

Entrepreneurship in Focus

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Why a paradigm shift is important for the reform of public procurement

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Summary

The German government is planning to reform the public procurement law. This seems necessary because public procurement in Germany is bureaucratic and strongly regulated. In addition, small and medium-sized enterprises (SMEs) often still face high barriers when participating in public tenders, despite the valid principle of SME-friendliness in public procurement law. The reform would therefore be a good opportunity to strengthen the participation of SMEs in public procurement. To achieve SME-friendliness, a paradigm shift in policy design would be important. Only this way, a sustainable reduction in bureaucracy and regulation – the main inhibiting factors for SMEs – can be reached.

Germany has one of the largest public procurement markets in the world. Around 15% of GDP is spent here (cf. OECD 2019). The current German government agreed in their “coalition treaty” to reorganise the public procurement process (see Coalition Treaty 2021). This should be done without compromising neither the legal certainty of award decisions nor the SME-friendliness (cf. Coalition Agreement 2021, p. 33f.). In addition, the reform aims to take measures to promote “legally secure digitalisation”, encourage “quick decisions in award procedures” and support the federal states and municipalities in “simplification, digitalisation and sustainability” (cf. Coalition Agreement 2021, p. 34). It is still unclear how the objectives of the reform will be prioritised as the draft law is still pending. Only a publication by the Federal Ministry for Economic Affairs and Climate Action from last year indicates that the reform is to be carried out under two guiding principles: procurement should become (1) more efficient (faster, simpler, and more digital) and (2) more strategic (more sustainable, social, and innovative) (cf. Terbrack/Häusinger 2023).

Since public procurement in Germany is highly regulated and bureaucratic, it is understandable that its acceleration and simplification is important. In the recent past, awarding authorities increasingly complain about a decreasing number of bidders in public tenders (cf. Tyufekchieva 2020). This finding is not surprising when considering the way how procurement procedures work.

Public procurement system

When the public sector wants to procure goods, services or construction work, it must put these out to tender as part of a formal procurement procedure. These formal procedures are open to all companies – including SMEs. This allows the public sector to ensure that it receives tenders during a competitive bidding process and hence achieves a good price-performance ratio. It thus fulfils the primary objective of public procurement, i.e., the careful use of budgetary resources (cf. Naumann 2022; BMWK 2023).

Awarding authorities are responsible for the implementation of procurement procedures. There are around 30,000 awarding authorities in Germany that work for contracting authorities at the federal, state or municipal level (cf. BMI 2023). Awarding authorities have to comply with a very complex public procurement law, which consists of a large number of different regulations in Germany. The actual law that has to be applied in the individual case depends on three factors: (1) the estimated contract value (cf. § 106 GWB), (2) the object of procurement (supply of goods and services on the one hand and construction services on the other) and (3) the contracting authority (federal, state or local authority).

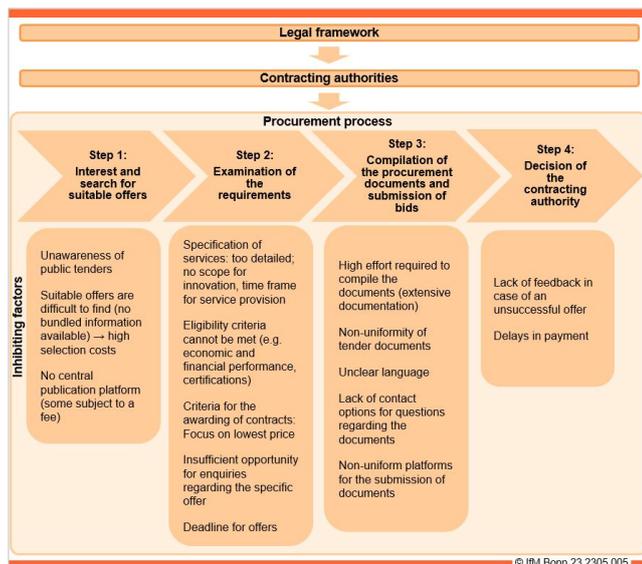
Participation of SMEs in procurement

Small and medium-sized enterprises are generally not able to bid for public contracts to the same extent as large companies because the latter have structural advantages over SMEs. They are per se larger and usually have also been operating on the market for a longer time (cf. Welter et al. 2015). As a result, they have more human and financial resources available than SMEs (cf. e.g. Schleppehorst et al. 2023; Holz et al. 2019). Thus, in contrast to SMEs, they often have specialised departments that regularly deal with bureaucratic requirements in the procurement process and their implementation and can therefore meet the requirements more quickly and efficiently (cf. Holz et al. 2019; Welter et al. 2016). In addition, they also have clear advantages over SMEs when public contracts are particularly large or public projects have to be largely pre-financed by the bidders. Their established market presence is also an advantage, e.g., when references are required. In order to compensate for these disadvantages of SMEs, the principle of SME-friendliness has been anchored in public procurement law (Section 97 (4) GWB; similarly in Section 2 (4) UVgO).

However, small SMEs are still underrepresented in public procurement (cf. BMWK 2023). Our study from

last year demonstrates that currently there are still many obstacles for SMEs in the procurement process (cf. Schneider et al. 2023). Our analysis of publicly available position papers and the literature of the past 20 years shows that SMEs experience obstacles at every stage of the procurement process. As a result, they may not participate in public tenders even though they are interested (see figure). SMEs face the greatest difficulties in the procurement process when examining the requirements (step 2) and compiling the documents (step 3). These steps are the ones where the bureaucratic obligations have a particularly strong impact. For example, in step 2, companies have to check all tender documents carefully in order to find out if they are able to fulfil all requirements. In step 3, they must compile all the necessary certificates, evidence, references, documents, declarations and self-declarations. These steps have to be carried out even for small tender sizes.

Obstacles from the SMEs' perspective



Source: Schneider et al. (2023).

Some solutions are available – but not yet implemented

There are small-scale solutions for many of the (more technical) obstacles we identified for SMEs. These solutions could basically make the procurement process more "SME-friendly" and could be implemented by the contracting authority (e.g., offering tools for market exploration) if they have sufficient (human) resources. However, this does not apply to the (more substantial) problems with bureaucratic obligations and excessive requirements. Here, more fundamental solutions are needed in the legal framework.

Paradigm shift for more SME-friendliness

If the German government wants to increase the number of bidders again, they have to focus on SMEs, which account for the majority of companies. To

achieve this goal, laws should be drafted from the perspective and with the involvement of SMEs. Holz and Icks are also calling for such a paradigm shift with regard to the overall regulatory process (2024). For example, the "Think/Act Small First" principle stipulated in European SME policy should be applied to a greater extent when designing the legal framework for public procurement. This would create the conditions to facilitate SMEs' access to public procurement systematically. A starting point could be to rethink bureaucracy and regulation in public procurement law – away from the traditional "command and control" approach towards a more risk-based "enable and motivate" approach (see Holz/Icks 2024). With a risk-based "enable and motivate" approach and a corresponding "leeway of trust", it would be possible, for example, to reduce the number of documents that have to be submitted by the firms to proof their suitability. At the same time, there should be sufficiently high sanctions for "black sheep". Although this would make award decisions riskier, it would relieve the burden on SMEs and could therefore increase their willingness to participate. This approach is also particularly suitable for achieving the reform's goal to make procurement more sustainable. Otherwise, a more sustainable procurement would be accompanied by additional obligations to provide evidence and therefore higher bureaucratic costs. This would in turn lead to an *even* greater burden on SMEs – and could therefore further reduce their willingness to participate in public tenders.

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All references of this Policy Brief can be found in IfM-Materialien Nr. 301.

Further studies:

Schneider, S.; Reiff, A.; Schlömer-Laufen, N. (2023): Mittelstandsfreundliche Gestaltung von öffentlichen Ausschreibungen, in: IfM Bonn, IfM-Materialien Nr. 301, Bonn.

Holz, M.; Icks, A. (2024): Paradigmenwechsel für spürbaren Bürokratieabbau, in: Förderkreis Gründungsforschung e.V. und IfM Bonn: Policy Brief 3/24, Bonn.

Holz, M.; Icks, A.; Nielen, S. (2023): Analyse zur Bürokratiebelastung in Deutschland – Wie kann ein spürbarer Bürokratieabbau erreicht werden?, im Auftrag der Initiative Neue Soziale Marktwirtschaft (INSM), Bonn.

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