

ETHICAL CONDUCT AS THE CORNERSTONE OF PUBLIC SECTOR PROCUREMENT

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ABSTRACT

The procurement of public goods and services is the link between public requirements and private sector providers. The public sector provides goods and services to satisfy the complex variety of needs of a country's citizens. The procurement of goods and service by the public sector is unlike procurement in the private sector: it is a process within the political system. This implies that it involves issues such as integrity, accountability, the national interest, effectiveness and efficiency. This article describes the responsibilities of the public sector in the delivery of services, and provides an understanding of the functioning of the Supply Chain Management system and the role of public sector managers in this process. Since ethical conduct plays a critical role in the procurement of goods and services in this domain, the article also focuses on the challenges of ethical considerations in public sector procurement.

INTRODUCTION

Public funds must be used for the sole purpose of providing goods and services to a country's citizens; thus, these funds must be spent in the public interest and for the public's benefit. Government spending must take place in the most efficient and cost effective manner possible. In the South African government environment, public sector procurement (also referred to as acquisition management) as part of Supply Chain Management falls under the administrative function of financial resource management. Any shortcomings or failure in procurement practices can open up opportunities for large-scale mismanagement of public money. An effective procurement system requires well-defined policies to ensure that all transactions are performed *in the open*, with a proper audit trail.

This article focuses on the procurement function, as well as considerations and challenges in the procurement process. In the private sector, the procurement process is

regarded as a source of competitive advantage with the ultimate aim of maximising profits. In the public sector, the process of procuring goods and services is designed, primarily, to apply public policy to ensure the proper use of the contribution of the taxpayer's money through best value-for-money solutions and secondly to promote broad black economic empowerment (BBEE).

RESPONSIBILITIES OF THE PUBLIC SECTOR

According to De Bruijn and Dicke (2006:79) the state is responsible, either directly or indirectly, for safeguarding substantive public values such as services, continuity, quality of services, affordability, and user and consumer protection. This responsibility has important consequences in terms of conformity to service provision. The aspects identified by De Bruijn and Dicke (2006) are normally stipulated either in standards or in national technical specifications. McGuire (2002:509) argues that public services have both a social and an economic value and that the benefits of public services are consumed collectively by the community, as well as privately by users.

Public administrations are in the process of moving to new ways of collaborating in activities. Altenburg and Von Drachenfels (2006:405) assert that it is important to identify carefully which services are actually purely private goods (which can and should be provided on a market basis) and in which cases governments should intervene by means of a procurement system to maximise the welfare of their citizens. Rasmussen, Malloy and Argarwal (2003:84) point out clearly that governments want inexpensive and efficient service delivery that conforms to the norms of democratic public administration, whereas non-profit organisations are driven by a strong desire to serve their clients in the best possible manner. Highlighting the core rationale from a financial perspective, Pongsiri (2002:492) suggests that public organisations externalise net social benefits as a result of organisational activities, whereas private organisations require adequate returns on their investments.

In its attempt to provide effective and efficient systems in the public sector, in terms of Section 6(1)(g) of the *Public Finance Management Act*, Act 1 of 1999 (the *PFMA*), as amended (South Africa 1999), the National Treasury must promote and enforce transparency and effective management in respect of revenue, the expenditure, assets and liabilities of departments, public entities and constitutional institutions. Section 38 (1)(a)(i) of the *PFMA* requires that the accounting officer for a department, trading entity or constitutional institution must ensure that these criteria are met and must maintain effective, efficient and transparent systems of financial and risk management and internal control.

Efficiency in the public sector therefore involves the efficient use of the available resources for the provision of public services. Efficiency is normally reflected in the delivery of processes and resource utilisation that achieve the following (Funnel & Cooper, 1998:36-38):

- a reduced number of inputs such as human resources or assets, whilst maintaining the same level or the improvement of service provision;

- a reduction in the pricing structure of the resources required to provide public services;
- increased outputs, such as improved quality or quantity of service, for the same level of inputs;
- improved output per unit cost or input; and/or
- a change in the balance between different outputs which is aimed at the delivery of similar objectives in a manner which achieves a greater overall output for the same inputs.

CONTEXTUALISATION OF THE PROCUREMENT OF GOODS AND SERVICES

The broad objectives of public financial management are to achieve overall fiscal discipline, the allocation of resources to priority needs and efficient and effective delivery of public services. As an illustration, one simply has to look at the implications of the South African government's commitment to spend over R300 billion over three years on various infrastructure projects, as part of AsgiSA (Pauw *et al.*, 2009:229).

Sound public financial management supports aggregate control, prioritisation, accountability and efficiency in the management of public resources, as well as the delivery of services that are critical to the achievement of public policy objectives. It should be clear from this that effective public financial management is therefore central to government's ability to render services to its citizens and to ensuring sustainable socio-economic development.

The public financial management system involves the statutory arrangements and processes for the following management activities:

- forecasting revenues and expenditures;
- formulating medium-term expenditure frameworks;
- linking the budget to policy-making;
- preparing and implementing the budget;
- managing cash and monitoring expenditure;
- performing internal control and audits;
- accounting and reporting;
- procuring public goods and services and managing assets;
- conducting external audits; and
- ensuring oversight by the legislature.

In order to ensure sound public financial management, the public financial system requires knowledge of the constitutional and administrative structures within which the system functions. In essence, government is accountable to Parliament for effective and efficient expenditure. The public finance management system supports this institution and enables accountability, in particular through the appropriate systems and through Parliamentary scrutiny (oversight) of government's performance.

Functioning of Supply Chain Management

A high degree of integration of public sector procurement and financial management have been forged in South Africa: the whole public financial system has been redesigned since the change of government in 1994. The focus of this redesign has been an effort to establish strong integration throughout the budget system in order to make the entire public financial management system accountable for achieving results. Within this overall approach, procurement has been established as a process of Supply Chain Management (SCM), which involves decisions to acquire, maintain and eventually sell off assets. As a result of the redesign, the procurement function is no longer seen as a purely technical process; and procurement specialists now operate alongside other leading officials. According to *Supply Chain Management: A guide for Accounting Officers* (National Treasury, 2004:2-3), Accounting officers participate in the decision-making processes that determine how departments manage their assets and spend their financial resources.

In the light of the above, the *Regulatory Framework for Supply Chain Management* was promulgated in the *Government Gazette*, (Number 25767, on 5 December 2003 South Africa 2003a). This framework was developed in terms of Section 76 (4)(c) of the *PFMA*. The framework serves as a formal requirement to accounting officers to ensure the implementation of the Supply Chain Management process as an integral part of their financial systems. Supply Chain Management functions in the domain of the *Preferential Procurement Policy Framework, Act 5 of 2000* (South Africa 2000) and the *Broad Based Black Economic Empowerment Act, Act 53 of 2003* (South Africa 2003b).

Supply Chain Management refers to the procurement by an organisation of goods, products and services of the right quality, in the right quantities, at the right time and place. It consists of the following elements, according to the *Policy Strategy to Guide Uniformity in Procurement Reform Processes in Government* (National Treasury, 2003:21-24):

- demand management;
- acquisition management;
- logistical management;
- disposal management;
- risk management; and
- regular assessment of supply chain performance.

Supply Chain Management provides the interface between customers and suppliers in order to organise, source, stock and deliver supplies of materials, goods and services. According to Pauw *et al.*, (2009:249), the Supply Chain Management system is simply a chain that acts as a medium for the exchange of information and the communication of orders and instructions to ensure that the required goods or services are made available. Supply Chain Management is a relatively new field of study in the South African context. Although there are no substantial differences between the public and private sectors regarding challenges in implementing Supply Chain Management, it should be noted that

the public ownership of the public sector imposes a specific obligation on the public sector regarding public accountability. This has led to a number of legislative requirements and policy frameworks that prescribe the methods of procurement and treatment of suppliers. The *PFMA* is the overarching legislative policy document that imposes tendering rules. The legislation takes into consideration that Supply Chain Management contributes to the overall performance of an organisation by means of the control of resources in an effective, efficient and economical manner.

In order to achieve the ideals of good governance and to address deficiencies in public sector Supply Chain Management, it is important to have uniformity with regard to procedures, policies, documentation and contract options. The implementation of sound systems of control and accountability should form the cornerstone of institutional governance. In this regard, according to the *Policy Strategy to Guide Uniformity in Procurement Reform Processes in Government* (National Treasury, 2003:25-26), the organs of the state should adhere to a number of principles when dealing with appointed suppliers and/or potential suppliers. They should

- preserve the highest standard of honesty, integrity, impartiality and objectivity;
- be fair, efficient, firm and courteous;
- achieve the highest professional standards in the awarding of contracts, so as to maximise value for money while adhering to international standards;
- provide clear specifications of requirements which encourage innovation and refer, where appropriate, to relevant technical and other standards;
- make available as much information as suppliers may need to respond to the bidding process and to define and publicise procurement contract points;
- manage the bidding process so that genuine competition is preserved and discrimination is avoided;
- make available the broad criteria intended for the evaluation of bids, evaluate bids objectively, and notify bidders the outcome promptly;
- within the bounds of commercial confidentiality, debrief (un)successful bidders regarding the outcome of the bidding process in order to facilitate better performance on future occasions; and
- achieve the highest professional standards in the management of contracts.

In terms of the above, government expects private companies bidding for work to ensure that standards are not compromised. Furthermore, suppliers must demonstrate *good standing* as far as all their tax, levy and service charge obligations are concerned. This should be a prerequisite for conducting business with government. Failure to meet such obligations should be sufficient grounds for exclusion from participation in public sector procurement.

Role of the manager in the acquisition process

All public managers play a role in the procurement of goods and services, either as requisitioners or procurers. Acquisition management is where the *mapping-out* of the

procurement process takes place (Khan, 2006:7). During this phase, public managers play a role in the

- choice of procurement method;
- choice of the sourcing strategy to be followed;
- following of the procurement prescriptions in terms of the use of brand names, conditions that will have an impact on the adjudication, and the tax clearance of the supplier;
- advertisement of the item in the *Government Tender Bulletin* or other media;
- compilation of the general and special contract conditions;
- use of standard bid documents;
- vetting of the bid content, completion of bid documents and methods available for the invitation of bids;
- receipt and evaluation of responses; and
- awarding of the contract and service level agreement.

Any shortcomings or failings in procurement practices can result in large-scale losses of public money and goods through inefficiency, waste, fraud or corruption. An effective system of accountability for procurement would require the regulations relating to limits or authority to be clearly defined, the mechanisms to define situations requiring emergency purchases to be clearly spelt out and all transactions to be conducted in an open manner and with a proper audit trail. The actions of the procurement officers should be subject to periodic review, both internally by supervisors and externally by the independent auditors. Thus an effective system of accountability would require all public managers to be held accountable for proper procurement.

ETHICAL CONDUCT IN THE PUBLIC SECTOR

In public administration, there is a specific structure of ethics whereby each and every person has his or her own set of responsibilities. The first level is personal morality, which requires a person to apply his or her basic sense of right and wrong. This particular level is based on a person's personal integrity and his or her past and depends on factors such as parental influences, religious beliefs, cultural and social morals. Personal experiences are also part of the first level (Shafritz & Russel, 2005:85).

The second level deals with professional ethics (Shafritz & Russel, 2005:85). Public administration is built on and recognises a set of professional norms and rules that necessitate public managers to act in a professional manner. Such guidelines can be codified and captured in a code of conduct. According to a set of best practice guidelines such as the *Guide for Accounting Officers in terms of Supply Chain Management* and the National Treasury's Code of Conduct, all role players and public officials must comply with the highest ethical standards. These ethical standards should promote mutual trust and respect and create an environment in which business can be conducted with integrity and in a fair and reasonable manner.

UNETHICAL CONDUCT

An important concern in good governance is financial mismanagement and official corruption, because it frustrates development goals. Corruption sets in when public officials are, for example, paid *rent* in order to circumvent restrictions in terms of quotas, import restrictions or excise duty, to secure a contract, to permit a monopoly over a contract or to limit competition. Officials could then position themselves in areas where they can be bribed for various decisions or services or to turn a blind eye to certain illegal practices. Corruption undermines both development and democracy. According to the Public Sector Anti-Corruption Strategy developed by the Public Service Commission (South Africa, 2003c), the following are examples of the areas where corruption frequently manifests itself:

- bribery;
- embezzlement;
- fraud;
- extortion;
- abuse of power;
- conflict of interest;
- favouritism;
- nepotism;
- theft; and/or
- collusion.

Poor financial management includes corruption in all its manifestations as reflected above, since corruption implies either that public funds are misused or applied to benefit a select individual or entity, or that potential public funds are diverted away from the national revenue to private income (Fourie, 2006:437). According to the *Report on Financial Misconduct for 2006/2007* compiled by the Public Service Commission (South Africa, 2007), the total amount lost due to unauthorised, irregular, fruitless and wasteful expenditure and losses resulting from criminal conduct reported by the departments and provinces for the 2006/2007 financial year was R130 615 994,82.

ETHICAL CONSIDERATIONS IN PUBLIC SECTOR PROCUREMENT: CHALLENGES

The procurement environment is the area most susceptible to misconduct in any organisation. Because it is very important to suppliers to gain government contracts, the temptation for misrepresentation and favouritism is high. It is therefore important that a high level of integrity and awareness be maintained in the procurement environment. The *Code of Conduct for Supply Chain Management Practitioners* as issued in terms of the *Framework for Supply Chain Management* (South Africa 2003b) promulgated in accordance of Section 76(4)(c) of the *PFMA* provides directives to employees with regard to their relationship with all other role players.

Ethical considerations within the procurement system include the standards of behaviour that guide individual public managers in their work. These considerations also refer to the motivations directing the conduct and behaviour of personnel in public organisations and provide the necessary guidelines in public decision-making (Du Toit *et al.*, 1998:125).

The ethical role and functions that public managers perform include

- establishing and enforcing a high moral tone in institutions;
- developing mechanisms to encourage ethical behaviour through the institution (an enforceable code of conduct);
- rewarding proper behaviour;
- involving colleagues and the public in decision-making;
- establishing a balance between employee rights and management prerogatives;
- ensuring responsibility and accountability in a system of representative democracy; and
- disclosing wastage of resources, illegal activities and strengthening the public trust by protecting whistle blowers.

It should be noted that ethical or unethical actions in the procurement of goods and services by particular managers do not necessarily occur in a vacuum. The actions of peer managers and top managers, as well as the organisational culture, all contribute to the ethical context of an institution. Nevertheless, the starting point for an understanding of the ethical context of management is each individual's own ethical standards.

Managerial context

According to Wittig (1999:10-15), there are three areas of managerial activity that require special attention:

- The relationship between the public institution and the officials, where the behaviour of the manager defines the ethical standards according to which the institution treats its officials. This includes issues such as hiring, wages, working conditions and employee privacy. If a manager becomes aware of an unethical practice and allows it to continue, he/she has contributed to an organisational culture that conveys the message that such an activity is permitted. Managers who justify corrupt behaviour by looking the other way invoke double standards in which enforced laws become irrelevant.
- The relationship between public officials and the institution: Organisational practices may strongly influence the ethical standards of officials. Numerous ethical issues also surround the relationship of officials in the institution, especially in regard to conflicts of interest, secrecy, and honesty in keeping accounts.
- Interaction between the public institution and the community: The purpose of the public sector is to render services to the public, and high demands are made on public officials who have to render these services. They can expect that they will have to behave in an accountable and reliable manner. Management ethics implies

that the social responsibility of an institution is expressed through its management. Managers are responsible for determining the validity of each expectation and, at the same time, for providing the ethical basis for the decisions that are taken. Actions initiated by managers and the decisions managers make directly or indirectly influence the community and the environment in which the institution operates. In this case, managerial ethics also come into play in the relationship between the institution and outside groups, such as organised interest groups. Public managers should then implement their decisions fairly in the delivery of goods and services, be sensitive to needs and honest in the handling of the scarce public resources.

Challenges from the political milieu

Public managers involved in the procurement of goods and services are confronted with many challenges, especially from the political environment. The distinction between the administrative and political environment has become increasingly blurred, because the political environment is interfering more and more in the administrative environment (Mafunisa, 2006:506).

Public management is different from business management primarily because of the constraints imposed by the political environment within which the management processes are conducted. An important difference is that the ethical values and norms applicable to public organisations vary considerably from those private organisations. Political authority and public accountability are two ethical norms specifically for public institutions. Public institutions are subject to a very large range of legislative restrictions, controlled by the legislature, executive and judicial authorities and subject to criticism by the public at large.

In terms of the *Constitution* (South Africa 1996), civil servants' duty is to their political heads; they carry out ministerial instructions and ministers are answerable to the public, that is, to Parliament, for the management decisions that are made in their name. Some of the difficulties that have arisen, involving public criticism of named public servants, are the result of ministers' failing to act in accordance with accepted constitutional practices. Not only have ministers not accepted full responsibility for decisions made in their name, but ministers can intentionally mislead or misinform Parliament and its committees. In such circumstances, public managers have to decide where their duty lies: to Parliament (that is, the public) or to their minister. They have to make an ethical personal judgement about how they should behave. Apart from the questions of answerability and transparency, there is also the ethical issue of discretionary decision-making. Officials throughout the public service make management decisions involving discretionary judgements on individual issues or where conceptions of the national interest have to be adjudicated against private actions on a daily basis. Those making such judgements are expected to apply the highest possible standards.

The involvement of officials in management decision-making raises various ethical questions. It requires, inter alia, good people management skills and especially the ability to listen to lower levels of employees. It also requires good communication and

negotiating skills, since the opinions of employees have to be reconciled with those of management.

Colluding in public purchasing

Colluding or fronting in public purchasing can take many forms such as fronts on paper, company fronts, fictitious fronts and fronts in joint ventures (National Treasury, 2004:23-24, General Condition of Contract, Section 1.13). Conspiracy between two or more suppliers to forward identical tenders or the receipt of identical tenders due to an oligopolistic situation often occurs. It is not always easy to detect. It is therefore a challenge to procurement personnel to be aware of the conditions and situations that might occur. In this case, skilled and well-informed procurement staff is of the utmost importance in assessing procurement documents (Building Women, 2006:32-33).

Communication

It has been found that interpersonal communication is one of the greatest obstacles to maintaining ethical standards, especially where business originates in an underdeveloped part of the population. Poor communication goes hand in hand with prejudices, mistrust and expectations that cannot be met. In the South African context, the problem of communication and prejudices in the affirmative procurement situation may be much greater because white men who are accustomed to being the previously favoured strong suppliers to people of the same race and gender, have limited exposure to and little understanding of underdeveloped entrepreneurs. Purchasers may then accuse small suppliers of insisting on being awarded a contract simply because they are small and belong to disadvantaged groups.

Infrastructural issues

The current infrastructure with reference to the implementation of the preferential procurement framework is not conducive to matters such as the education of the Small, Medium and Micro Enterprises (SMMEs) on the bidding process. Some owners and managers of SMMEs have a limited educational background and the bid documents are not user-friendly. Indeed, in some instances, they are difficult to understand and interpret. Documents should be expressed in readily understood terms. Clear specifications and selection criteria will assist potential service providers to formulate bids appropriately. Where it is necessary to deviate from the criteria, bidders should be informed and educated properly regarding the reasons for the change as they would have formulated their bids on the basis of the predetermined selection criteria (Johnston, 1997:47). This will ensure transparency and ultimately contribute to ethical conduct in the procurement of goods and services. The training of SMMEs on how to engage in the tendering process should receive more attention in the light of unequal starting points.

CONCLUSION

The procurement of goods and services is a complex and dynamic system, but it is essential for the delivery of services and the promotion of sustainable development. Procuring goods and services is at the centre of the way in which public funds are used, since budgets are translated into services largely through the government's purchase of goods and services.

Ethical considerations are significant in the competent functioning of individual public departments and thus the entire economy. Dishonesty, fraud and corruption are an abuse of public office and pose a wide governing and administrative challenge. Moreover, unethical behaviour can be costly: the consequences of ignoring ethics are expensive in terms of opportunities that are lost and of economic inefficiency.

Managers should not only be aware of the various challenges in the procurement environment, but should also take a leading role in ensuring ethical conduct in the procurement of goods and services. All levels of management should seek to make improvements in order to enhance procurement's contribution to the overall strategic objectives of a given department. Furthermore, managers should act as role models in demonstrating ethical conduct in service delivery standards. Mechanisms should be in place to ensure that fronting or collusion are detected as soon as possible, and are reported. Internal and external communication strategies should be streamlined, not only to inform the relevant stakeholders, but also to educate them regarding the relevant procurement processes in an effort to prevent unethical conduct.

Public procurement systems can be at opposite ends of the spectrum: they can either add value to the economy or deplete it when corrupt, wasteful or unethical practices are common. In order to uphold ethical conduct in the procurement environment, a number of policies have been developed, but the implementation of these policies is limited by a number of challenges such as political interference and a lack of managerial skills, communication with suppliers and a well-skilled procurement work force. As the economy of the country grows, its procurement requirements will become more complex. If public sector procurement is to support economic growth, the workforce involved in procurement must have the ability to make informed judgements regarding the best products available to satisfy the requirements of government policies.

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