

# The Public Procurement System: A Business Sector Perspective

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The Public Procurement System:  
A Business Sector Perspective

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## The Public Procurement System: A Business Sector Perspective

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### **Abstract:**

This study empirically evaluates the public procurement system in Croatia, a transition country and a new EU member state. The research is based on empirical evidence collected by surveying a large sample of companies. It investigates how businesses as actors in the public procurement tenders evaluate the system and what their perceived and experienced views are on the various components of public procurement. The baseline model borrows from the literature by including companies' characteristics in terms of company size and sector of business operations. Furthermore, it assumes that there are significant differences in attitudes and ratings among companies that have participated in public procurement as direct suppliers compared to companies that have been indirectly involved as subcontractors. The business opinion on the public procurement system procedures and regulations has been assessed as well, providing insights into the business perceptions on main public procurement principles: accountability, effectiveness, value for money, integrity and achieving the EU standards. Special attention has been dedicated to the assessment of corruption risks in public procurement. The evidence for Croatia reveals that in spite of the EU standards introduced there are still, at least from the point of view of companies, irregularities and lack of trust in the national public procurement system.

**Keywords:** public procurement, survey, Croatia, business attitudes

**JEL classification:** D22, H83, K20, L51

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## Sustav javnih nabava iz perspektive poslovnog sektora

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### **Sažetak:**

U radu se empirijski ocjenjuje sustav javnih nabava u Hrvatskoj, tranzicijskoj zemlji i novoj članici Europske unije. Anketni podaci prikupljeni na velikom uzorku poslovnih subjekata omogućili su istraživanje stavova poduzeća u ulozi sudionika natječaja javne nabave: kako ona ocjenjuju sustav te koje su njihove percepcije i iskustva povezana s pojedinim sastavnicama javnih nabava. Model polazi od postojećeg koncepta iz literature koji razlikuje poduzeća prema veličini i djelatnosti i proširuje ga s još jednim važnim obilježjem ispitanika: je li poslovni subjekt sudjelovao u javnim nabavama kao izravni ponuđač ili kao podugovarač. U radu se provjerava hipoteza da postoje značajne razlike u mišljenju i ocjenama između izravnih ugovarača i podugovarača. Struktura ankete omogućila je ispitivanje stavova poslovnog sektora o postupcima javnih nabava, regulativi, poštivanju glavnih načela javne nabave, dosegnutim europskim standardima i razini korupcijskih rizika u javnim nabavama. Iskustva Hrvatske prema mišljenju poslovnog sektora ukazuju da su usprkos uvođenju EU normi još uvijek prisutne nepravilnosti i manjak povjerenja u nacionalni sustav javnih nabava.

**Ključne riječi:** javna nabava, anketa, Hrvatska, stavovi poslovnog sektora

**JEL klasifikacija:** D22, H83, K20, L51



# 1 Introduction

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Public spending makes up a significant portion of national economies, and in most countries government procurement of goods and services accounts for 15 to 20 percent of gross domestic product (GDP). While in OECD countries this figure is 12 percent on average, developing and emerging economies often spend about 25 to 30 percent of GDP on public purchasing. In 2008, on average public procurement in the EU was about 15 percent of GDP, with large variations among national procurement expenditures observed (OECD, 2011). The size of the public procurement market is hard to measure precisely because of different legislative definitions of what is considered public procurement and registered in national records, thus making worldwide comparisons impossible. However, due to the considerable impact of public spending on the economy, policy-makers use public procurement for economic policy purposes, striving to channel as much public spending as possible through public procurement bidding procedures, and setting the principles governing the public procurement market.

Governments in many countries responded to the latest economic crisis with increased public investment that should have generated a new business cycle. Croatia is a South-East European transition country with a small and open economy highly dependent on EU trade and political relationships and struggling with serious structural problems (World Bank, *Croatia Overview*). There is an ongoing expert debate on the role of public procurement in the times of economic downturn which have hit Croatia severely. Some arguments are in favor of public procurement that would serve as a driving force for economic activity and increased competitiveness, whilst others argue that doing business predominantly with the state has already created imbalances and had actually led to the unfavorable situation of the Croatian economy even before the crisis. Apart from the economic policy debate, public procurement participants in Croatia seem often to get around the declared principles of public procurement. Big corruption scandals in Croatia are associated with awarding public contracts to loyal companies managed by persons closely connected with the politicians in power and in conflict of interest (Ateljević and Budak, 2010). Public procurement is sensitive to corruption, as supported by the evidence in Western Balkans countries and post-communist transition countries (Grødeland and Aasland, 2011). Anecdotal evidence<sup>1</sup> on subcontractors complaining that they have difficulties getting paid for the work done in huge public contracts, that bidding documentation is designed to suit large companies and/or preferential ones, that suppliers were asked to pay an entry fee, and other irregularities deserve to be further explored. It might be the case that other countries in the region with a similar past institutional environment share the same concerns, which are not present in the developed Western economies and old EU countries.

On the other hand, in the process of Croatia's accession to the EU and upon implementation of strict public procurement legislation since 2008, the new institutional

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<sup>1</sup> Lider, 13 December 2013, pp. 26-28.



set-up was expected to increase the efficiency of the public procurement system. How do businesses as actors in the public procurement tenders evaluate the system? What are their perceived and experienced views on the various components of public procurement? One of the hypotheses is that there are differences in attitudes between direct suppliers and their subcontractors. Which principles of public procurement are fulfilled and where are the weak points? Another hypothesis is that the national system actually performs worst if compared to the “ideal” EU standards. This study provides unique insights into the functionality of the system from the point of view of companies, and the results could be instructive for both public procurement authorities and for policy-makers in the countries with a similar business environment in the Western Balkans region.

The paper is organized as follows. The next section describes the public procurement principles and the EU policy context, as well as selected up-to-date studies we use to develop our research model. The survey tool and sample characteristics are elaborated in the separate methodology section. The core part of the paper is the analysis of survey data. There are three groups of results: findings about the factors explaining the reluctance to participate in public procurement, findings on participants’ experiences of public procurement tenders and procedures, and findings on the general business sector perceptions of the public procurement system. The last section concludes with policy recommendations and provides the lines of future research.

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## 2 Research Background and Model

Literature on public procurement tackles a wide range of issues, and as Preuss (2011) duly noted, there is no single literature body that covers the entrepreneurship and public procurement nexus. Studies dealing with public procurement market, regulations and business participation in public tendering are often interdisciplinary and cross-dimensional, exploring a variety of issues in the domain of public policy, entrepreneurship, law and regulation, competitiveness and other, depending on the particular research question and objectives. Therefore, only a brief literature introduction into the context of this research will be offered. First the study provides an overview of the principles of public procurement because they reflect the policy objectives and derived regulations and procedures of the public sector. Secondly, and having in view that the study examines entry barriers to the involvement of companies in public procurement, the selected empirical studies dealing with the role and participation of firms in public procurement will be used to conceptualize the research model.

### 2.1 Public Procurement Principles and the EU Policy Context

The EU principles of public procurement date from the early 1970s and are in line with the fundamental principles of the EU common market and its four freedoms: free movement of goods, capital, services and persons. The EU principles of public

procurement are equal and non-discriminatory treatment, transparency of terms and procedures, and proportionality of requirements (for a review of EU public procurement regulation, see Bovis, 2012). Public procurement policy guidelines developed for practitioners in European countries describe these principles in more detail. For example, the Central Procurement Directorate of Northern Ireland (2011) elaborates twelve principles governing public procurement: accountability, competitive supply, consistency of procurement policy across the public sector, effectiveness, cost-efficiency, fair-dealing and commercial confidentiality, integration with other economic and social policies, integrity, informed decision-making, legality, responsiveness, and transparency. In the process of accession to the EU, Croatia had developed a new public procurement system in line with the EU standards, so the principles of competitiveness, transparency, fairness and equal treatment, integrity and corruption-free procedures are implemented in the national legislation (Box 1).

**Box 1 Principles of Public Procurement in Croatia**

Article 3

(1) In the implementation of public procurement procedures under this Act, in relation to all economic operators, contracting authorities/entities shall respect the principle of freedom of movement of goods, the principle of freedom of establishment and the principle of freedom to provide services and the principles deriving therefrom, such as the principle of competition, the principle of equal treatment, the principle of non-discrimination, the principle of mutual recognition, the principle of proportionality and the principle of transparency.

*Source: Public Procurement Act (Official Gazette, 90/2011, 83/2013, 143/2013).*

Erridge and McIlroy (2002) found that contemporary public procurement practices lay on three competing strands of public procurement: commercial, regulatory and social strand. Policy-makers and procurers are urged to prioritize and find the optimal combination of the selection criteria applied. Previous literature examined barriers for small and medium enterprises (SMEs) to participate in the public procurement tenders. The participation of SMEs in public procurement markets is far below their share in national economies. In the EU27, in 2008 SMEs on average secured 38 percent of the value of public contracts and 61 percent of the number of successful bidders (European Commission DG Enterprise and Industry, 2010), and middle-sized companies were performing better than micro-firms. The European Commission study offers the systematization of entry barriers that should be overcome by EU policy measures (Box 2). Accordingly, the European policy-makers have recognized the need to make the public procurement market easily accessible to SMEs<sup>2</sup> by reducing the administrative burden and costs related to tendering, by improving transparency and simplicity of procurement systems (for example, in terms of encouraging the usage of e-procurement).

<sup>2</sup> For the effects of SME-friendly policies in the public procurement domain, see Loader (2013).

**Box 2 Obstacles for SMEs to Access Public Procurement Markets in the EU**

- Difficulties in obtaining information
- Lack of knowledge about tender procedures
- The large size of the contracts
- Too short time span to prepare the proposal
- Cost of preparing the proposal (since many costs are fixed, SMEs face disproportionately high costs in comparison with larger enterprises)
- Too high administrative burdens
- Unclear jargon used
- High qualification levels and required certification
- Financial guarantees required
- Discrimination against foreign tenderers, in other words, favoring local and national enterprises
- Finding collaboration partners abroad

*Source: European Commission DG Enterprise and Industry (2010).*

## 2.2 Literature Review

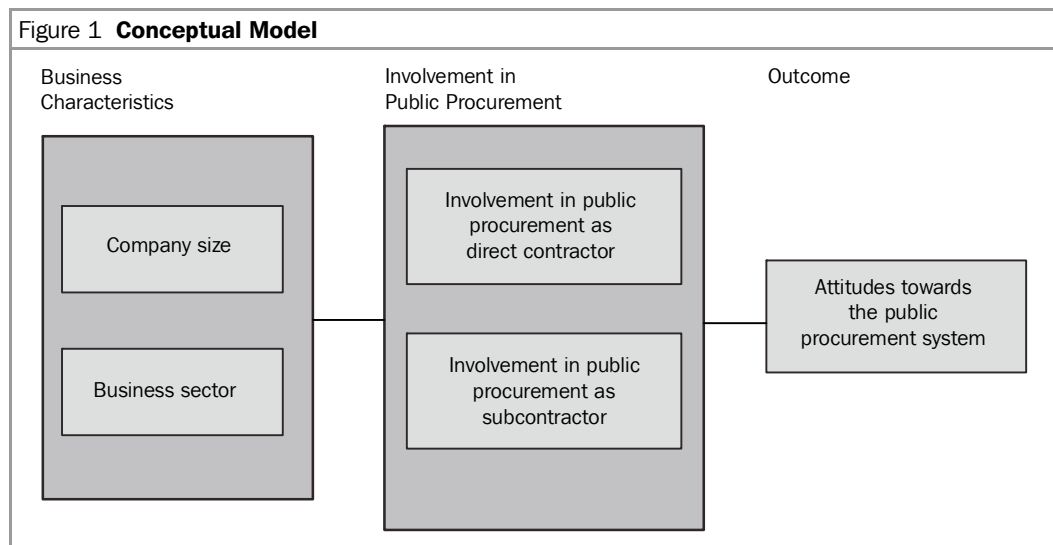
From the business sector perspective, three broad categories of obstacles for SMEs could be identified: the bidding process and regulation, the size of the contract and lack of information. The empirical research arguments are in line with above-mentioned barriers identified by policy-makers. However, academic literature on public procurement market barriers is two-fold. The major body of the research deals with the obstacles from the business sector perspective, however, it is worth mentioning the empirical investigation from the point of view of public tenderers. Preuss (2011) conducted empirical research to identify barriers for sourcing from SMEs as perceived by UK local government procurement managers. His study listed barriers in terms of restrictions arising from EU procurement directives, skill levels of devolved buyers, lack of information and resources among public tenderers, excessive bureaucracy and suppliers' perceptions that public contracts are difficult to win (Preuss, 2011).

Studies that have examined the relationship between the size of firms and public sector tendering showed that "size, measured by employee number, significantly influences small and medium-sized enterprises' (SMEs) tendering resources, behaviour and success" (Flynn, McKeivitt and Davis, 2013). Karjalainen and Kemppainen (2008) examined how availability of resources as perceived by companies influence SME involvement in the bidding process. Based on the survey results of 203 Finnish SMEs, they demonstrated that companies facing a lack of IT, legal, administrative and supply capacities are less likely to become public sector suppliers. As expected, the perceived lack of legal and administrative resources prevented SMEs from participating in public procurement tenders, and micro-firms were shown to be more vulnerable to the lack of resources. SME involvement in public procurement was higher for Finnish SMEs using electronic processing of orders and invoices. On the other hand, there is empirical evidence that SMEs perceive the public procurement market to be attractive for their business for a

range of benefits including long-term growth opportunities or raising reputation.<sup>3</sup> Based on a survey of SMEs in the UK, Loader (2005) listed perceived benefits in terms of certainty of payment, speedier payment and security over the long term. However, SMEs perceived serious obstacles to their engagement in public procurement, where major barriers included lack of awareness of opportunities, difficulty in getting on the approved supplier list, lack of knowledge of the procurement process, and lengthy and complex tendering process (Loader, 2005).

## 2.3 Model

The existing literature is focused on the role, barriers to and benefits of SMEs' involvement in public procurement. The interest in SMEs stems from the fact that about 98 percent of companies in the EU are SMEs (corresponding to the share of SMEs in the total number of Croatian companies as well<sup>4</sup>), and because of the policy goal to increase SMEs' involvement as public suppliers. In assessing business attitudes towards the public procurement system, this research builds on the empirical literature regarding the company size, and adds the supplier business sector as an underexplored but possibly significant characteristic of respondents (Flynn, McKeivitt and Davis, 2013). The model also differentiates between principal contractor and subcontractors as shown in Figure 1.



The developed model therefore fills the gap in the research body on “how SME characteristics influence ability and willingness to tender”, as suggested by Flynn, McKeivitt and Davis (2013). They proposed to extend future empirical investigation to variables other than company size, such as business sector, and to include large

<sup>3</sup> Flynn, McKeivitt and Davis (2013) offer a literature review.

<sup>4</sup> In 2012, out of 97,254 companies in Croatia, 99.6 percent were SMEs: 98.3 percent were small and 1.3 percent were medium-sized companies (CEPOR, 2013).

companies into the analysis. Here the experience and attitudes of firms towards public procurement practices in the new EU member state of Croatia are explored so this study may serve to test the previous findings in jurisdictions other than the old EU and Western-type developed countries.

Based on Morand's observation on the disproportional participation rate of prime contractors vs. subcontractors in the public procurement market (Morand, 2003), the model distinguishes between direct supplier and subcontractor. It is posited that incentives and problems associated with public procurement differ significantly between companies that negotiate in the bidding process on their own and companies that are engaged as subcontractors after the public contract has been awarded.

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### 3 Methodology

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This study uses data on Croatian companies collected in a specially designed cross-sectional survey conducted in April 2013.<sup>5</sup> In developing the core questionnaire, this research borrowed from available similar surveys (OECD, 2007; PPDA, 2010; EC, 2007; Tátrai, 2010) and customized the survey to capture the public procurement issues we consider specific for Croatia.

The target population includes active businesses of all sizes. The stratified sampling procedure is applied with company size, region and business sector as control variables. There were three categories for company size (small, medium, large), six categories for region (Zagreb region, Northwest Croatia, Central and Mountainous Croatia, Slavonia, Dalmatia, Istria and Croatian Littoral) and 15 categories for business sector according to the NACE Rev. 2 classification, where sectors omitted from the sample were sectors considered not participating in public tenders (Table 2). The total net sample size is 300 Croatian companies, where the share of SMEs is 90 percent (Table 1). The sampling procedure combined stratified sampling and quota sampling, where the stratification variable is participation/non-participation in public procurement tenders. Namely, the sampling was conducted by first randomly selecting 200 companies and then filling the rest of the sample with 100 companies that had participated in public procurement tenders. The sample includes medium and large companies above their share in the national economy because it is assumed that larger companies are more eligible to participate in the public procurement market (Table 1). The survey was administrated through telephone interviews.

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<sup>5</sup> The authors would like to thank Transparency International Croatia for supporting the survey fieldwork conducted by the Promocija Plus agency which supplied us with the original database for this research. The survey tool development and interpretation of the results remain the authors' responsibility only.

Number of employees*	Number of respondents/companies	Structure, as % of total	Structure of companies in Croatia, in % of total number of companies**
1-10	11	3.7	
11-20	14	4.7	
21-50	139	46.3	
Small	164	54.7	98.3
51-100	64	21.3	
101-250	41	13.7	
Medium	105	35.0	1.3
251-500	18	6.0	
Over 500	13	4.3	
Large	31	10.3	0.4
<b>Total sample</b>	<b>300</b>	<b>100.0</b>	

Notes: \* As on December 31, 2012. \*\* Source: CEPOR (2013).

The business profile of the companies shows the prevalent orientation towards the domestic market: for almost 80 percent of the respondents, the principal sales market is the national (Croatian) market, a further 10 percent mainly operate on the regional market of neighboring countries, and the remaining 10 percent export to the EU or the global market. Most of the companies surveyed (63 percent) are from construction, services, and wholesale and retail trade sectors (Table 2).

Business sector*	Number of respondents/companies	Structure, as % of total
C - Manufacturing	15	5.0
D - Electricity, gas, steam and air conditioning supply	13	4.3
E - Water supply; sewerage; waste management and remediation activities	13	4.3
F - Construction	68	22.7
G - Wholesale and retail trade; repair of motor vehicles and motorcycles	49	16.3
H - Transporting and storage	12	4.0
I - Accommodation and food service activities	5	1.7
J - Information and communication	12	4.0
K - Financial and insurance activities	5	1.7
M - Professional, scientific and technical activities	10	3.3
N - Administrative and support service activities	9	3.0
P - Education	2	0.7
Q - Human health and social work activities	12	4.0
R - Arts, entertainment and recreation	2	0.7
S - Other services activities	73	24.3
<b>Total sample</b>	<b>300</b>	<b>100.0</b>

Note: \* According to the NACE Rev. 2 classification.

Regional representativeness of the sample (Table 3) shows that 39 percent of the respondents are from the Zagreb (capital city) region.

Region	Number of respondents/companies	Structure, as % of total
Zagreb region	116	38.7
Northwest Croatia	27	9.0
Central and Mountainous Croatia	24	8.0
Slavonia	36	12.0
Dalmatia	53	17.7
Istria and Croatian Littoral	44	14.7
<b>Total sample</b>	<b>300</b>	<b>100.0</b>

The questionnaire consists of 37 questions.<sup>6</sup> The structure of the survey enabled us to differentiate experiences of Croatian companies that have participated in the public procurement tenders directly as principal contractor and those that have participated as subcontractors. For both groups of participants the study identified main reasons for not participating and not being awarded a contract. The business opinion on the public procurement system procedures and regulations has been assessed as well, providing insights into the business perceptions on main public procurement principles: accountability, effectiveness, value for money, integrity and achieving the EU standards. Special attention has been dedicated to the assessment of corruption risks in public procurement.

The survey data were analyzed by means of descriptive statistics techniques and chi-square test, and the results are presented in the following section.

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<sup>6</sup> The questionnaire is available from the authors upon request.

## 4 Results

Out of the total 300 companies surveyed, over the last five-year period 75 percent have competed in public procurement tenders as a direct supplier, with a significant success rate (93 percent of participants were awarded a public contract), and above one-third of the surveyed companies have participated as subcontractors.

The structure of the competitors in public tenders shows a prevalence of small companies. Almost half of the participants in public procurement tenders were companies with less than 50 employees (Table 4). The participation rate is evenly distributed among small, medium and large companies regardless of their role as direct suppliers or subcontractors. There is a statistically significant difference in structure by size between those companies that participated in public procurement as direct contractors and those that did not. There is a considerably larger share of small companies among non-participants than among participants in public procurement as direct contractors (71.6 percent vs. 49.1 percent). Both medium and large companies are more prevalent among participants in public procurement as direct contractors when compared to non-participants (38.5 percent vs. 24.3 percent for medium-sized companies; 12.4 percent vs. 4.1 percent for large companies).

The large share of SMEs in public tenders in Croatia and especially the important participation of small enterprises indicate that small companies (up to 50 employees) play an important role in the Croatian economy and that they could be considered relatively “big” for Croatian standards.

Business size	Participated as a direct supplier/contractor (%) <sup>*</sup>		Participated as a subcontractor (%) <sup>**</sup>	
	Yes (n = 226)	No (n = 74)	Yes (n = 108)	No (n = 192)
Small	49.1	71.6	48.2	58.3
Medium	38.5	24.3	38.0	33.3
Large	12.4	4.1	13.9	8.3

Notes: <sup>\*</sup> Chi-square: 12.1124, df = 2, p = 0.002344. <sup>\*\*</sup> Chi-square: 3.79945, df = 2, p = 0.149615.

With regard to the business sector of the competing companies, the largest share of participants come from the construction sector, followed by services and trade (Table 5). Companies originating from the service sector equally participated as direct suppliers and subcontractors (about 22 percent). Differences have been observed in the case of construction companies, with a prevalent share of subcontracting suppliers, while trade companies prefer to compete directly. This result is expected since construction bids are more complex and require a range of specific work that might be more effectively contracted and performed by specialized suppliers engaged as subcontractors. In the case of wholesale trade, one supplier can more easily offer the entire quantity of goods.



Business sector	Participated as a direct supplier/contractor (%)*		Participated as a subcontractor (%)**	
	Yes (n = 226)	No (n = 74)	Yes (n = 108)	No (n = 192)
C - Manufacturing	4.0	8.1	3.7	5.7
D - Electricity, gas, steam and air conditioning supply	5.3	1.4	6.5	3.1
E - Water supply; sewerage; waste management and remediation activities	4.9	2.7	1.9	5.7
F - Construction	27.9	6.8	37.0	14.6
G - Wholesale and retail trade; repair of motor vehicles and motorcycles	16.4	16.2	9.3	20.3
H - Transporting and storage	4.4	2.7	5.6	3.1
I - Accommodation and food service activities	0.4	5.4	0.9	2.1
J - Information and communication	4.4	2.7	4.6	3.7
K - Financial and insurance activities	0.9	4.1	0.0	2.6
M - Professional, scientific and technical activities	2.2	6.8	4.6	2.6
N - Administrative and support service activities	3.5	1.4	1.9	3.7
P - Education	0.0	2.7	0.0	1.0
Q - Human health and social work activities	2.7	8.1	0.9	5.7
R - Arts, entertainment and recreation	0.9	0.0	0.0	1.0
S - Other services activities	22.1	31.1	23.1	25.0

Notes: \* Chi-square: 45.0003,  $df = 14$ ,  $p = 0.000041$ . \*\* Chi-square: 37.7889,  $df = 14$ ,  $p = 0.000561$ .

There are statistically significant differences both for direct contractors and for subcontractors in structure by business sector between participants and non-participants. The most striking difference is evident for companies from the construction sector. They have a much larger share in the participant group, both for direct contractors and for subcontractors.

## 4.1 Reluctance to Participate

The main reason for not participating in public tenders as a potential direct supplier and/or subcontractor is not offering goods or services purchased by the public sector (Table 6). The remaining reasons could be grouped in three categories: no capacity, no interest and no trust (Table 6) and each group of reasons calls for a different policy response.

<b>Main reasons for not participating in public procurement tenders</b>	<b>Direct supplier (n = 74), % of all reasons listed</b>	<b>Subcontractor (n = 192), % of all reasons listed</b>
Not eligible	48.3	36.0
No interest	11.4	18.2
No trust	10.1	10.8
No capacity	13.8	5.9
Corruption	0	1.0
Other/Don't know/Don't remember/ No answer	16.4	28.1

Besides companies that are actually not eligible for public tenders, over five percent of potential subcontractors declared they compete exclusively as a direct supplier. Companies indeed prefer to get the principal contract and this fact contributed to the total of 18 percent of “no interest” reasons reported by potential subcontractors. As expected, lack of resources in terms of human and other capacities is the second major reason for not participating in tenders as a direct supplier. As for subcontractors, a perceived lack of capacities is not so important a reason for not participating in public tenders (less than 6 percent of reasons as shown in Table 6).

Companies having no interest or lacking capacity to participate in public procurement are worth considering by public procurement policy-makers; however, having no trust in the regularity or fairness of procedures is worrying. One out of ten reasons for not participating in public tenders is bad past experience or belief that public contracts are not transparently awarded. Additionally, informal payment or counter-favor asked to get the subcontract was reported by potential subcontractors. This makes corruption one of the reasons why some companies are excluded from the procurement market.

## 4.2 Evaluation of Procurement Procedures as Experienced by Participants

The level of satisfaction with selected components of procedure (Table 7) helps in identifying the potential corruption risks related to the public procurement procedures. Actually, companies that were awarded public contracts express most dissatisfaction with the price achieved and tender deadlines, which are two components not directly related to corruption risk. The majority of companies (about two-thirds) are satisfied with the transparency of procedure and consider the tender documentation clear. This business opinion stands in favor of low corruption risk in the public procurement procedure, at least for those companies that were successfully awarded a public contract.

	<b>Dissatisfied, %</b>	<b>Satisfied, %</b>
Price level achieved	36.4	34.4
Tender deadlines	10.5	71.3
Clear tender documentation	8.6	73.2
Transparency of procedure	7.7	72.7
Contract deadlines	5.7	78.0
Openness of the tender to competitors	5.3	76.1
Availability of the tender information	1.9	86.1

*Notes: \* Respondents that were awarded contract in at least one public procurement tender (n = 209). Dissatisfied = fully dissatisfied and mostly dissatisfied; satisfied = completely satisfied and mostly satisfied.*

From the point of view of companies that have not been successfully awarded, the public procurement decision was influenced by unfair and illicit behavior in terms of designing the tender for a pre-selected contractor (39 percent of responses) and by “too much bribery and corruption” (7.7 percent). The corruption-related reasons, however, make up less than half of all reasons (46 percent) and could be attributed to the frustration of companies that lost in the bidding process. The remaining one-third of companies admitted they failed due to objective reasons such as not fulfilling formal tender requirements, undergoing bankruptcy, or submitting a less competitive offer (Table 8).

<b>Reasons</b>	<b>Structure, %</b>
The tender was designed to suit known future contractor	38.5
We did not fulfil formal tender requirements	15.4
Don't know	15.4
Our offer was not competitive	7.7
We are awaiting the results of a current tender we are participating in as a direct supplier/contractor	7.7
We were not aware of the fact that we could not participate because our company is in bankruptcy	7.7
Too much bribery and corruption	7.7

The companies that were not awarded a public contract in 70 percent of cases did not submit an appeal, mainly because they did not want to further waste resources on an appealing process with an uncertain outcome (Table 9). Some respondents think there is no point in submitting an appeal because nothing would change, or they have no evidence to claim irregularities. Few respondents think that submitting an appeal would jeopardize their future business.<sup>7</sup>

<sup>7</sup> The results presented in tables 8 and 9 should be taken as an indication of potential issues only because of the small subsample (n = 13).

<b>Appeals submitted</b>	<b>Structure, %</b>
No, we didn't want to waste further resources on the appeal process	30.8
Yes, and we are satisfied with the outcome of the appeal (decision cancelled, etc.)	15.4
No, an appeal would not change anything	15.4
No, we didn't have solid evidence to submit an appeal	15.4
No, submitting an appeal would jeopardize the business prospects of our company	7.7
Don't know/Don't remember	7.7
Refuse to answer	7.7

Getting the subcontract in public procurement is attributed to a track record of successful business relations with the principal supplier (according to 49 percent of respondents). In some cases it is the result of their pre-agreed cooperation with the principal supplier in the event that they are awarded the public contract. Around 15 percent of subcontractors ensured the deal by informal channels and less than 2 percent won due to pure competitive advantage, either because of the best price or regional presence (Table 10).

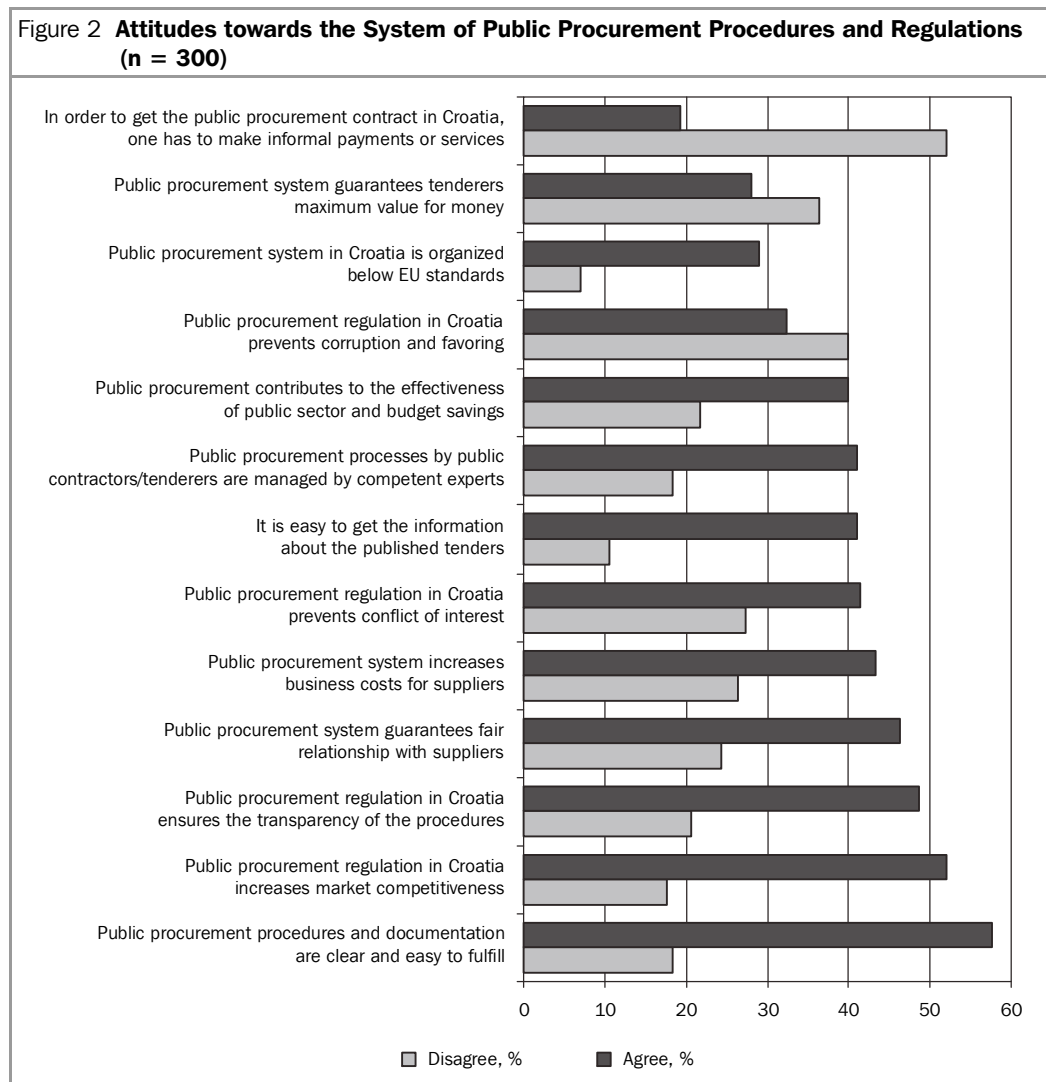
<b>How the subcontract was awarded</b>	<b>Structure, %</b>
Due to the previous successful business relationship with the contractor	49.1
We had agreed cooperation and business deals in advance if the principal contract was signed	17.6
Our company ensured the subcontracting by informal channels	14.8
Because our company is doing business in the particular region	0.9
Due to the best price we offered	0.9
Don't know/Don't remember	16.7

### 4.3 Evaluation of Procurement Procedures as Perceived by the Business Sector

Evaluation of procurement procedures by companies that have participated in public procurement and have experienced the system from the inside does not necessarily match the business sector perceptions on the public procurement system. Figure 2 presents the attitudes of companies in Croatia towards a set of public procurement procedures and regulations. All statements have been evaluated on the 5-point Likert scale (from 1 - fully disagree to 5 - fully agree).

The empirical data do not confirm the anecdotal evidence on the high prevalence of corruption in public procurement in Croatia. Companies most strongly disagree with the statement that one has to make informal payments or render services in order to get a public contract. However, the system itself does not prevent or stipulate corruption and favoring, but it prevents a conflict of interest. Transparency, availability of information,

clear and well-prepared documentation, as well as market openness are seen as the advanced features of the public procurement system. The public procurement system promotes budget savings and it is operated by competent staff. The survey pointed out the weaknesses of the system as well. It increases business costs for suppliers that might, however, be compensated by ensuring a fair relationship with the contractor. From the business point of view, one of the most important principles of public procurement – the best value for money – is not guaranteed (Figure 2).



*Note: Disagree = fully disagree and disagree; agree = fully agree and agree.*

In the context of the recent EU membership, companies were asked to compare the national public procurement system with the EU standards and around 40 percent of respondents answered “don’t know” (Table 11), while almost 30 percent think that the public procurement system is organized below the EU standards. Such a large share of “don’t know” answers might be explained by the rather large share of respondents operating primarily on the national market so they lack experience in EU public tenders.

This might change in due course with increased participation of Croatian companies in the EU market; however, it is too early to conclude whether the recent EU integration will result in this kind of benefit for the Croatian business sector.

Selected statements with <i>Don't know</i> answers given by more than 10% of respondents	Don't know, %
The public procurement system in Croatia is organized below EU standards	44.0
Public procurement contributes to the effectiveness of the public sector and budget savings	14.0
The public procurement system guarantees tenderers maximum value for money	11.3
In order to get a public procurement contract in Croatia, one has to provide informal payments or services	11.3
Public procurement processes by public contractors/tenderers are managed by competent experts	11.0

Public contractor/tenderer	Least irregularities	Most irregularities
Ministries	17.7	11.7
Pre-schools, primary and secondary schools	14.3	1.3
Non-governmental organizations and civil society organizations	7.3	0.0
Local government (counties, towns and municipalities)	6.7	29.3
Public companies	4.7	15.0
Courts and other judiciary bodies	4.3	2.0
Health sector (public hospitals, etc.)	3.7	3.7
Government of the Republic of Croatia	3.0	3.0
Cultural institutions	3.0	0.3
Public universities, research institutions	2.3	0.3
Croatian Parliament	1.7	2.0
Media	0.3	0.7
Don't know/Not sure	30.7	30.0
Refuse to answer	0.3	0.7
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

Taking into account the specifics of the national public procurement system, the survey investigated the perceived prevalence of irregularities among different types of public tenderers. Twelve types of contractors have been differentiated, most of them being obliged to publish public tenders (NGOs were included in the survey for their presumed transparency and fair policies). Table 12 indicates that local governments run public procurement with significant irregularities, according to the opinion of 29 percent of respondents. Malpractices in procurement are widespread in public companies (15 percent of respondents), followed by ministries. The case of ministries is interesting because these are the public tenderers simultaneously seen as the best performing (18 percent of respondents) and as the worst performing tenderers (12 percent). A possible

explanation is that different companies, depending on the sector in which they operate, have different experiences with particular ministries, so one ministry might be evaluated as performing well and another as performing poorly. Pre-schools, primary and secondary schools are clearly at the top of the “clean” tenderers. As 30 percent of the respondents could not evaluate public tenders, the remaining tenders on the list were not the subject of evaluation (less than 5 percent of positive or negative ratings).

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## 5 Conclusion and Future Research

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The empirical assessment of Croatian companies’ attitudes and experiences in public procurement has indicated some points worth discussion and further research. First, it seems that low participation of SMEs in the public procurement market is not as big an issue in Croatia as it is in the EU and larger national economies, where it represents a major policy concern. Moreover, the relative presence of small companies in public tenders shows there is an opportunity for small enterprises to grow bigger through public investments. As far as obstacles in the public procurement system are concerned, limited human and other resources prevent companies from participating in tenders as direct suppliers and this is in line with other empirical studies and EU procurement policy concerns. From the business point of view, one of the most important principles of public procurement – the best value for money – is not guaranteed in Croatia. This implies that policy-makers might want to consider placing greater emphasis on the so-called “economically best offer” criterion instead of the widely accepted (and easier to implement) criterion of the lowest price. The implementation of the “economically best offer” criterion, however, should not be an issue for the tenderer, although it implies more expert knowledge, because in the opinion of the business sector, the public procurement system is operated by competent staff, and this is seen as a differentiating advantage of the Croatian system if compared to the experience in other countries (Preuss, 2011).

The results confirm two hypotheses, the first one on the existing differences in attitudes between direct suppliers and their subcontractors and the second one that, at least according to the opinion of the business sector, the Croatian public procurement system is performing below the EU standards. The empirical data, however, do not confirm the anecdotal evidence on the high prevalence of corruption in public procurement in Croatia. The lack of trust, as one of the mentioned reasons for not participating in public tenders, might be related to the perceived irregularities. This and the “no interest” reason deserve future investigation by conducting case studies. The assumption that bidding documentation is pre-designed to favor certain companies was not covered by this large-scale survey and remains to be further explored as well. In Croatia it might sooner be the case of “rigging” the tenders, where the bidding requirements are adapted to suit the personal needs of the final user, that is, the manager working with the public tenderer. This kind of empirical evidence at the micro-level would shed light on the failures of the procurement system and help to improve the system and to reinforce trust.

Those public institutions that are perceived by businesses as performing irregular public procurement practices should build their reputation by promoting business ethics principles more clearly in their everyday activities.

This empirical research contributes to the limited knowledge on companies' opinions and evaluation of the public procurement system. This work empirically assesses the various attributes of the public procurement in a transition country that has undergone significant changes in the process of very recent accession to the EU. Therefore, the findings and policy implications derived would be instructive for scholars and practitioners in the Western Balkans region and other transition economies.



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