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**Public Procurement and SMEs**

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This briefing paper provides a general overview of SME performance in securing public procurement contracts. It also looks at some of the barriers encountered by SMEs in relation to the public procurement process, including the particular problems faced by the social economy sector.

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# Public Procurement and SMEs

## Introduction

Public procurement covers a wide range of supplies, services and works required by governments, local authorities and public organisations, utilities and agencies. The size of such contracts varies hugely. Whilst some are beyond the capabilities of SMEs<sup>1</sup> to fulfil, a significant proportion of the public procurement opportunities in Europe are well within the scope of SMEs. With a market in the EU estimated at around 16% of GDP, or about €1,800 billion in 2006, public procurement contracts represent a major opportunity for very many enterprises.<sup>2</sup>

The public sector in Northern Ireland spends approximately £1.7bn out of a total budget of £7bn each year on public procurement. While it is impossible to detail the full range of works, goods and services that these public bodies purchase, the most common procurement are: Accountancy/Audit; Banking; Bottled Water; Catering Equipment; Catering Services; Cleaning Services; Clothing and Footwear; Construction/Maintenance Services; Facilities Management; Food Products and Beverages; Furniture and Fittings; ICT Equipment; Information and Computer Technology Services; Laundry Services; Legal Services; Medical and Laboratory Devices; Medical Surgical Equipment and Supplies; Office Machinery; Pharmaceuticals; Plant and Machinery; Post Office Counters; Protective Wear; Repair, Maintenance and Installation Services; Tools, Equipment and Building Materials; Training Services; and Uniforms.<sup>3</sup>

## The Experiences of SMEs in Public Procurement

SMEs' access to public procurement varies from one Member States to another. In 2005, SMEs secured 42% of the value and 64% of the number of contracts above the thresholds fixed by the EU directives on public procurement.<sup>4</sup> The directives cover roughly 16% of the EU public procurement market. SMEs tend to perform better in bidding for central government contracts and less well in the old Member States compared with the new. It is also interesting to note that medium sized companies perform much better than small and micro companies.<sup>5</sup>

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<sup>1</sup> Companies classified as small and medium-sized enterprises (SMEs) are defined officially by the EU as those with fewer than 250 employees and which are independent from larger companies. Furthermore, their annual turnover may not exceed €50 million, or their annual balance sheet total exceed €43 million. This definition is critical in establishing which companies may benefit from EU programmes aimed at SMEs, and from certain policies such as SME-specific competition rules.

<sup>2</sup> "Opening public procurement to SMEs", European Commission Enterprise and Industry DG - [http://ec.europa.eu/enterprise/entrepreneurship/public\\_procurement.htm](http://ec.europa.eu/enterprise/entrepreneurship/public_procurement.htm)

<sup>3</sup> "Public Procurement – a guide for social economy enterprises", Central Procurement Directorate, Department of Finance & Personnel - <http://www.cpdni.gov.uk/social-economy-enterprises-guidance-pdf.pdf>

<sup>4</sup> See OGC website for information on latest EU procurement thresholds - [http://www.ogc.gov.uk/procurement\\_policy\\_and\\_application\\_of\\_eu\\_rules\\_eu\\_procurement\\_thresholds.asp](http://www.ogc.gov.uk/procurement_policy_and_application_of_eu_rules_eu_procurement_thresholds.asp)

<sup>5</sup> "Opening public procurement to SMEs", European Commission Enterprise and Industry DG - [http://ec.europa.eu/enterprise/entrepreneurship/public\\_procurement.htm](http://ec.europa.eu/enterprise/entrepreneurship/public_procurement.htm)

In 2004, the EU Council and Parliament adopted a package of directives on public procurement designed to reduce the administrative burden and costs related to tendering, make procurement systems more transparent and easier for SMEs (in particular) to access, and encourage the use of information technology systems (e-procurement) to simplify the process. These directives were due to be transposed into national law in all Member States by January 2006.

To facilitate this ongoing process, within the framework of the European Small Business Act (introduced by the Commission on 25 June 2008)<sup>6</sup> the European Commission proposed a Code of Best Practices to assist SMEs in the public procurement process. The Code encourages Member States to learn from each other as they implement the new rules under the public procurement directives. The Small Business Act also includes 10 principles to guide the conception and implementation of policies at EU and Member State level. These policies include granting a second chance for business failure, facilitating access to finance and enabling SMEs to turn environmental challenges into opportunities.<sup>7</sup>

Despite actions taken at both EU and national level, there are still many barriers which discourage SMEs from responding to these EU-wide tenders. These include basic difficulties in finding information about tenders, or about the procedures for bidding, or there are problems in understanding jargon; too short a deadline for responding and/or the costs of responding are too high; the administrative procedures are too complex, or particular certification is required; a high financial guarantee is required to bid; or companies may face discrimination on the basis that they are located in a different country from the contracting authority.<sup>8</sup>

A recent report on the experience of European SMEs, entitled *“Evaluation of Small and Medium-Sized Enterprises’ (SMEs’) Access to Public Procurement Markets”*, highlighted the problems faced by SMEs. The study was undertaken by GHK and Technopolis between April and September 2007 on behalf of Directorate-General Enterprise and Industry.<sup>9</sup>

The study found that the most frequent problem faced by European SMEs in bidding for public procurement tenders is the over-emphasis placed on price by awarding authorities (52% of the companies encountered this either ‘regularly’ or ‘often’). Onerous paperwork requirements were also mentioned as a common problem (46%).

The use of e-mails as a preferred channel of communication, improving tender specifications and documentation, as well as improving information on tenders in general were seen as the three most helpful actions that awarding authorities could do. Training

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<sup>6</sup> See [http://ec.europa.eu/enterprise/entrepreneurship/sba\\_en.htm](http://ec.europa.eu/enterprise/entrepreneurship/sba_en.htm)

<sup>7</sup> See European Commission Press Release IP/08/1003 - <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/1003&type=HTML&aged=0&language=EN&guiLanguage=en>

<sup>8</sup> “Opening public procurement to SMEs”, European Commission Enterprise and Industry DG - [http://ec.europa.eu/enterprise/entrepreneurship/public\\_procurement.htm](http://ec.europa.eu/enterprise/entrepreneurship/public_procurement.htm)

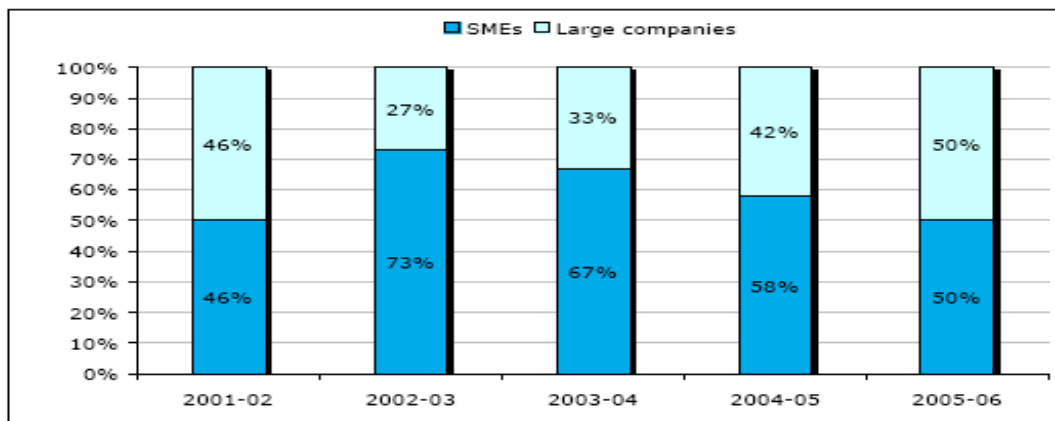
<sup>9</sup> “Evaluation of SMEs access to public procurement” Final Report produced by GHK and Technopolis on behalf of European Commission Directorate General Enterprise and Industry [http://ec.europa.eu/enterprise/entrepreneurship/docs/SME\\_public\\_procurement\\_Summary.pdf](http://ec.europa.eu/enterprise/entrepreneurship/docs/SME_public_procurement_Summary.pdf)

for companies, the use of framework agreements and contracts, and more time to draw up tenders were less frequently emphasised.

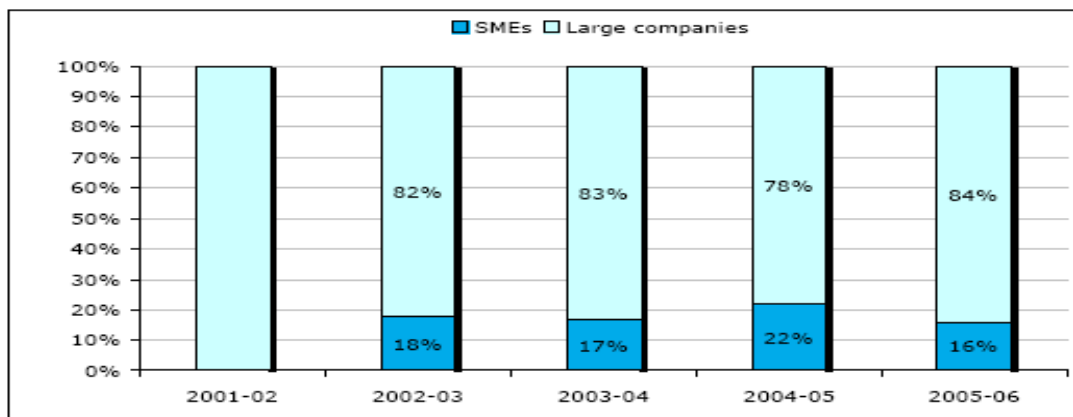
Overall the study findings suggest that there is still scope for improvement in the performance of SMEs in public procurement. The report therefore recommended that steps should be taken to: reduce differentials in access between SMEs, and in particular small and micro-enterprises, and larger companies; exchange experience and encourage peer learning activity amongst Member States and awarding authorities; and, improve the information and research base.

Within the UK, there has been a decline in recent years in the number of contracts being awarded to SMEs following an initial leap in 2002/03 in reaction to the work carried out by the Office of Government Commerce (OGC) and government reviews (Figure 1). Whilst the number of contracts awarded to SMEs has been relatively high, the total value has consistently remained around the 20% mark (Figure 2).<sup>10</sup>

**Figure 1. Share of number of UK public sector contracts awarded by company size**



**Table 2. Share of value of UK public sector contracts awarded by company size**



<sup>10</sup> Annex to Final Report “Evaluation of SMEs access to public procurement” produced by GHK and Technopolis on behalf of European Commission Enterprise and Industry DG, Section on United Kingdom - [http://ec.europa.eu/enterprise/entrepreneurship/docs/SME\\_public\\_procurement\\_Annex.pdf](http://ec.europa.eu/enterprise/entrepreneurship/docs/SME_public_procurement_Annex.pdf)

In 2003, the Better Regulation Task Force (BRTF), in collaboration with the Small Business Council (SBC), set out with the aim to “counter the excessive burdens on small businesses”. Their report “*Government: Supporter or Customer?*” was produced in reaction to the fact that whilst SMEs are very important to the UK economy (99% of all businesses) they are underrepresented in public procurement contracts. The report aimed to consider the barriers that face SMEs when doing business with the public sector and the wider benefits to the economy when procuring from SMEs. Eleven recommendations were put forward in the report to be carried out by procurement offices both at the national and local government levels.<sup>11</sup>

#### **Recommendation 1**

- The DTI should ensure adequate resources for the "Supplying Government" web portal project. The portal should advertise lower value contracts from across central government and include information on future contract opportunities. There should be a named contact for each advertised contract. The portal should be set up and piloted by spring 2005.

#### **Recommendation 2**

- The Office of the Deputy Prime Minister and the Local Government Association should encourage local authorities to develop "selling to the council" websites by 2005. Websites should include information on contracts for tender, forthcoming contract opportunities and guidance on how to do business with the council. There should be a named contact for each advertised contract.

#### **Recommendation 3**

- Within the context of small business support, the Small Business Service should provide advice and training for small and medium-sized enterprises on how to do business with central government and local councils. The Business Links Operators should deliver this by spring 2004.

#### **Recommendation 4**

- Regional Development Agencies should ensure by spring 2004 that, as part of the supply chain development work for which they are already funded, they work with prime public sector contractors to develop opportunities for small and medium-sized enterprises.

#### **Recommendation 5**

- The public sector should develop a common core pre-qualification information document for lower value contracts so that businesses do not have to put together different information in different formats to get past the expression of interest stage. The Office of Government Commerce and the Office of the Deputy Prime Minister working with the Local Government Association should develop and pilot this by spring 2004.

#### **Recommendation 6**

- The Small Business Service should publicise the mechanism for reporting non-compliance with the Office of Government Commerce "Government Procurement Code of Good Practice" that firms can use to ensure that they receive adequate debriefing.

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<sup>11</sup> Annex to Final Report “Evaluation of SMEs access to public procurement” produced by GHK and Technopolis, Section on United Kingdom - [http://ec.europa.eu/enterprise/entrepreneurship/docs/SME\\_public\\_procurement\\_Annex.pdf](http://ec.europa.eu/enterprise/entrepreneurship/docs/SME_public_procurement_Annex.pdf)

**Recommendation 7**

- The Office of Government Commerce, the Office of the Deputy Prime Minister with the Local Government Association should consider how to promote the wider use of the Government Procurement Card, recently extended by the Office of Government Commerce, to include local authorities and other non central civil Government bodies, in order to improve prompt payment by the end of 2003.

**Recommendation 8**

- The Office of Fair Trading should carry out research to identify the characteristics of those markets where it is important to ensure that small and medium-sized enterprises are able to compete to ensure competition, particularly where this may have an impact on innovation and value for money achieved by public sector procurement. Within this, it should also assess the impact of framework agreements and contract aggregation on small and medium-sized enterprises.

**Recommendation 9**

- Where public sector procurers opt for prime contractors, they should ensure that their business case for doing so in those particular markets brings value for money. Public sector procurers should ask prime contractors during the procurement process to demonstrate their track record in achieving value for money through effective use of their supply chain – including use of small and medium-sized enterprises. This should also be examined as part of the on-going contract management. Public sector procurers should ensure that prime contractors pay subcontractors on time and that when paying progress payments to prime contractors the payments flow down through the supply chain. In order to make subcontracting opportunities more transparent to small and medium-sized enterprises, Government Departments and local authorities should list details of prime contractors and contracts on their websites.

**Recommendation 10**

- The Local Government Procurement Forum, with input from the Small Business Service, should develop an SME-friendly procurement concordat. All local authorities should be able to sign up to this by 2005.

**Recommendation 11**

- The Office of the Deputy Prime Minister and the Local Government Association should encourage local authorities to set out in their procurement strategies the steps they are taking to engage with small and medium-sized enterprises by the end of 2003. Government Departments should include in their procurement policy statements the steps they take to engage with small and medium-sized enterprises by the end of 2003 or publish this information in their annual reports.

Most of these recommendations have now been acted upon by local and national bodies. Guidance has also been published by the OGC and by the respective regional procurement bodies with the aim of overcoming the barriers faced by SMEs and to help realise the benefits of involving them in public procurement contracts.

Recent research, however, by a company called Freshminds, suggests that more still needs to be done to address the problems faced by SMEs in relation to public procurement. Their findings included the following:<sup>12</sup>

- Nearly three quarters of SMEs rarely or never bid for government work.
- Over three quarters of SMEs believe that there are barriers to awareness of government opportunities.
- Over half of SMEs feel that the process of tendering for government contracts requires more time and resource than their business can allow.
- On average, SMEs find the private sector easier to sell to than the public sector – their rate of success in winning private sector contracts is double their rate of success in winning public sector contracts.
- Nearly three quarters of SMEs feel that the public sector is more difficult to deliver work to than the private sector, due to a greater amount of formality, a lack of responsiveness and unrealistic timescales.

In addition to recommending a number of practical steps for SMEs to take (in terms of identifying opportunities, preparing for bids, and meeting customer needs), the researchers recommended a number of ways in which Government could continue to work to improve the procurement process for SMEs:

- *Improve SME access to information on public procurement opportunities* - Whilst considerable progress has been made, it is imperative to develop one single point of reference for SMEs to find information about bidding opportunities available to them.
- *Simplify and clarify the bidding process* - Existing portals are known to confuse some applicants. The Government needs to move towards simplifying the procurement process from start to finish, both in terms of the administrative burden and the use of accessible language.
- *Reduce bureaucracy (compliance demands)* - Efforts to reduce the bureaucracy for SMEs should impact both the time spent to amalgamate information required in bids as well as the level of contractual compliance required by procurers, which is often prohibitive for small companies.
- *Make the process more transparent* - Some SMEs still perceive some procurement bias, particularly towards lower cost options. Procurement needs to continue to become more transparent, selecting on the basis of value for money.
- *Provide appropriate support schemes for SMEs* - Guidance documents and 'Meet the Buyer' events can be extremely valuable for SMEs in improving their chances of winning a contract.
- *Introduce innovative measures such as performance bonds and contract banding to combat the perceived risk associated with SMEs* - Any reduction of the risks associated with contracting with SMEs would likely result in an increase in procurement from these companies.

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<sup>12</sup> "Evaluating SME experiences of Government procurement", Report by Freshminds for the Scorecard Working Party – a joint initiative between the British Private Equity and Venture Capital Association (BVCA), Federation of Small Businesses (FSB), and Confederation of British Industry (CBI), October 2008.

- *Provide constructive and clear feedback on lost bids* - Some public sector organisations are still not providing timely and appropriate feedback to SMEs, which makes improving their future chances of winning bids more difficult.
- *Support the expertise of public sector procurement professionals* - The greater the skills and experience that procurement professionals can apply to their job, the more likely the process is to be transparent and appropriate.
- *Make delivery terms and conditions more adaptive to the needs of the SME supplier* - SMEs are often less able to cope with prolonged periods of financial insecurity; simply paying invoices in a timely manner and speeding up the contractual process would benefit smaller companies.

## **The Social Economy Sector**

The social economy includes co-operatives, mutual societies, non-profit associations, foundations and social enterprises. From the village farmers who set up a co-operative to market their produce more effectively to the group of savers who set up a mutual to ensure they each receive a decent pension, by way of charities and organisations offering services of general interest, the social economy touches a huge range of individuals across Europe. There are around 10 million jobs in the social economy across Europe, but membership of social economy enterprises is much wider, with estimates ranging as high as 150 million.<sup>13</sup>

Different Member States have different traditions, so the forms of enterprise and the fields in which they are active vary across Europe, but there are few areas where the social economy has no interest. Co-operatives are prominent in fields such as banking, craft industries, agricultural production and retail. Mutual societies are found in the insurance and mortgage sectors, whilst associations and foundations are active in health and welfare services, sports and recreation, culture, environmental regeneration, humanitarian rights, development aid, consumer rights, education, training and research. Whilst some social economy enterprises provide services on behalf of or instead of the public sector, for example healthcare and social services, others produce products or services sold on the open market in competition with investor-driven companies. In such circumstances, the social economy is an important player in ensuring effective competition and it is therefore vital that regulation takes full account of the specific characteristics of such enterprises.

The social economy sector is big business in the U.K. with at least 15,000 social enterprises contributing some £18 billion to the economy. While Northern Ireland has some baseline data for nearly 400 SEEs with a turnover of just over £355 million (DETI Survey 2007), information on the actual size of the sector is limited.<sup>14</sup>

The social economy sector in Northern Ireland includes a range of organisations such as credit unions, housing associations, local enterprise agencies, community businesses, co-operatives, employee-owned businesses, community development finance initiatives, social entrepreneurs and social firms. Given its relatively low visibility to date and

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<sup>13</sup> “Europe’s social economy”, European Commission Enterprise and Industry DG - [http://ec.europa.eu/enterprise/entrepreneurship/public\\_procurement.htm](http://ec.europa.eu/enterprise/entrepreneurship/public_procurement.htm)

<sup>14</sup> Social Economy Network briefing to Enterprise, Trade & Industry Committee, 13 November 2008.



diversity, no firm figures are available to quantify the overall size and scale of the sector. A rough estimate of employment was carried out in June 2000 which indicated a range of between 30,000 and 48,000 jobs (5 - 8% of total employment). However, this was based on different definitions. It is now recognised that this is a relatively limited way of measuring the sector and work is now underway to develop a robust set of baseline figures for the size and scale of the sector as a way of benchmarking against the social economy in the UK and in other regions and to measure growth.<sup>15</sup>

According to the Social Economy Network (SEN), the sector is not as well developed in Northern Ireland as in England and Scotland.<sup>16</sup> They believe that one of the most significant problems facing the development of Social Economy Enterprises (SEEs) in Northern Ireland is the lack of progress on the inclusion of social clauses into the procurement process.

SEN also argue that there is evidence that social enterprises, particularly smaller ones, are at a disadvantage compared with private sector businesses in this arena. There is a limited knowledge of the social economy sector and its potential as a provider of goods and services among public sector procurement personnel. A programme of awareness raising and training is required to ensure that social economy enterprises are equally considered with the private sector in procurement considerations.

Social enterprises with little or no experience of doing business with the public sector also need practical advice and training on procurement procedures and writing tenders so that they can acquire the necessary skills to enable them to take advantage of the opportunities presented.

SEN welcomes the actions proposed by the Central Procurement Directorate to provide information and advice sessions on the tendering process and to organise "Meet the Buyer" events to increase opportunities for SEEs to do business with the public sector.

However, it is their view that SEEs operate their businesses in a market place which does not recognise or take account of the added value they create and this puts them at a disadvantage when competing for public sector business.

The social economy sector is further disadvantaged by the emphasis in consideration of tenders, on financial capacity demonstrated by a build up of reserves in assessing the financial health of companies. This particularly affects those companies in the early stages of development who were prohibited from building up reserves while in receipt of grants. SEN argues that if there is to be equality of opportunity in accessing tenders then it must be acknowledged that existing means and criteria are exclusionary to SEEs and that amendments to criteria must be introduced to create a level playing field.

Some additional problems faced by SEEs who have successfully secured tenders for the delivery of services include the length of time the process takes; and the fact that the level of finance available for service delivery this year, in the health and social care field, is set at 3% less than the cost of delivering the same service last year. Departmental

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<sup>15</sup> "Public Procurement – a guide for social economy enterprises", Central Procurement Directorate, Department of Finance & Personnel - <http://www.cpdni.gov.uk/social-economy-enterprises-guidance-pdf.pdf>

<sup>16</sup> Social Economy Network briefing to Enterprise, Trade & Industry Committee, 13 November 2008.

efficiency savings were not intended to affect front line services but it appears that in such instances they will. It is also argued that pressure on public bodies to secure efficiencies by aggregating contracts will discriminate against small businesses, including many social enterprises.

The Social Economy Network (SEN), in its recent presentation to the Enterprise, Trade and Investment Committee, proposed the following actions to help SEEs:

- Inclusion of social clauses into public procurement specifications to ensure a more equal playing field;
- Adoption of a consistent approach to the measurement of social value which can be embedded in the practice and processes of public procurement; and
- Exploration of innovative ways of increasing business opportunities for SEEs through public/social partnerships and private/social partnerships.<sup>17</sup>

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<sup>17</sup> Social Economy Network briefing to Enterprise, Trade & Industry Committee, 13 November 2008.