

## *Chapter 17*

# **UK PUBLIC PROCUREMENT POLICY AND THE DELIVERY OF PUBLIC VALUE**

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### **INTRODUCTION**

This paper will first analyse UK public procurement policy against regulatory, commercial and socio-economic goals; then propose an analytical framework based on values against which to assess the delivery of public procurement policies; and finally, argue that whilst the achievement of regulatory and commercial goals and values remains important, opportunities to deliver wider socio-economic policies through public procurement should be pursued more extensively. The paper will refer in particular to a pilot project on increasing employment through public service and construction projects in Northern Ireland.

### **REGULATORY, COMMERCIAL AND SOCIO-ECONOMIC GOALS**

Erridge and McIlroy (2002) identified the above three sets of sometimes conflicting goals against which public procurement policy may be analysed. These are summarised briefly below.

#### **Regulatory Goals**

The main focus is on compliance with the European Union Public Procurement Directives (the “Directives”). These provide three mechanisms, open, restricted and negotiated, for the selection of suppliers for contracts over specified financial thresholds. The emphasis is on the transparent use of competitive procedures through advertising in the Official Journal, rather than the achievement of competitive supply. “The objective of the Union’s public procurement policy is to achieve fair and open competition...to achieve value for money for taxpayers” (European Commission, 1996, p. 3).

However, a restrictive interpretation of the Directives by the Office of Government Commerce (OGC), part of UK Treasury, resulted in a negative

view of the use of procurement for socio-economic purposes. In addition, public procurement regulations and accountability systems reinforce formal procedures and a risk avoidance culture.

### **Commercial Goals**

Pursuit of commercial goals emphasises the use of market mechanisms, such as competitive tendering, market testing and contracting out, and Private Finance Initiative, to achieve procurement goals such as reduced cost and increased quality. Public choice theorists argue that “without market discipline civil servants have no incentive to control costs and are likely to expand production beyond socially optimum levels to maximise their own rewards in terms of status, power and income” (Erridge & McIroy 2002, p. 53). Moreover, “competitive tendering will result in greater economic efficiency through reductions in costs, which will produce savings and maximise operating efficiency” (Fernandez Martin, 1996, cited in Erridge & McIroy 2002, p. 54).

The emphasis on competition resulted in resistance to the implementation of successive government reports (Treasury, 1995; Cabinet Office, 1998; Gershon, 1999; National Audit Office, 1998) proposing the adoption of perceived private sector best practice, including:

- Early involvement with customers and suppliers,
- Co-operative rather than adversarial supplier relationships, and
- Contract management (Erridge & Greer, 2000).

### **Socio-economic Goals**

Pursuit of socio-economic goals emphasises the use of public procurement to support wider government policy and includes “any purposeful action intended to improve the social welfare of the whole or part of the same population” (Fernandez Martin, 1996, p. 39). Policy areas include employment, social exclusion, protection of minorities, economic development, particularly in relation to small firms, and environmental policy.

Whilst policy delivery mechanisms include:

- Prompt payment policy to protect smaller firms and sub-contractors;
- ‘Green’ sourcing protects natural resources and the environment;
- Contract compliance to combat discrimination; e.g., gender, race, religion, and disability;

- Set asides overcome market inequalities by allowing only certain sections of the economy; e.g., small firms, to tender for contracts (Erridge & McIlroy, 2002).

### **Conflict of Goals**

Conflicts clearly arise in the pursuit of the goals identified above.

***Conflicts between Regulatory and Commercial Goals.*** An over restrictive interpretation of the Directives and public procurement rules can lead to failure to achieve competitive supply. Adoption of closer supply relationships may reduce transparency, compromise propriety and lead to a greater incidence of fraud.

***Conflicts between Regulatory and Socio-Economic Goals.*** Proponents of a restrictive interpretation of the Directives argue that allowing the use of public procurement for socio-economic purposes carries a greater risk of breach, with severe financial penalties if found guilty.

***Conflicts between Commercial and Socio-Economic Goals.*** Those who argue that solely commercial considerations should be taken into account argue that the outcome of allowing socio-economic criteria to be considered is likely to be extra or hidden costs.

As the main emphasis of this paper is on the development of a rationale for the use of public procurement to pursue socio-economic goals, the conflicts with regulatory and commercial goals will be addressed below by outlining arguments in support of the pursuit of socio-economic goals.

## **ARGUMENTS SUPPORTING THE USE OF PUBLIC PROCUREMENT FOR SOCIO-ECONOMIC PURPOSES**

### **Scope of Public Procurement**

The goals of the public sector and consequently of public procurement range more widely than a single company's profit to a concern for the wider economy and the economic, efficient and effective delivery of a wide range of public services including law and order, health, social services, education, defence, transport and the environment. The scope of most public sector organisations is therefore much wider than private companies in terms of the diversity of customers served and their requirements.

### **Values in Public Procurement**

The nature of the values pursued in the public sector is driven by ideology and is therefore contested, not only by politicians and political

parties but by groups and individual citizens. Thus the nature of policies, how and to what extent they are delivered, and at what cost is open to challenge and dispute in the public sector (Walsh, 1995; Cox, 1998).

### **Public Interest**

Self (1993) challenges the pursuit of commercial goals through the market model in the 'public interest', which he defines as "normative standards and practices which guide the political life of the society based upon widely shared moral principles or beliefs" (cited in Erridge & McIlroy, 2002, p. 58). He argues that public choice theory encourages the individual to maximise economic opportunities and personal wealth, which is difficult to reconcile with the collective notion of the public interest. He also argues that political liberty cannot be treated as the dependent variable of a strong, autonomous market system but rather what is required is a balancing of the roles of the state and the market.

Furthermore, the market system makes no distinction between "wants", which are personal desires of individuals, and "needs" which are the basic requirement for a tolerable life which all human beings have in common. Given that the market model is flawed, Self argues that there is a moral imperative for governments to ensure that the public interest is served.

### **Justice**

A further challenge to the commercial perspective is provided New (1997), who argues that at present the only voices heard in supply chain research are commercial interests, usually large powerful corporations which ignore other issues such as the imbalances of power in the corporate economy or the exploitation of poorer producers.

He contrasts efficiency and justice in relation to the questions, which these contrasting perspectives pose, as shown in Table 1. New's argument suggests that public procurement, which is not driven purely by shareholder value, should consider the broader social dimension as public bodies are in a unique position to provide such moral leadership.

### **Empirical Evidence**

The assumptions of increased cost, reduced transparency, or legality arising from the pursuit of socio-economic goals may not be correct. There has been limited experience of properly structured procurement projects directed at achieving socio-economic goals within regulatory and

**TABLE 1**  
**Efficiency and Justice Criteria**

Efficiency	Justice
<ul style="list-style-type: none"> <li>- How should firms organize their relationships with customers and suppliers in order to achieve increased efficiency?</li> <li>- How do firms' strategies in regard to vertical integration correlate to corporate performance?</li> </ul>	<ul style="list-style-type: none"> <li>- How should firms deal with the problem of child labour in the Indian textile industry?</li> <li>- How do firms evaluate the ethical and environmental performance of their suppliers?</li> </ul>

Note: Adapted from New (1997, p. 20)

commercial constraints, and limited dissemination of the outcomes of projects, which have been attempted.

From the preceding discussion, the framework of values set out in Table 2 is proposed.

**TABLE 2**  
**Framework of Public Procurement Values**

Goals	Values
Regulatory Goals	
Propriety	Conduct, behaviour and corporate governance
Transparency	Requirements and procedures are open
Commercial Goals	
Economy	Cost reduction
Efficiency	More for the same price; same for less
Socio-economic Goals (bundles of values)	
Social welfare	Equality, protection of minorities, sustainability
Public value	Trust, legitimacy, equity, ethos and accountability

### PUBLIC VALUE

One of the difficulties in reconciling the pursuit of public policy goals through procurement with the commercial imperative is that the concept of 'value' is dominated by market based language, and most of the published literature reflects private sector experience (see, for example, Ramsay, 2004). However, as argued above, the public sector has wider and more complex goals and values, which are contested through political and administrative processes. Therefore, can the concept of 'public value'

provide the basis for assessing the use of procurement for socio-economic purposes?

Jackson (2001, pp. 18-19) identified the link between public value and procurement: “The object is to enhance delivered value to the users of public services but little is known about how much value is actually delivered...Value will be added by managing relationships with suppliers, users, employees, etc.”

Kelly and Muers (2002) argued that the concept of public value provides a useful way of thinking about the goals and performance of public policy, and the means used to deliver them. The key criteria for assessing its achievement are trust, legitimacy, equity, public sector ethos and accountability. The authors identify the important areas of value as services, outcomes and trust. Achieving Public Value involves finding out what the public thinks, and requires the use of techniques, which are effective at probing public preferences. It also involves assessing the different resources available to a provider– leadership, capacity to listen to and work with citizens/local groups, openness, and the ability to innovate - together with the provider’s track record in converting these resources into dimensions of public value.

The authors reinforce the link with procurement, emphasising the importance of consultation to ensure that what is being delivered to citizens reflects public preferences, and the nature of providers who should have experience in delivering public value.

### **Critique of the Concept of Public Value**

A number of criticisms of the concept may be identified:

- It is difficult to define and measure the concepts underlying public value, namely ‘public,’ ‘value,’ and ‘values.’
- As values in the public sector are contested, the following questions need to be addressed: which values should be pursued? Who should make the selection and how? What groups and interests in society does a particular selection of values favour?
- There is a strong emphasis on participation, but it is difficult to achieve.
- It may become a tautological argument i.e. that Public Value can only be achieved through achievement of socio-economic goals.
- The concept has not been developed very far either by government or academics.

However these criticisms may be countered by the following positive arguments:

- The concept is useful as a demanding standard against which procurement policy can be assessed.
- It emphasises a focus outwards on societal outcomes rather than inwards on internal processes.
- It provides a working tool that can be developed and tested.

Figure 1 presents a framework for analysing public procurement against the values identified in Table 2, with the addition of direct/indirect impact on government goals/society on the vertical axis, and extent of consultation/impact on external stakeholders on the horizontal axis, derived from the concept of public value. This will be used to analyse delivery against government policy in the next section of the paper.

**FIGURE 1**  
**Framework for Analysis of the Value of Public Procurement**

<b>Impact on Society/ Contribution to Government Goals</b>	Direct	<i>Public Value</i>						
		<i>Social Welfare</i>						
		<i>Efficiency</i>						
		<i>Economy</i>						
		<i>Transparency</i>						
	Indirect	<i>Propriety</i>						
						<i>Internal Customers</i>	<i>Suppliers/Markets</i>	<i>External Stakeholders</i>
						Low	High	
						<b>Consultation/Participation</b>		

**POLICY DELIVERY THROUGH PUBLIC PROCUREMENT**

The extent to which regulatory, commercial, and socio-economic goals and values are currently being achieved through public procurement will be examined below.

### **Regulatory Goals**

As indicated in Table 2, pursuit of regulatory goals is directed towards ensuring that procurement activities and contracts meet the requirements of propriety and transparency, evidence on which is presented below.

- Competition remains central to EU and UK policy and procedures though there is increased provision for partnership, e.g., the use of Public Private Partnerships (PPP).
- The EU Commission's restrictive interpretation on the use of procurement for socio-economic purposes remains, although the Parliament and Court are more progressive.
- The risk avoidance culture is being addressed through the introduction of risk management frameworks emphasising that 'the purpose of control is to contain risk rather than to obviate it' (Treasury, 2000). This does not ensure that the culture of procurement has become more risk taking, or that risks are allocated appropriately between client and contractor:

"EU rules do not always encourage good procurement but local authorities can find ways to follow good practice within the rules Local authorities should not use the current rules as an excuse to avoid innovation (Byatt, 2002)."

### **Commercial Goals**

As indicated in Table 2, pursuit of commercial goals is directed towards ensuring that procurement activities and contracts meet the requirements of economy and efficiency, evidence on which is presented below.

The results of a recent study by the UK National Audit Office on government departments' capability to procure cost effectively (NAO, 2004) suggest that whilst progress is being made on achieving commercial benefits from public procurement, there is scope for further improvement.

- Savings of £1.6 billion achieved exceeded the target of £1 billion.
- Gateway Reviews under which progress on major projects is reviewed at a number of 'gates' or stages were used by 76% of departments surveyed, but their use could be extended to projects other than IT and Construction; e.g., refurbishment of buildings.
- Procurement decisions need to be closely linked to the delivery of departments' core services and functions... more progress is needed to ensure that sufficient consideration is given at Board level to the

procurement implications of key decisions affecting the delivery of public services.

- There is a lack of commercial awareness and market knowledge: only half of departments maintain a database of suppliers and only a quarter assess the extent of suppliers' dependency on them.
- The rate of progress on professional skills remains relatively slow, with less than a quarter of staff being fully qualified to full professional membership of the Chartered Institute of Purchasing and Supply (MCIPS).
- There is a lack of measurement information: departments require reliable information on the whole life costs of procurement covering all costs associated with the acquisition of goods and services and doing business with suppliers, the costs of maintenance and operation over the whole life of the asset or service, ending with the conclusion of a service contract or ultimate disposal of an asset.

Overall there is evidence of progress on some commercial aspects, such as savings and Gateway Reviews, but limited progress on market knowledge, skills and measurement cast doubt on the extent to which Commercial goals are being achieved across the full range of departments and agencies.

Whilst there is evidence of recognition of the importance of procurement at Board level, further progress is necessary if procurement is to contribute to design and delivery of wider departmental policies, including those related to Socio-economic goals.

### **Socio-economic Goals**

As indicated in Table 2, pursuit of socio-economic goals is directed towards ensuring that procurement activities and contracts meet the requirements of social welfare and public value, evidence on which is presented below.

***Sustainability and the Environment.*** Examples of procurement assisting the achievement of government goals on sustainability and the environment are provided in two contracts let by the then Department of the Environment, Transport and the Regions (DETR) (Erridge & McIlroy, 2002).

1. The Home Energy Efficiency Scheme (HEES) was designed to combat "fuel poverty" by distributing grants for the upgrading of heating systems and home improvement to eligible persons. The contract is let by DETR to Scheme Managers (SM) who subcontract to local

contractors who carry out the work for the end user. Other parties involved include local statutory and voluntary agencies (Department of Social Services, Local Councils, Help the Aged etc).

2. Environment Action Plans (EAPs) are concerned with the environment and its impact on local communities. DETR awarded the contract to one contractor who is responsible for administering the scheme and subcontracts the assessment of potential projects to individuals with expertise in the area. The end user is the community/school that is awarded the grant and the community in general.

These contracts illustrate the balanced achievement of Commercial (cost), Regulatory (compliance with EU Directives and fairness) and Socio-economic goals (delivering social benefits to communities/individuals).

**Best Value.** This is the policy introduced by the Labour government to replace the previous government's Compulsory Competitive Tendering (CCT) policy. Whilst the Best Value review process retains an emphasis on competition where appropriate, there is also a requirement to take the views of service users and suppliers into account, and to consult local taxpayers, service users and business community. Thus there is a mix of commercial, regulatory and socio-economic priorities, with public value in particular being emphasised in the requirement to consult widely. This mix of goals was highlighted by Geddis and Martin (2000, p. 382): "there is...no simple choice to be made between cost reduction and service improvement. Best Value authorities are required to achieve both."

Prior to the full introduction of Best Value, pilot projects were carried out over a three-year period. Geddes and Martin (2000) distinguished 4 types of Best Value Pilot Projects: Service, Market, Corporate and Community. In relation to the latter, projects focused on the needs and priorities of communities, either specific estates/ neighbourhoods, or client groups: "Many of these initiatives have emphasised the role of 'consultation'... have adopted deliberative approaches designed to engage a range of different types of citizens... aim has been to empower communities to exert greater influence over the design and delivery of services" (Geddes & Martin, 2000, p. 385).

Community based approaches demonstrate the potential for procurement to participate in the design and delivery of socio-economic projects through Best Value, involving extensive consultation, thereby contributing to Public Value.

**Ethnic Minority Involvement in Public Procurement.** According to the Performance and Innovation Unit (2002, p. 167), "though public

procurement has been used as a major lever overseas to improve the position of ethnic minority businesses (EMBs), emphasis on this policy lever [in the UK] is less well developed.”

However, the Race Relations Amendment Act (2002) “imposes a duty on public sector agencies to ensure that their services are available to all communities... [and] to engage more actively with EMBs in a position to supply” (Ram & Smallbone, 2003, p. 188).

The authors examined a range of types of supplier diversity initiatives, including large purchaser driven initiatives, e.g., London Development Agency, British Telecom, and intermediary initiatives, which provide business-to-business brokerage to facilitate access of EMBs to contracts with large purchasers. Targeted measures included:

- Condition that firms show a commitment to diversity with their suppliers;
- Simplified procurement regulations;
- Use of smaller contracts below EU thresholds;
- Advertising in the local press (in ethnic minority areas);
- Circulating information through ethnic media;
- Seminars, meet-the-buyer, and other local business events;
- Assistance to facilitate the development of consortia and invitations to tender;
- Local training and capacity building; and
- Development of brokerage agencies.

The authors argued that a strategy of building the capacity of EMBs, on a ‘fit-to-supply’ basis was a more attractive option than one of positive discrimination.

### **Summary on Delivery**

Whilst there is evidence of progress on some commercial aspects, such as savings and Gateway Reviews, and recognition of the importance of procurement at Board level, further progress is necessary if procurement is to contribute to the design and delivery of wider departmental policies, including those related to Socio-economic goals. However, procurement is contributing to wider policy goals, including the environment, poverty reduction, social inclusion and community development. There is evidence

that socio-economic policies can be delivered within the constraints of the EU Directives, take into account value for money concerns, and balance commercial, regulatory, and socio-economic goals.

### **NORTHERN IRELAND PUBLIC PROCUREMENT POLICY**

In this section of the paper an analysis of the development of a procurement policy, which incorporates the pursuit of socio-economic goals, will be provided. This arose from the particular experience of community conflict and economic disadvantage in Northern Ireland, in particular:

- Pressure from local politicians and interests, especially in respect of winning business locally, and meeting regional socio-economic needs.
- The requirement under Section 75 of the Northern Ireland Act 1998 to ‘pay due regard to the need to promote equality of opportunity.’
- The need to review NI procurement policy following devolution as no policy existed for the devolved administration, resulting in the new policy being approved by the Executive in 2002.

The implementation team was specifically tasked to “identify the scope to use public procurement in Northern Ireland to further local social and economic objectives within the context of current EC and international law relating to procurement” (“NI Public Procurement Policy,” 2001, p. 1).

The criterion of ‘best value for money’ was adopted, defined as “the optimum combination of whole life cost and quality (or fitness for purpose) to meet the customer’s requirements” (“NI Public Procurement Policy,” 2001, p. 15).

This definition allowed for the inclusion, as appropriate, of social, economic and environmental goals within the procurement process, and measures were introduced in the following areas:

- Equality and discrimination;
- Disabled employment schemes and procurement,
- Unemployment;
- Environmental purchasing; and
- Small and medium-sized enterprises (SMEs).

Of these, the most controversial is the Unemployment Pilot Project (UPP). Seven devolved government departments contributed 20 contracts ranging in value from £700,000 to £8.5 million. Contracts cover services

such as cleaning, catering, and security; and construction such as road improvements, and Kilkeel harbour works. Contractors are required to include an Employment Plan for utilising the unemployed in work on the contract with their bid, failure to do so resulting in rejection of the bid. Under current EU law, the Employment Plan cannot be used as a primary selection criterion, but is only considered in the case of a tie between two or more bids evaluated on price alone or cost/quality criteria, in which case the Employment Plan acts as a tie-breaker. On award of the contract, the successful contractor and sub-contractors are required to implement their Employment Plan.

Evidence from the Projects initiated to date shows that the UPP is not having a detrimental effect on the contracting process - in fact, the process has worked very smoothly. There is no evidence of significantly increased costs or workload for clients or contractors. The UPP process has quickly become an embedded part of the culture of contracting with government amongst construction contractors, those most involved to date. Whilst it was never likely that large numbers of unemployed people would be taken on by winning contractors, already three people have been employed with a fourth to be appointed soon. The Pilot Project is compliant with EU Directives and with the NI Public Procurement Policy's Best Value for Money criterion.

### **APPLICATION OF ANALYTICAL FRAMEWORK**

Figure 2 presents the results of applying the analytical framework to the regulatory, commercial, and socio-economic policies and processes. These three policies are located on the vertical axis against the values to which they relate, and on the horizontal axis according to the extent to which they involve consultation/participation and impact on external stakeholders. The policies and processes examined are discussed briefly below.

#### **Risk Management**

This relates mainly to propriety and has an indirect impact on government goals and society. Risk management frameworks are developed in conjunction with internal customers and there is little consultation outside the organisation. However, risk management has an important role in protecting against fraud and impropriety, which in turn supports more innovative approaches to procurement, including the pursuit of socio-economic goals.

**FIGURE 2**  
**Application of the Analytical Framework**

<b>Impact on Society/ Contribution to Government Goals</b>	Direct	<i>Public Value</i>		EAPs UPP	
		<i>Social Welfare</i>		PPP	EMBs BV-Community HEES
		<i>Efficiency</i>		Gateway Reviews	
		<i>Economy</i>	VfM Savings		
		<i>Transparency</i>		EU Directives	
	Indirect	<i>Propriety</i>	Risk Management		
			<i>Internal Customers</i>	<i>Suppliers/ Markets</i>	<i>External Stakeholders</i>
			Low	High	
		<b>Consultation/Participation</b>			

### **EU Public Procurement Directives**

These provide the legal basis for procurement throughout the European Union, and relate mainly to transparency. As with risk management, they have an indirect impact on government goals and society, but their development is influenced by wide ranging consultation with national governments and representatives of employees and employers, trade organisations and other ‘social partners’. Whilst competition remains the primary mechanism for supplier selection, the recent review and proposed amendments to the Directives featured a prolonged debate between the European Parliament and Commission on proposals to enhance the extent to which public procurement may be used to pursue socio-economic goals.

### **Value for Money (VfM) Savings**

The focus here is on economy and efficiency, producing savings from procurement, which may have an impact on society, and government goals by freeing resources to provide for more or better quality services to the public. However, purely price based purchasing may have a negative impact if it results in poor quality goods or reduction in services. There is however rarely consultation on efficiency savings even within government, as savings targets are generally set by Treasury as part of the Comprehensive

Spending Review. In relation to procurement, recent savings targets have been set by Peter Gershon, Director of the Office of Government Commerce, and there has been consultation only on their implementation.

### **Gateway Reviews**

Although these relate mainly to efficiency and have a similar potential as VfM savings to enhance service provision, the projects to which they relate generally will have been subject to formal planning procedures, requiring consultation with affected organisations and individuals. There is also the potential for greater social welfare benefits to result from projects subject to review, particularly those relating to the construction and equipping of schools, hospitals, and transport infrastructures.

### **Public Private Partnership (PPP)**

PPPs provide a mechanism for involving private sector providers in the financing, production and delivery of facilities and services of direct benefit to society, and contribute to government goals without the full cost being provided from public expenditure. As with Gateway Reviews, formal consultation is necessary where a planning application is required, but in addition where there is a local partnership between a community, close working relationships will be developed between government and private providers, thus contributing to social welfare.

### **Home Energy Efficiency Scheme, Best Value Community Projects, Unemployment Pilot Project, Ethnic Minority-owned Businesses, Environmental Action Plans**

All of these contribute to Public Value by impacting directly on society and contributing to the achievement of government goals. It is also important to note that all are fully compliant with regulatory requirements, and there is no evidence that they transgress Value for Money commitments. Providers are involved to a greater or lesser extent, as are a range of external stakeholders. There is also consultation with service providers and recipients in setting up projects or contracts, and in some cases, in their delivery, management, and evaluation.

## **CONCLUSIONS**

This paper has argued that there has been an overemphasis in UK public procurement on regulatory and commercial goals to the detriment of its use

for socio-economic purposes. A review of these aspects of procurement has found that:

- A restrictive interpretation of regulation constrains effective use of commercial best practice as well as pursuit of socio-economic policy;
- The extent of development of infrastructures and commercial aspects of procurement varies across government departments and sectors; and
- There is considerable evidence of the potential and actual use of innovative public procurement to deliver socio-economic policy within the existing competitive and regulatory environment.

The concept of 'Public Value' is proposed as a guide to public preferences in relation to services and projects delivered by public procurement, and an Analytical Framework has been proposed for development and testing as a means of assessing procurement initiatives against a framework of public procurement values.

#### NOTES

1. The Conservative Government originally introduced the Private Finance Initiative (PFI) in 1991 in order to attract funding from private companies and financial institutions to bid jointly to design, build and operate public sector facilities mainly in the health, education and transport sectors. The policy has been revised and extended by the current Labour government.

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