The Contracting-out of the Procurement Process by Government Departments and Agencies

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INTRODUCTION

Numerous thorny issues arise and need to be addressed by government departments and agencies in procuring the many and varied goods and services the government needs to operate effectively in today's economy with its emphasis on productivity, quality assurance and value for money. All government departments and agencies must, wherever possible, ensure that goods and services are competitively provided by, or to, them and, generally, be responsive to market forces. Essentially, this entails reducing the costs of procurement (especially tendering) and establishing procurement policies, procedures and programs that are efficient yet fair and which comply with all necessary government and other relevant requirements.

MARKET TESTING OF ACTIVITIES

In striving for these overall goals, uneconomic activities must be identified and rationalised. This task is greatly facilitated by actively encouraging market testing to determine whether suppliers outside a particular government department or agency can provide the required goods and services more efficiently and cost effectively than can be done "in-house". As the main mechanism for making such decisions is the procurement process itself, it is submitted that the contracting out of that process for a few selected projects to test the efficiency of existing arrangements appears to have merit. This is particularly so in relation to the tendering stage of the procurement process which typically involves:

(a) the formulation and issue of project specific invitations to register interest, requests for proposals and/or requests for tenders;

(b) the evaluation of statements of interest, proposals and/or tenders (often entailing in the last case the assessment of various important design, performance, financial and risk elements against pre-set criteria which vary from project to project and industry to industry involved in the procurement); and

(c) the making of recommendations in relation to the outcome of the evaluation process (e.g. that a particular offer be accepted by the department or agency in question and, where necessary, submitted for Cabinet approval) or that the tender be terminated, with or without retendering.

PUBLIC SECTOR COMPLIANCE BURDEN

In many cases, this is an exacting process which consumes considerable resources in terms of both time and money. Apart from this considerable burden, recently, there has been a proliferation of new requirements of a quasi-legal nature which impinge on tendering procedures to which government agencies and departments, among others, must adhere. These ever growing stipulations include:

- Government (Federal and State) and industry codes of tendering, ethics and practice (e.g. tendering and labour relations);
- best practice guidelines for selected industries;
- quality assurance guidelines;
- government purchasing policies;
- government borrowing requirements;
- various industry and trade policies;
- social policies (e.g. equal opportunity and affirmative action);
- market testing and contracting-out guidelines; and
- guidelines for private sector participation in the provision of infrastructure.

PUBLIC SECTOR ACCOUNTABILITY

These requirements add significantly to the public sector's traditionally high level of accountability which primarily flows from the fact the public interest demands:

- fairness in the treatment of potential suppliers of goods and services to and on behalf of government; and
- value for money and the utilisation of public property for maximum public benefit where the acquisition, use or disposal of assets owned or controlled by government is concerned.

Government agencies and departments must therefore:

- maintain objectivity and avoid impropriety and partiality, both in fact and in appearance; and
- given that their decisions are open to close public scrutiny by a wide range of 'watchdogs' including the various Commonwealth and State Parliaments, anti-corruption commissions, trade and price surveillance authorities, ombudsmen and courts, be ready and able to defend their decisions (and

the policies and procedures that led to and implemented them) in terms of compliance with all relevant requirements.

PITFALLS IN PUBLIC SECTOR TENDERING

This burden weighs most heavily in the tendering area where government departments and agencies are very exposed to criticism. This is illustrated by the fact that of the 31 matters dealt with to date by the Independent Commission Against Corruption (ICAC) in New South Wales which have resulted in a formal hearing and report, 9 (29%) of them concerned tendering.

Application of Abstract Concepts

One of the reasons for the pitfalls inherent in government tendering is that many of the requirements referred to above are extremely difficult to apply in practice. Concepts such as "value for money" and "fairness", for example, are open to wide interpretation and careful project-specific analysis of all relevant facts and circumstances is necessary to determine if they have been met. This is frequently a time consuming and expensive undertaking and one that is inextricably bound up with meticulous assessment of the technical and performance aspects of each tender.

Divided Responsibility for Compliance

Moreover, due primarily to the large number of requirements that must be complied with by government departments and agencies, their size and the devolution of authority to different operating units within them, responsibility for compliance is often divided and dealt with by different divisions and personnel. This opens the real possibility of overlapping responsibilities or gaps in accountability in support areas resulting in significant matters escaping proper attention. In these circumstances, senior management cannot be confident that all procurement requirements have been met and that they and their organisation are not at risk of being challenged by, for instance, a disgruntled tenderer who claims to have been unfairly treated and has demanded action from the responsible Minister (or as some public sector executives refer to the Minister in this context - "the court of disputed returns").

Difficult Management Strategies

Ironically, some of the generally recognised methods of reducing the costs of tendering and effectively managing the process can present special problems for government departments and agencies. These methods include:

(a) reducing the number of tenders the client must examine by staging the tender process; and
(b) reducing the frequency of going out to tender by entering into extended supply agreements for required goods and services.

Staging Tender Process

Staging the tender process can involve the client utilising one or more of the following techniques:

(a) inviting prospective suppliers to register their interest in a project or requesting proposals from them concerning possible solutions prior to the issue of a request for tenders;
(b) short-listing tenderers or prospective tenderers after receipt of expressions of interest, proposals or tenders or at some point during the evaluation of the tenders; and/or
(c) pre-qualifying prospective tenderers.

Extended Supply Arrangements

Extended supply arrangements can involve:

- the use of standing offers or period agreements;
- the awarding of long term contracts;
- the formation of long term agreements with preferred suppliers; or
- the use of co-operative contracting techniques such as partnering.

The adoption of these strategies by government departments and agencies raises some difficult issues. Measures directed towards reducing the number of tenders, for example, potentially involve tenderers or prospective tenderers being unfairly or inappropriately excluded if the methods of exclusion fail to pass stringent probity and efficiency tests. Extended supply arrangements on the other hand can over time give rise to cosy, incestuous business relationships and jeopardise the benefits of effective competition (i.e. treating competitors fairly, leading to the award of a contract which represents value for money). For example, ICAC takes the view that close-knit working relationships over a long period tend to severely erode competition and carefully examines them if brought to its attention. There is also the concern that such relationships can be used as covers for collusive and anti-competitive arrangements. Given these difficulties and concerns, there would appear to be a distinct advantage in a government department or agency involving an independent third party in decisions relating to adoption of the measures in question.

Open Tendering

Alternatively, frequent highly contested open tenders are often considered at best to be very wasteful of scarce resources and otherwise risky as 'hungry' contractors in open competition may tender for work that they cannot perform adequately or perform for the low price submitted in an attempt to secure the job. This in turn inevitably leads to increased claims and disputes as the contractor fails to perform or seeks to extract a profit from the job by extraneous means.

A highly contested bidding process, however, need not necessarily add substantially to the costs of tendering. Any suggestion that open tendering is intrinsically inefficient and leads to a high incidence of claims and disputes needs to be challenged. Poor tendering and contracting practices should not be used to discredit open competitive tendering as a selection mechanism. Conversely, the early development and use of effective criteria and procedures for the assessment of tenders and the eligibility of tenderers

in terms of, among other things, their technical competence, experience and financial capacity should go a long way towards eliminating the adverse consequences of excessive risk taking by tenderers. However, much expertise and effort are necessary to establish such protections and properly apply them on a case by case basis.

ADVANTAGES OF CONTRACTING-OUT THE TENDERING PROCESS

Whatever approach is considered appropriate, it is clear that the tendering process is administratively very complex and resource intensive and that significant advantages are likely to flow from contracting-out its management to specialist organisations that have this as their mainstream business. The potential benefits of doing so include the following:

(a) Transparently Independent Assessment of Tenders

The complex task of assessing tenders and, in the process, ensuring that all government and other relevant requirements have been met would primarily be carried out by (or at least under policies and procedures set by) an independent third party, free of fear and favour and conflicts of interest.

This is important because internal assessments often fail to appear impartial; reports to senior management may be driven by extraneous factors and result in a false sense of security being held by the responsible officers. On the other hand, an objective, independent assessment would provide not only reassurance but valuable protection in this regard. The fact that the policies and procedures adopted in respect of a particular procurement have been set or scrutinised by an independent third party and found not to be wanting should provide an immediate answer to those who question the treatment they have received.

The ability to defend decisions relating to the procurement process is likely to be even more important in the future than it has been in the past. This is due to the growing willingness of courts, discernible in a wide range of recent decisions concerning mainly equitable doctrine, to utilize broad and uncertain standards such as "good faith", "fair dealing", "moral propriety" and the "legitimate expectations" of persons as bases for providing remedies in equity for breaches of codes, policies, guidelines and so forth that could not be described as legal rights or obligations or duties. Under the doctrine of **legitimate expectation**, which has been developed by the courts as part of "natural justice", for example, it is likely that a remedy would lie for a disgruntled tenderer if quasi-legal government requirements were not met by one of its departments or agencies. Where processes and procedures are established for the purpose of making a decision, people who have an interest in the decision have an enforceable legitimate expectation that the promised processes and procedures will be followed. In granting remedies in these circumstances, the courts have repeatedly asserted that the expectations are enforced not only as a matter of equity but also in the public interest. That is, it is in the public interest that governments honour their promises, notwithstanding that the promises made were not intended to create legally enforceable rights and duties.

(b) Allows Concentration on Core Activities

Each government department and agency would be able to move more of its resources from a costly support activity (procurement) to its core ones.

In this regard, it is appreciated that primarily for security or confidentiality reasons some government departments and agencies, from time to time, may need to retain total control of a particular procurement or part of it and for this purpose may require an 'in-house' tender issue and evaluation capacity. It is likely however that only a small percentage of procurements will fall into this category.

(c) Provides Benchmarks

The results of out-sourcing the procurement process, initially, on a limited trial basis would give the relevant department or agency some benchmarks of the administrative costs involved in this support activity against which it could compare its "in-house" performance and make decisions regarding improvements (if necessary) to, or retention of, the in-house capacity.

(d) Promotes More Efficient Decision Making

The use of external specialists in the management of the procurement process would not usurp the department's or agency's role as the client but rather facilitate more efficient decision making by it.

The external specialist's function would essentially be to ensure that all government and other relevant probity and efficiency requirements are met in the issue and evaluation of tenders and related matters. This would involve:

- developing effective policies and procedures in consultation with the relevant department or agency; and
- reducing the mound of technical, financial and other material typically received in respect of a major tender into digestible form to be submitted to the relevant department or agency with appropriate recommendations.

All critical decision making would be left to the department or agency.

ACCOUNTABILITY FOR OUTSOURCED PROCUREMENT

Public Sector Remains Accountable

It is important to recognise that although the engagement of outside specialists to manage the procurement process should provide significant benefits, a government department or agency, by taking this step, would not be able to avoid its compliance and accountability obligations in this sphere. This is so in the same way that the shift of many of the traditional functions of government generally into the private sector as a result of increasing privatisation and out-sourcing does not make government departments or agencies less accountable for the outcomes of the transactions in question. And nor does it remove the political sensitivity that surrounds many of these transactions.

On the contrary, government departments and agencies remain accountable with the consequence that public scrutiny extends to decisions to privatise the operation of, or out-source, the provision of a public facility or service, including procurement itself. Such examination is not confined to the manner in which the decision to do one or other of these things is made but covers how it is implemented from beginning to end, leaving the public sector exposed to its traditional high level of accountability.

Industry Shoulders Public Sector Level of Accountability

This being the case, it is incumbent on industry as more and more public business is channelled into the private sector to adhere to the same probity and accountability requirements as government - something which should give comfort and valuable protection to government departments and agencies. Any failure in this regard on the part of private sector organisations involved in government related work may expose their client (the government) to political and legal sanctions and the firms themselves to possible damaged reputation and legal action. Industry today is therefore obliged to work co-operatively with the public sector on projects of public importance to ensure that any such failure does not occur. Private sector businesses, including procurement specialists, that are unwilling or unable to do so are unlikely to be given the opportunity to participate in the enormous benefits that should flow from the increasing shift of government work into the private sector. ❑

Insolvency

Section 440J Corporations Law

Prudent business people often take the precaution of insisting on guarantees from third parties to secure debts owing. When the debt is owed by a company, and the guarantees have been given by directors of that company, creditors may find they are unable to enforce those guarantees if the debtor company is under administration.

Section 440J of the Corporations Law reads:

"During the administration of a company:

(a) a guarantee of a liability of the company cannot be enforced as against:
  (i) a director of the company who is a natural person; or
  (ii) a spouse, de facto spouse or relative of such a director; and

(b) without limiting paragraph (a), a proceeding in relation to such a guarantee cannot be begun against such a director, spouse, de facto spouse or relative; except with leave of the Court and in accordance with such terms (if any) as the Court imposes."

Accordingly, while the administration of a company continues, enforcement action against any guarantor who is also a director is barred.

This is an unusual provision. It was introduced to the Corporations Law by the Corporate Law Reform Bill of 1992. However, the explanatory memorandum shed no light on the purpose of the provision. It is suggested that its introduction was intended to assist the administrator of any scheme of arrangement to secure the co-operation of the company's directors and officers who may be guarantors of the company's debts.

There is little case law on Section 440J. In fact, only one has been reported being the Supreme Court of Queensland decision in *re: Grenadier Constructions No. 2 Pty Limited (Administrator Appointed)*. In that matter, the Court considered an application for leave to institute proceedings against guarantors of a company pursuant to Section 440J. The Court noted that it did not have the benefit of any precedents to consider. The Court took the view that it should have regard to whether or not such enforcement action would impede the ordinary winding up