Supplier Control for Government Procurement

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Abstract — Currently, the government is one of the biggest and most reliable partners in business relationships. When the situation is unfavorable for the development of the national economy, the importance of the state increases, which leads to the increased need for its security, economical one included. Thus, one of the activities of state customers using the government procurement mechanism becomes a way of providing an indirect impact on the economy and a way of governmental control. This mechanism implies the interaction between state customers and numerous contractors. Suppliers make up a small proportion of contractors, and they interact with state customers on a daily basis.

Keywords: government procurement, supplier control, agricultural produce, high-risk areas, auditing methods

I. INTRODUCTION

State needs are defined according to the requirements of the Russian Federation and its constituents in agricultural produce, raw materials, and food. The purchase of agricultural produce for state needs is performed in order to implement state programs for agribusiness development and other economic and social initiatives aimed at providing the population with food; facilitating the export of agricultural produce; organizing state reserves for agricultural raw materials and food, etc. Implementing their authorities and functional duties by the state customer alone is impossible nowadays, and therefore it enters into agreements with contractors in order to perform its functions successfully and efficiently. The economic security of the state customer is largely predetermined by the relationships with contractors, formalized in signed agreements and contracts. However, before entering into an agreement, the state customer should make sure its future purchasing partner is reliable. Today, contractors' cheating and fraud during the fulfillment of their contractual obligations are becoming a usual thing. Many business entities are striving to sign contracts by deceit in order to receive personal benefits, even if inflicting economic damages to the state customer. Some of the contractors do not fulfill their obligations on purpose, while others do it because they have overestimated their own capabilities. Therefore, the assessment of contractors’ reliability, diligence, responsibility and assiduity is a key element of ensuring the economic security for the state customer. At the moment, contractual system legislation for government procurements does not regulate standard assessment procedures for contractor, aka procurement participants. Legal requirements for the procurement participants are put to work in order to filter the contractors, but they cannot help to work out a clear profile of a potential contractor. The existing assessment methods used by state customers when they are auditing procurement participants do not allow this as well. To make matters worse, the existing legislation does not require that the state customer shall audit its potential contractors. It only allows this, and it is a right that is sometimes neglected. State customers employ both large companies and individual businesses in order to maintain the sustainable development of small and medium enterprises. It must be understood that every contractor (procurement participant) shall be picked very carefully in order to avoid risks and threats to economic security, as well as to protect the state customer.

II. SPECIFIC FEATURES OF GOVERNMENT PROCUREMENTS OF AGRICULTURAL PRODUCE

The purchase of agricultural produce can be described as the purchase of this kind of product for producers by the government for the purpose of their further processing and sale. The procurement stands for the contractual relationships between the commodity producers (suppliers) and buyers (consumers) of the finished agricultural products and food. State needs are defined according to the requirements of the Russian Federation and its constituents in agricultural produce, raw materials and food [1].

The agricultural produces supplied to satisfied the state needs must comply with quality standards, biomedical requirements, sanitary norms, and contractual terms. Purchase and procurement amounts shall be defined by the government of the Russian Federation and the executive authorities of its constituents for a five-year period with amendments made every year but no later than six months prior to the beginning of the year and with notifying the state customers [2].

State customers in their turn shall inform the supplier of agricultural produce about the amounts of purchase and procurement, along with the product list within three months prior to the beginning of the year.

Commodity producers in horticulture receive guarantees from the government of the Russian Federation and the executive authorities of its constituents, including the
advance payments of no less than 50% of the procurement amount prices stated in the governmental contract, 25% after the governmental contract is signed and the rest once the sowing is finished. As for livestock farming and its products, the producers shall receive funding from the respective budget to improve their cost-effectiveness [3].

Yet another feature of government procurement of agricultural produce is that if encashment payments are used, the payment period is 10 days of the acceptance of the payment documents in the payer's bank or 5 days for perishable products.

The liability for non-performance or improper performance of contractual obligations for the purchase of agricultural produce, raw materials and food to satisfy state needs (article 8 of the Federal Law) is also quite specific.

Firstly, in case of a breach of procurement or purchase (acceptance) obligations for agricultural produce, the guilty party shall pay the contractor a penalty of 5-10% of the price of the short-delivered or unaccepted goods.

Secondly, the untimely payment for the purchased (procured) horticultural produce shall result in the state customer (buyer) paying a penalty (fine) to the commodity producer to the amount of 2% of the price for the untimely-paid products per each day of default; if the payment is over 30 days late, it shall be 5%.

The state customer can reject the purchase of agricultural produce as stated in the contract only under the condition of complete compensation of the damages incurred by the commodity producer (supplier) through the state customer.

III. DETERMINING HIGH-RISK AREAS WHILE SELECTING CONTRACTORS BASED ON SPECIFIC AUDITING METHODS

The auditing activities of state customers in order to assess their contractors differ from those employed in business companies. However, the experience shows that the methods for auditing potential contractors used in business companies are much more efficient because these methods and the scope of assessment are a lot wider and more complex [4].

In general, the purchasing activity of state customers is the same as that of purchasing departments in businesses. The difference is that the former can only use the state budget and the purchasing process is implemented according to special government-made procedures prescribed by the Government Procurement Law. [5]

Besides, while state customers use their authority, they address economic, political, social, and ecological issues. However, the solution of such problems depends on the professional qualities of the state customers: only efficiently arrange government procurements can benefit the entire society, i.e. all citizens who funded the activities of the state customer.

State customer activities inevitably imply signing governmental contracts with companies of various types. The government contract stands for an agreement that is aimed at satisfying some state needs and one of the parties on which represents the Russian Federation or one of its constituents. Government contract making may result in certain risks and economic security threats for the state customer and it is of primary importance because its successful execution influences the budget savings and the application of funds. [6]

The other party of a governmental contract is an executive agent, i.e. a contractor. A contractor stands for a person or entity that can accept obligations stated in the governmental contract.

State customers employ both large companies and individual businesses in order to maintain the sustainable development of small and medium enterprises. It must be understood that every contractor (procurement participant) shall be picked very carefully in order to avoid risks and threats to economic security, as well as to protect the state customer.

One of the key factors in contractor due diligence used in business companies is the contractor's lack of negative experience. Finding this out helps determine the high-risk areas, including economic threats. A widely-used method for this type of test is a post-hoc analysis of the data presented on the Commercial Case File website. [7]

The aforementioned factors shall be taken into consideration while selecting a supplied in order to make rational and efficient decisions concerning the making of governmental contracts. It is possible that state customers do not use thorough due diligence procedures to test their potential and real contractors not only because they are irresponsible, but also due to the fact that the making of governmental contracts uses budgetary funding, not their own money. Business entities use their own money to pay for contracts and they are very careful about selecting a contractor because they realize that questionable deals may lead to significant economic losses for them.

The problem of selecting diligent and reliable suppliers is becoming more and more pressing nowadays. According to contract legislation for procurements, contractors shall be selected if they satisfy a number of requirements.

The existing standard requirements for procurement participants do not allow state customers to fully ascertain the efficiency, safety, and rationality of a contractor selection. [8]

Relationship building practices for a state customer and a contractor is first and foremost aimed at the reduction of material costs. In other words, the key indicator of procurement efficiency is the economy of budgetary funds, and the key criterion of tender assessment is the price. Thus, an unreliable contractor can win the tender if they offer the best contract price. Since the price is the most important criterion, the state customer has a limited opportunity to select a more rational and beneficial offer. [9] Due to this, the contractor’s professionalism shall be considered a key criterion.

Currently, the procurement law states that licenses to perform certain activities shall be the key factor in determining a contractor’s professionalism. However, we claim that a contractor's professionalism should be also determined based on such factors as their working experience in the area of the contract, employment of
properly qualified specialists, necessary facilities (premises, equipment, etc).

The existing legislation requires checking the experience of procurement participant only in the cases described in the Decree of the government of the Russian Federation of 04.02.2015 N 99 On additional requirements for the participants of the purchase of certain types of products, works and services that can only be supplied, produced or performed by contractors (suppliers, executive agents) with the necessary qualification due to their technical and (or) technological complexity, innovative, high-tech or specialized nature, and on the documents that prove the compliance of the procurement participants with the additional requirements.

We deem necessary that this factor should be made one of the obligatory requirements for all of the procurement participants, except cases when the subject of the contract is not related to the key activities of the state customer. This factor shall be included in clause 12 part 1 article 31 of the government procurement law in the following way: “procurement participants shall have over 80% of positive experience in contract fulfillment for the three years prior to submitting the application for the government procurement. These must include the work in the same area as the contract and proved by providing a copy (copies) of a previously executed contract (contracts), agreement (agreements) and a progress statement (statements).” Two other factors that help expose procurement participants' professionalism shall be included in the government procurement law as obligatory in a similar way. Clauses 2 and 4 part 2 article 31 of the government procurement law shall be moved to clauses 13 and 14 part 1 article 31 of the same law respectively. While auditing their potential contractors, business entities request their accounting reports (form 1 and form 2). With these data at hand, conclusions can be made about the financial responsibility and well being of the contractor. It is important because they might not be able to pay the fines if they fail to fulfill their contractual obligations. [10], [11]

Thus, part 1 article 31 of the Government Procurement Law shall be complemented with clause 15: “sufficient financial solvency and well-being of a procurement participant that is necessary for the fulfillment of their obligations”. Compliance confirmation for this requirement shall be provided by the procurement participant in the form of accounting reports (form 1, form 2). If this factor is used as an obligatory requirement, the government customer will be able to decide, among other things, whether the procurement participant is capable of paying in tender security or contract execution.

Besides, we think that the current legislation must be complemented with an obligatory requirement to check procurement participants for regular previous non-fulfillment or improper performance of obligations associated with government contracts or third-party contracts. Good business standing of the contractor shall be yet another obligatory assessment factor. This factor shall be included in clause 16 part 1 article 31 of the government procurement law in the following way: “procurement participants shall provide information about their business partners alongside with their feedback on the quality of obligation fulfillment by the participants for three years prior to the date of application”.

Currently, contractors verify their compliance by providing a declaration of conformity for procurement participants [12]. The problem is that at the moment there are no uniform requirements concerning the filling-out of this document. Therefore, procurement participants fill it out differently and provide excessive information for some points and insufficient for others. This calls for the development of a uniform template that would help procurement participants fill in the declaration of conformity for government procurements.

It must be noted that the declaration provided is currently authorized by the company CEO only, which increases the possibility of providing false data. Taking into consideration the abovesaid, clause 1 part 1 of article 31 of the government procurement law shall be complemented with a requirement that a procurement participant shall submit declared information on their compliance with specified requirements authenticated with a signature and a seal of the legal entity manager or sole proprietor, and tax statements and penal clearance certificates attached that were issued no later than 10 days of the deadline for purchase participation applications. Certificates shall be provided in order to verify the declared compliance with the requirements set out in clauses 5 and 7, part 1 art. 31 of Government Procurement Law.

Summing up the improvement suggestions for the government procurement law, we can harmonize the factors influencing the selection of product (work, service) suppliers in order to maintain the economic security of government customer. This system is presented in Table 1.
Thus, the factors suggested above shall be formalized as separate clauses in part 1 of article 31 of the Government Procurement Law. Formalizing these factors in legislation will allow the government customer to work out a more comprehensive and objective opinion of the procurement participant and take a more rational and economically feasible decision, concerning the selection of a better contractor.

Along with amending the Government procurement law by putting stricter requirements to the procurement participants into practice, part 8 of article 31 of the Government procurement law shall be modified so that the procurement commission would have a right to require participants’ compliance with the law.

The suggested system of factors influencing the selection of a supplier that would not endanger the economic security of the government customer shall be subject in verification by the government customer along with the existing uniform requirements for procurement participants. In case of simultaneous detection of risks and economic security threats from the potential contractor that would influence the execution of the contract and when no breaches of procurement regulations are found, the government customer should refuse further cooperation with the participant. The methods and information sources for the verification of suggested factor compliance data provided by the potential contractor are presented in Table 2.

Thus, Table 2 shows that the government customer can test the procurement participant for the compliance with the suggested factors using the following methods: inspection, data comparison, observation, formal assessment, vertical and horizontal data analysis, polling.

IV. CONCLUSION

To sum up, the existing procurement contract legislation has some loopholes in terms of setting the requirements for procurement participants and methods of their assessment. The suggested factors influencing the selection of suppliers in order to maintain the economic security of a government customer is aimed at minimizing the risks and threats of non-performance or improper performance of contractual obligations by the contractors.

REFERENCES


