budget planning matters a lot. A recent study of shortcomings in planning suggests that engineers' cost estimates are, on average, twice those provided by the funding authorization.²² An improper needs assessment results in unnecessary purchases, waste of public funds, and excessive renegotiations.²³ The prospect of scrutiny enhances the level of attentiveness demonstrated by public officials.²⁴

Tendering, evaluation, and award

At a minimum, governments need to perform the following six procedures to award a public contract:

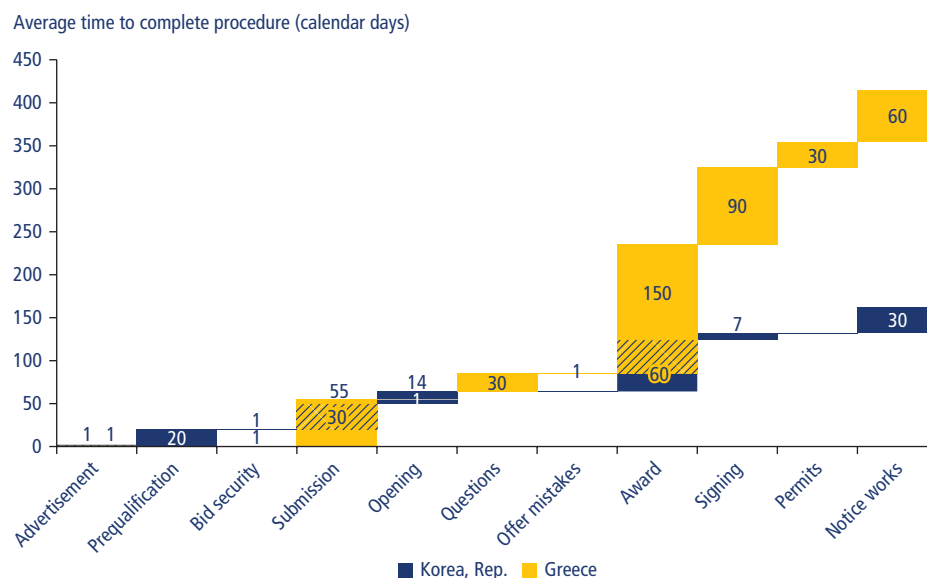
1. Communicate the opportunity to the private sector.
2. Collect the bids.

3. Open all bids received.
4. Evaluate the bids and award the contract.
5. Sign the contract.
6. Authorize the beginning of the works.

These steps are essential to the awarding of a public contract like the standardized case study, and they take place everywhere. How rapidly they are carried out, however, as well as how many additional procedures are required, results in vast differences in efficiency. The opening of all bids received, for example, may happen immediately after the submission deadline, as in Belgium and South Africa, or may take 20 days, as in Tunisia. The time to evaluate all bids and choose the winner is about 30 days in China, Georgia, and Norway, but is more than six months in the Kyrgyz Republic and Lebanon. Additional steps, such as prequalification, take as little as 21 days in Canada or as long as 90 days in Indonesia and Pakistan, and 120 days in Ireland.

Korea—the economy in the sample that awards contracts fastest—performs the six necessary procedures in just four months on average (figure 5.2). Two additional steps are required: undergoing a prequalification process (completed in less than three weeks) and obtaining a bid

FIGURE 5.2 Time and procedures to award a public procurement contract for road maintenance in Greece and the Republic of Korea



Source: *Doing Business* database.

Note: The number in each column refers to the number of days required for each procedure to be performed. If no number is included, that procedure does not take place in that country. In Korea, the bidding process takes 8 procedures; in Greece, it takes 10.

security (done simultaneously with the submission of the bid). All in all, awarding a simple routine contract for road resurfacing in Korea takes 161 days on average.

In other economies, the process is more convoluted. In Greece, for example, it takes one year to perform the six procedures. The deadline for submission of the bids is almost twice as long as in Korea (55 compared to 30 days). The evaluation of all bids received takes five months, and back and forth between contractors and the procuring entity typically delays it by an additional month. Once the decision is made and all documents are ready, signing the contract should take place in a matter of days. Instead, it takes an additional three months because of the need to receive approval from the Court of Auditors. Once this approval is obtained and the contract is signed, the contractor still needs to obtain an activity permit and an environmental permit before being able to commence the works—taking an additional month.

Greece grants those permits efficiently. Other economies do not. Obtaining permits to work on the road (such as occupancy permits, environmental permits, or traffic permits, if applicable) takes five months in the Arab Republic of Egypt and seven months in São Paulo, Brazil. In these economies, contractors aiming to work on government projects spend months obtaining permits from public authorities.

Efficiency in awarding public contracts improves the level of competition and encourages the participation of suppliers.²⁵

Contract amendments, invoicing, and payment

Once the works begin, three procedures are necessary:

1. The contractor needs to let the procuring entity know that the works are complete.
2. The procuring entity needs to confirm that the works are indeed complete.
3. The contractor needs to receive payment.

Efficiency in carrying out these steps, however, varies tremendously. Issuing a certificate of completion report takes two weeks or less in Australia, Canada, Denmark, Finland, Hungary, the Netherlands, and Malaysia; but contractors are left waiting for more than six months in Italy. Disagreements between the procuring entity and the contractor on whether the works were properly performed may significantly delay this approval (by 320 days in Mongolia and 455 days in República Bolivariana de Venezuela, for example). The process does not end there. Despite agreement by both parties, contractors may have to wait months to obtain payment. In Lebanon, Mali, and Panama, obtaining payment takes more than six months.

Contract amendments are another source of delays during the execution of the contract. Although frequent amendments indicate poor planning, how well the procuring entity handles such amendments is an indication of efficiency. A simple change order, such as for example a change in materials that had been provided for in the initial procurement document, delays

execution of the works by as little as two weeks in Canada and Finland, or as long as four months in Armenia. A more significant renegotiation of one or more contract terms delays the process by 135 days in Mexico City, Mexico, or 180 days in Tanzania. More efficient economies handle this unexpected occurrence in three weeks (as in Finland and Korea). All in all, delays in contract execution vary widely across the world. In Ireland, this phase takes five procedures and 153 days, whereas in Mozambique it takes eight procedures and 716 days.

Changes in contract terms and values are the most common channels of corruption in public procurement.²⁶ When the work is complete, low-quality goods are used to defraud procuring entities.²⁷ The delivery of substandard (overpaid) works—or a failure to deliver them at all—represents the most significant risk of this phase. Occasionally, before the delivery of subpar goods is detected, officials in the procuring entity may delay payment for completed works to solicit bribes.²⁸ A lack of transparency during the invoicing and payment phase leads to misuse of public funds.

Complaints

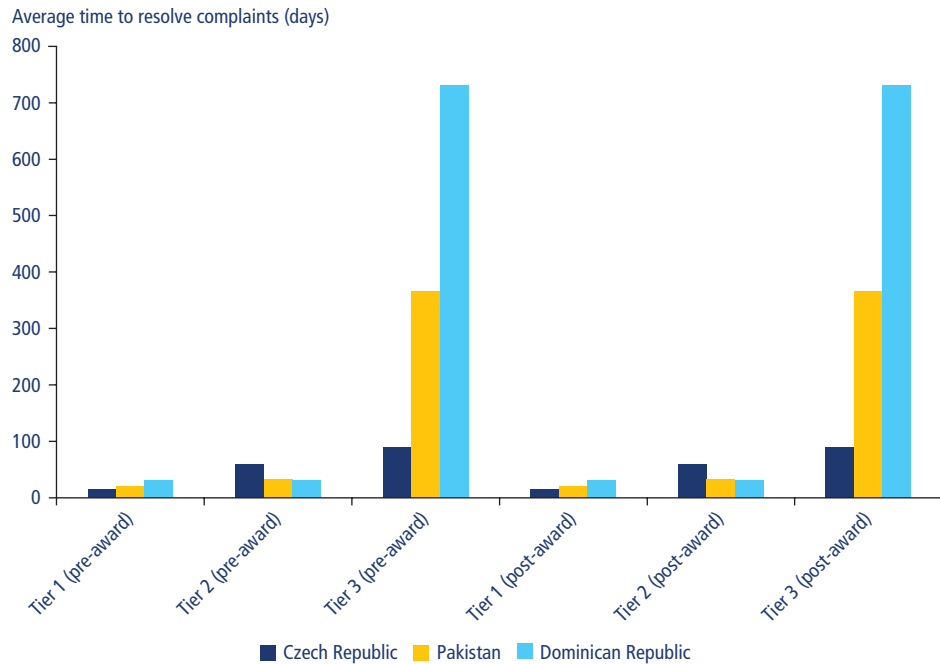
Complaints are claims brought against the public administration throughout the public procurement process. They are brought before or after the award and may refer to a variety of issues. A potential bidder, for example, could argue that the tender documents favor a specific bidder, or that a costly performance guarantee hinders access by small firms. An environmental nongovernmental organization could claim that the works harm a protected species, or that the tender documents do not include environmental parameters to ensure that they are executed in a sustainable manner. Once the contract is awarded, losing bidders could challenge the grounds of their exclusion or claim that the procuring entity granted special treatment to the winning bidder. In some cases, raising a complaint might be necessary to ensure fairness in the process. In others, it is used as a dilatory technique.

Trust in complaints procedures increases participation in the public procurement process, obtaining the best value for money. In turn, inefficient complaint resolution can stall the award and execution of a simple contract for years.

There is no minimum set of procedures to determine whether complaints work efficiently. Instead, the contracting with the government indicator set measures complaints brought before and after award, and focuses on who brings these complaints, which authority would have jurisdiction to hear them, how often they are raised, how long they would take to be resolved, and whether they suspend the procurement process.

In the Czech Republic, where complaints are usually pursued until there is no further recourse available (three tiers before contract award and three tiers after), resolving these complaints takes 330 days on average (figure 5.3). Resolving the same complaint in the Dominican

FIGURE 5.3 Calendar days to resolve complaints in the Czech Republic, the Dominican Republic, and Pakistan



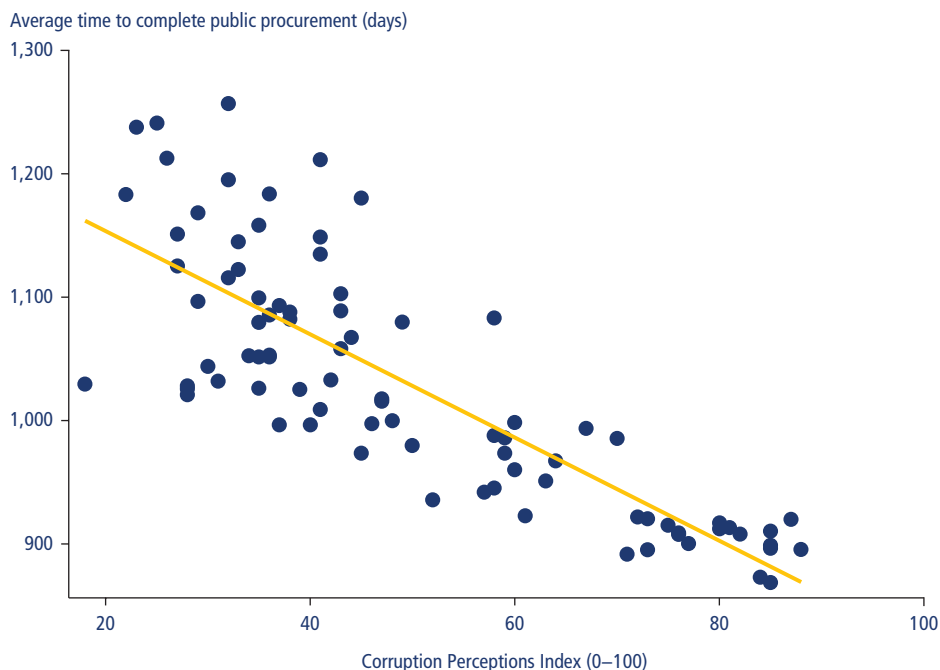
Source: *Doing Business* database.

Note: "Pre-award" refers to any challenge raised before the contract is awarded, such as that of a bidder arguing that the tender documents favor one specific company. "Post-award" refers to any challenge raised after the contract is awarded, such as by a bidder arguing that one of the evaluation criteria was used arbitrarily by the procuring entity to reduce the bidder's final score. Tier 1, tier 2, and tier 3 refer to the number of instances such a challenge would typically undergo.

Republic would take more than four years (1,580 days). Worldwide, resolving complaints takes longer when courts are involved, and tends to be more efficient once a dedicated administrative authority is in charge. In 2011, Tanzania established the Public Procurement Appeals Authority as an independent and quasi-judicial administrative body to resolve appeals from challenges against procuring entities in an efficient and specialized manner. As a result, challenges against award decisions are decided in 41 days, and challenges on tender documents are resolved in 18 days.

The public procurement process is carried out in a similar way around the world, but its efficiency varies greatly. And efficiency matters. Data show that, on average, economies with more efficient public procurement—as measured by the time it takes to award a contract, manage the unexpected during execution, obtain payment, and resolve challenges—tend to have lower perceived levels of corruption (figure 5.4).

FIGURE 5.4 Faster public procurement processes are associated with higher overall levels of transparency



Sources: *Doing Business* database; Transparency International data (<https://www.transparency.org/cpi2018>).

Note: The Transparency International Corruption Perception Index 2018 captures perception of public sector corruption according to experts and businesspeople, using a scale of 0 (highly corrupt) to 100 (very clean). The public procurement time is recorded in calendar days. The sample includes the 85 economies for which contracting with the government data were finalized as of July 2019. The relationship is significant at the 1% level after controlling for income per capita.

Summary

The contracting with the government dataset constitutes a one-of-a-kind repository of comparable data on how the public procurement process is carried out worldwide. These data inform change. Moreover, the impact of these reforms goes beyond effective public procurement. It affects management of public funds, efficiency in their expenditure, and accountability of public officials. It also fosters innovation in the delivery of projects, potentially leading to cost savings for governments worldwide. Along with all other *Doing Business* indicators, the contracting with the government dataset will be an important tool for governments and researchers to design more efficient rules that promote growth and development.

Notes

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28. Campos and Pradhan 2007.