

## ETHICS IN PUBLIC PROCUREMENT – AN OVERVIEW

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**Abstract:** *The discipline of ethics relates to the concepts of right and wrong conduct, moral duties and obligations, a system of moral principles and values, and moral character. Though ethics is a very old concept since times immemorial but ethical conduct in public procurement has gained importance in recent times. Public procurement accounts for a significant portion of the overall demand for goods and services and is increasingly seen as an attractive and feasible instrument for developing society and nation. Therefore, a well-designed policy of public procurement can make a profound impact on a nation. Most procurement related principles, i.e. fairness, integrity, transparency and accountability, are based on ethics. If these are followed in true spirit, it can improve services delivery and establish citizens' trust. This article aims at examining what are ethical issues in public procurement in India and particularly in Indian Railways, the existing framework to handle them and how we can strengthen it.*

### Public procurement

Public procurement refers to the purchase of goods, services and works by governments and state owned enterprises. As per World Bank, public procurement is a strategic tool for achieving development, social and environmental objectives of governments, rather than using it as a tool for mere compliance with rules and regulations. As public procurement accounts for a substantial portion of the taxpayers' money, governments are expected to carry it out efficiently and with high standards of conduct in order to ensure high quality of service delivery and safeguard the public interest.

World Bank has estimated that in 2018, out of global GDP of US \$90 trillion, around \$11 trillion were spent on public procurement. This means globally, on an average, 12% of GDP is spent via public procurement. Though there are wide variations in this expenditure amongst various countries, in India it accounts for over 20% of GDP.

Public procurement is a crucial pillar of services delivery for Governments. Because of the sheer volume of spending it represents, well governed public procurement can and must play a major role in fostering public sector efficiency and establishing citizen's trust. Well-designed public procurement systems also contribute to achieving pressing policy goals such as environmental protection, innovation, job creation and the development of small and medium enterprises.

### Ethics and its role in Public Procurement

*"If you once forfeit the confidence of your fellow citizens, you can never regain their respect and esteem" - Abraham Lincoln.*

Ethics is defined as moral principles that govern a person's behavior or the conducting of an activity. Ethics is concerned with what is good for individuals and society and is also described as moral philosophy. The term is derived from Greek word "Ethos" which means custom, habit, character or disposition. It seeks to resolve questions of human morality by defining concepts such as good and evil, right and wrong, virtue and vice, justice and crime.

Since the amount involved in public procurement is huge and multiple government and public sector enterprises are involved, it attracts numerous challenges including governance issues. India's annual public procurement is estimated over US \$300 billion as per CUTS-Centre for International Trade, Economics and Environment (CUTS-CITEE, 2014). Several ministries spend over 50% of their budget on public procurement (India: Probity in PP, 2013). These massive outlays create opportunities for implementing national policies and for positively impacting the economy, but unfortunately are vulnerable to mismanagement, fraud and corruption. Consequently, the public procurement function needs to be well managed and implemented transparently and efficiently.

Given the magnitude of spending involved, even small efficiencies realized in procurement functions can release large financial resources, which could be used for further development efforts leading to more inclusive growth. Ethics can play an important role in achieving these efficiencies as most procurement related principles, i.e. fairness, integrity, transparency and accountability, are based on ethics. If these are followed in true spirit, it can improve services delivery; establish citizens' trust, good governance, underpinning public servants' responsibility to exercise stewardship, and to use and develop all resources in the most economical, efficient, and effective way. A sound ethical framework, therefore, enables a public sector environment that encourages high standards of professional ethics and integrity in public procurement.

### Core Principles of Public Procurement

1. **Value for money:** Value for money means the effective, efficient and economic use of resources, which requires the evaluation of relevant costs and benefits, along with an assessment of risks and non-price attributes and/or life cycle costs, as appropriate. Price alone may not represent value for money.
2. **Efficiency:** The principle of efficiency requires that procurement processes be proportional to the value and risks of the underlying activities. Procurement arrangements should be time sensitive and strive to avoid delays.
3. **Economy:** This principle takes into consideration factors such as sustainability, quality and non-price attributes and /or life cycle costs as appropriate, which support value for money.
4. **Integrity:** Integrity refers to the use of funds, resources and authority according to the intended purposes and in a manner that is well informed, aligned with the public interest and broader principles of good governance. It, therefore, requires all stakeholders involved in the procurement process to observe the highest standards of ethics and refrain from fraud, corruption, etc.

5. **Transparency:** Transparency means unimpeded visibility. Since public procurement involves use of and accountability of public funds, transparency is, perhaps, paramount in all procurement activities. It implies:
  - relevant public information be made publicly available to all interested parties consistently and in a timely manner through readily accessible/available sources at reasonable or no cost
  - appropriate reporting of procurement activities and
  - the use of confidentiality provisions in contracts only where justified
6. **Fairness:** It implies-
  - equal opportunity and treatment for bidders
  - equitable distribution of rights and obligation between purchaser and supplier
  - credible mechanism for addressing procurement related complaints and providing timely recourse
7. **Accountability:** Accountability is answerability, blameworthiness, liability, and the expectation of account giving. Accountability in procurement means that buyers must take ownership of all responsibilities and commitments that have been allocated to them and maintain a clear audit trail of the actions and decisions taken. Accountability cannot exist without proper accounting practices.

### Potential Areas of Risk in the Procurement Cycle

Procuring officials are exposed to a number of risks when dealing with suppliers. Situations posing ethical dilemmas can occur in any type of procurement activity but will have a higher impact in high value/high risk purchases. Regardless of the value of the procurement activity, the highest standards of ethical behavior must always be maintained to ensure probity of the procurement process.

Some potential areas of risk relating to ethics in the procurement cycle are listed in the table below.

SN	Area of Risk	Explanation and Examples
1.	Budgeting	Lack of proper budgetary control, for example when all funds are not allocated to a specific purpose, can provide the necessary funds for fraud and corruption to take place.
2.	Financial approval policy	Without regular audits and strict management controls, there are opportunities for fraudulent use of a person's own levels of authority, or of misusing someone else's.
3.	Perceived need	Requirements can be invented or falsified.
4.	Specification development	Specifications can be written to favor a specific supplier. Clarifications on specifications can be provided to only one of the invitees during the tendering process.
5.	Evaluation criteria	Evaluation criteria can be written, or amended, after receipt of offers to favor a particular supplier.
6.	Pre-qualification	This process can be used to limit the field of competition to give a favored supplier an advantage.
7.	Invitation to	This process can be used to give the illusion of competition

SN	Area of Risk	Explanation and Examples
	tender/sourcing	where it does not really exist by inviting tenders from companies who are known to be unsatisfactory or ineligible, or by not sending out complete specifications to all bidders at the same time etc.
8.	Offer evaluation	Fraud at this stage occurs mainly when objective evaluation criteria have not been agreed in advance. It can also occur where technical staff is able to use their specialist knowledge to mislead other members of the evaluation team.
9.	Negotiations	Favored suppliers can be assisted or given useful information during negotiations.
10.	Contract award	Suppliers may find opportunities for fraud either through deliberately fraudulent acts or through buyer incompetence. Procurement staff could artificially split contract award to remain under the organizational threshold for contract committee review or to award more contracts to preferred suppliers.
11.	Post award changes to specifications	Allow suppliers to increase profits by charging more for revised specifications.
12.	Ordering and receipt of goods	Examples are: Allowing under-deliveries of goods or non-performance to specifications, Drafting false goods inward notes, Deliberately over ordering, Allowing inventory to dwindle so that emergency orders at a higher price will have to be processed.
13.	Invoice certification	Deliberate overcharging, backdating orders to allow benefit from price changes, paying twice, failing to insist on or monitor retentions.
14.	Decentralized procurement organization	Delegations to a large number of people making it difficult for the central procurement function to exercise total control and awareness of what is going on in the decentralized units. Although decentralization can often improve efficiency and reduce costs, it can also increase the risks of corruption.

### Potential warning signs of unethical practices

There are some typical signs that may indicate or warn of unethical practices. These include, but are not limited to the following:

- Deviation from proper procedures
- Poor record keeping: missing files and documents
- Buyer's extravagant lifestyle
- Resistance to audit and reluctance to delegate
- Exclusive handling of supplier by only one person
- Secrecy Vs. confidentiality
- Dictatorial management style
- Unnecessary meetings with suppliers
- Reluctance of suppliers to submit bids

There are both internal and external forces, which can serve as barriers to someone

making ethical decisions. External forces include political pressure, following group norms, doing what is rewarded in the organization and what someone is told to do. Internal forces include personal expedience and greed, fear of reprisal and intimidation and ethical ignorance and blindness.

### **Ethical risks for Procurement officials**

- **Accepting supplier favors and gifts:** Offering gifts to customers is a very common practice in the private sector. It is a marketing strategy based on the universal sense of reciprocity. If we receive something, we feel obliged to give something in exchange; i.e. there is no such thing as a “free lunch”. The acceptance of a gift can also create a conflict of loyalties or raise expectations from the giver of the gift.  
Accepting gifts, favors and freebies from suppliers are the most common unethical practices. This may affect buyer’s decision to evaluate and select a supplier.
- **Conflict of interest:** Conflict of interest arises when buyers or their close family/friends have direct financial interest in a supplier’s organisation. This is a major unethical practice and a serious breach of ethics.
- **Confidentiality of information:** Confidential information should be shared only when needed and with the persons who are liable to get the same as part of their profession. Confidential information should be carefully shared with the internal and external world. There are various kinds of information that need to be protected. Some of the examples are pricing, T&Cs, personnel information of customers, commercial information of suppliers, cost break up, any business and trade secrets etc.
- **Fair and unbiased treatment:** All suppliers should be treated fairly and in an unbiased manner. Any biased treatment to any particular vendor raises unethical behavior.
- **Integrity:** Integrity is the quality of being honest and having strong moral principles. Any compromise on the integrity has a negative impact on the overall procurement process.

### **Unethical behavior by Procurement officials and suppliers**

Cases of fraud, bribery, corruption, coercion and collusion can involve both procurement staff and suppliers. These different types of unethical behavior are described below:

- **Fraud**  
Fraud is any act or omission, including misrepresentation that knowingly or recklessly misleads, or attempts to mislead a party to obtain a financial or other benefit or to avoid an obligation. With regard to procurement, this kind of practice can be done in order to influence the competitive selection process or the execution of a contract.
- **Bribery/Corruption**  
Bribery and corruption involve the practice of offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence the actions of

another party. A bribe can consist of immediate cash or personal favors, a promise of later payment, or anything else the recipient may view as valuable.

- **Coercion**

Coercion is an act or omission that impairs or harms, or threatens to impair or harm, directly or indirectly, any party or the property of the party to improperly influence the actions of a party. An example of coercion would be for a supplier to use knowledge it has about a procurement official to blackmail him/her into improperly carrying out his/her procurement functions in order to provide the supplier with an undue advantage.

- **Collusion**

Collusion means a scheme or arrangement between two or more parties designed to achieve an improper purpose, including influencing improperly the actions of another party. With regard to procurement, collusion between two suppliers could be designed to establish prices at artificial, non-competitive levels. It can also mean an arrangement between a supplier and a procurement staff member to manipulate the procurement process by restricting the list of suppliers or restricting competition to a particular geographic area. Practices could involve "kick-backs" or bribes benefiting both the supplier and the staff member.

An example of collusion between two or more suppliers is "price fixing and bid rigging" with the goal of suppressing and eliminating competition on contracts. Price fixing is an agreement where one or more bidders agree not to submit a bid, while bid rigging is where two or more bidders agree to submit bids that have been pre-arranged amongst them. Such schemes usually fall into one or more of the following categories:

- ❖ **Bid Suppression:** One or more suppliers who otherwise would be expected to bid, or who have previously bid, agree to refrain from bidding or withdraw a previously submitted bid so that the designated winning competitor's bid will be accepted.
- ❖ **Complementary Bidding:** An agreement by suppliers whereby at least one of them agrees to submit a bid that is either too high to be accepted or contains special terms and conditions that will not be acceptable to procurement entity. Such bids are designed to give the appearance of genuine competitive bidding.
- ❖ **Bid Rotation:** Suppliers submit bids but agree to take turns being the low bidder.
- ❖ **Subcontracting:** Suppliers agree not to bid or to submit a losing bid in exchange for subcontracts from the successful bidder.

### Existing Ethical Framework

"General Financial Rules, 2017" and "Manual for Procurement of Goods, 2017" lay down the following framework:

#### **Rule 144: Fundamental Principles of public Procurement**

Every authority delegated with the financial powers of procuring goods in public interest shall have the responsibility and accountability to bring efficiency, economy,

and transparency in matters relating to public procurement and for fair and equitable treatment of suppliers and promotion of competition in public procurement.

**Rule 173:** All government purchases should be made in a transparent, competitive and fair manner, to secure best value for money. This will also enable the prospective bidders to formulate and send their competitive bids with confidence.

**Rule 174:** Public procurement procedure should ensure efficiency, economy and accountability in the system.

**Rule 175 (1): Code of Integrity for Public Procurement (CIPP)**

No official of a procuring entity or a bidder shall act in contravention of the code which includes-

- (i) Prohibition of
  - making offer, solicitation or acceptance of bribe, reward or gift or any material benefit, either directly or indirectly, in exchange for an unfair advantage in the procurement process or to otherwise influence the procurement process.
  - any omission, or misrepresentation that may mislead or attempt to mislead so that financial or other benefit may be obtained or an obligation avoided.
  - any collusion, bid rigging or anti-competitive behavior that may impair the transparency, fairness and the progress of the procurement process.
  - improper use of information provided by the procuring entity to the bidder with an intent to gain unfair advantage in the procurement process or for personal gain.
  - any financial or business transactions between the bidder and any official of the procuring entity related to tender or execution process of contract; which can affect the decision of the procuring entity directly or indirectly.
  - any coercion or any threat to impair or harm, directly or indirectly, any party or its property to influence the procurement process.
  - obstruction of any investigation or auditing of a procurement process.
  - making false declaration or providing false information for participation in a tender process or to secure a contract;
- (ii) Disclosure of conflict of interest.
- (iii) Disclosure by the bidder of any previous transgressions made in respect of the provisions of sub-clause (i) with any entity in any country during the last three years or of being debarred by any other procuring entity.

Procuring authorities as well as bidders/suppliers should observe the highest standard of ethics and should not indulge in the prohibited practices at any stage during the procurement process. All Procuring officials need to sign declarations to this effect periodically and in various Procurement decisions. The bidders/suppliers should be asked to sign a declaration about abiding by a Code of Integrity for Public Procurement in registration applications and in bid documents, with a warning that,



in case of any transgression of this code, its name is not only liable to be removed from the list of registered suppliers, but it would be liable for other punitive actions such as cancellation of contracts, banning and blacklisting or action in Competition Commission of India, and so on.

### **Integrity Pact (IP)**

The Pre-bid Integrity Pact is a tool to help Governments, businesses and civil society to fight corruption in public contracting. It binds both buyers and sellers to ethical conduct and transparency in all activities from pre-selection of bidders, bidding and contracting, implementation, completion and operation related to the contract. This removes insecurity of bidders, that while they themselves may abjure bribery, but their competitors may resort to it and win contract by unfair means.

The pact essentially envisages an agreement between the prospective bidders and the buyer, committing the persons/officials of both sides, not to resort to any corrupt practices in any aspect/stage of the contract. Only those bidders, who commit themselves to such a Pact with the buyer, would be considered competent to participate in the bidding process. In other words, entering into this Pact would be a preliminary qualification.

Ministry of Finance, Department of Expenditure has mandated to incorporate Integrity Pact, depending on the nature of procurements above a threshold value. As guidance, the threshold should be such as to cover bulk of its procurement expenditure.

### **Railway Services (Conduct) Rules**

The Procuring officials being Railway servants are also governed by “**Railway Services (Conduct) Rules, 1966**”, which are framed with a view to promote ethical conduct. These prescribe that Railway servant shall at all times-maintain high ethical standards and honesty (Rule 3 (1) (vi)), promote the principles of merit, fairness and impartiality in the discharge of duties (Rule 3(1) (viii)), maintain accountability and transparency (Rule 3(1) (ix)), use public resources efficiently, effectively and economically (Rule 3(1) (xii)), declare any private interests relating to his public duties (Rule 3(1) (xiii)), take steps to ensure integrity (Rule 3(2) (i)) and not accept tips (Rule 13). Conduct Rules also prohibits acceptance of gifts beyond a certain threshold limit.

### **Anti-Corruption Law**

On the legal side, there is “Prevention of Corruption Act, 1988 (PCA)” to prevent corruption in public offices. Any public servant taking/seeking gratification other than legal remuneration in respect of an official act is committing a criminal offence. Giver and taker of bribe both are committing offence as per this act. In reality, after the Act's first passage in 1988, for almost 25 years, there has not been much change in the perception about India as a nation with high corruption levels, as measured by Transparency International's Corruption Perception Index (CPI). The CPI ranked



India at a historical low of ninety-fifth rank in 2011. In 2017, owing to pro-governance policies, technology, automation of various government processes with public interface (e.g., passport, train tickets, public procurements such as e-tender/e-procurement/e-payments), India's rank improved to eighty-first position out of 180 countries.

Due to PCA's limited success, there was a need to introduce changes that could help make it more effective. The Prevention of Corruption (Amendment) Act, 2018 (Amendment Act) came into force on 26 July 2018, and seeks to bring the Indian anti-corruption legal framework in conformity with current international practices laid down by the United Nations Convention Against Corruption (UNCAC). Now, Commercial Organisations will be proactively required to identify bribery and corruption risks applicable to their businesses, and develop adequate procedures in compliance with such guidelines as may be prescribed to prevent persons associated with it from undertaking such conduct.

### **Shortcomings and the Way Forward to Ethical Procurement**

Existing Rules and guidelines for encouraging ethical procurement on Indian Railways are reasonably adequate. However, we are far from implementing these guidelines in true spirit. Code of Integrity in Public Procurement and Integrity Pact are yet to be implemented. Though, with the introduction of e-Procurement, there is considerable improvement in transparency and reduction in time delays, we are yet to go a long way. Further, there are implementation issues at each stage of procurement cycle right from need assessment. Ethical behavior has still not become a culture in the organization. Further, there is a need to have an Ethics unit to guide in case any employee faces ethical dilemma.

Rules and guidelines are at best a good start, but the emphasis has to come from the top down. Top leadership needs to ensure they are acting in an ethical manner and be very clear from the start that unethical practices will not be tolerated throughout the organisation.

In corruption, it takes two parties to be involved not just one. To fight corruption, we need to go after both the parties. Penalties alone will not suffice. We need to involve all stakeholders and have regular dialogue with all stakeholders to address ethical issues.

Ethics begins with the individual. As a public servant it is important to disconnect one's leanings toward favoritism. It is human nature to develop attachments towards individuals we like and people who satisfy our needs. As a representative of public interest, however, it is important to never let these emotional bonds sway our judgment. It is also essential that gifts of gratitude (or otherwise) are not accepted, as these gifts may cloud our judgment in future dealings with a particular vendor.

Public procurement officials must be constantly aware of how their actions appear to

outside observers, and they should always behave in such a way that their actions cannot be perceived as improper. Behaving correctly in a "technical" sense is not enough; it is also necessary to avoid even the appearance of impropriety.

Also important in gaining public trust is the notion of professionalism. A procurement professional will always strive to better themselves through education. This education base should be all-inclusive, as broad-spectrum training will serve as a tool kit, which an experienced procurement officer can draw upon in the hopes of making sound ethical decisions.

Becoming affiliated with professional organizations while participating in professional activities, such as purchasing seminars, is also important in the field of public procurement. This will help to spread relevant information about the field to peers as well as bolster the image of the profession from a clerical task to one that requires not only education, but also a strong networking base that encourages growth in like-minded professionals. Also, be aware of ethical violations that have occurred in the past, so that one knows how to avoid them.

Public procurement officials should do whatever possible to learn about ethics. Ethics training can open debate on potential ethical dilemmas that may arise in the public procurement profession. Exploring real life scenarios with a group of like-minded individuals will often prove that there is not only one means to an end, and may spark interesting debate that will assist in dealing with real life ethical dilemmas when they occur. Ethics branch can extend professional help at the time of ethical dilemma.

If we expect to set standards for conduct then ethical behavior must start at home. The importance of maintaining integrity off the job also needs to be looked at. Living our values through a code of conduct, which is clearly articulated, communicated and – most importantly – enforced without regard to grade level or affiliation is critical for building a supportive environment for ethical behavior.

We should treat public money with the same responsibility we would expect if we were to entrust our own funds to another individual or entity. It isn't our money, and for that reason we must respect the way in which we spend it.

## Conclusion

Efficient and effective procurement of goods, services and works is vital to the core purposes of government, including infrastructure investment and the delivery of essential services to its citizens. Further, public procurement is a key economic activity of governments that is particularly vulnerable to mismanagement, fraud and corruption. Efforts to enhance good governance and integrity in public procurement contribute to an efficient and effective management of public resources and therefore of taxpayers' money.

Ethics is a significant issue when it comes to public procurement. As procurement

professionals, it is our responsibility to ensure that the core values of honesty, integrity and transparency are not only followed, but disseminated throughout the supply chain. Procuring entities must have a strong code of ethics for their business processes including procurement process. Employees must be given training regularly on ethical behavior. Procurement officials must never use their authority for personal gain. Holding high ethical standards in our daily works is critical to maintaining a healthy organization and winning citizen's trust.

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