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COULD PUBLIC PROCUREMENT BECOME AN INCENTIVE FOR DEVELOPING THE NON-PROFIT SECTOR IN RUSSIA?

Non-profit organizations deliver a wide range of meaningful resources to communities in such diverse areas as education, arts, social services, etc. However, compared to the private sector, their funding potential is much more limited. The increasing social and economic impact of the non-profit sector is a reason why there is a need to persistently enhance these opportunities. State contracts have the potential to be regarded as one of the most essential sources of funding for non-profit organizations in the social sphere. In Russia, recently passed laws ensure substantial benefits for 'socially oriented' non-profit organizations that participate in public procurement. Nevertheless, despite the existence of norms allowing socially oriented NPOs to be granted preference in tenders, the presence of the non-profit sector in the Russian public procurement market is still insignificant. This study seeks to analyze the peculiarities of Russian public procurement legislation. The main question of the study is why state procurement failed to become a driver for the development of the non-profit sector in Russia? To answer this question, firstly we consider the functioning mechanisms of socially oriented

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NPOs in the public procurement market. Then, we analyse the results of expert interviews, which let us identify the following barriers limiting the participation of NPOs in public procurement: economic, financial, social, and organizational. Finally, we draw the conclusion that, for the majority of non-profit organizations, state procurements are an optional source of funding in view of the barriers identified above. This study is relevant for government and public authorities as it can serve as a starting point for improving the mechanisms of attracting the non-profit sector to the sphere of public procurement.

Keywords: socially oriented non-profit organizations, public procurement, social service, non-profit sector, procurement procedures

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Introduction

The non-profit sector plays a crucial role in a country's social and economic life by providing stability in society and acting as a source of social innovation. Non-profit organizations perform a number of critical functions: they help deliver vital human services, such as health, education, counselling, and aid to the poor, often in partnership with the state and the market (Salamon 2010: 168). At present, this role is increasingly becoming more relevant: non-profit organizations are positioning themselves as subjects of social policy, taking an active part in its development and implementation. As has been noted, 'the process of social policy transformation is starting to attract new actors, including social and non-profit organizations' (Sidorina 2010: 125). Considering the growth and value of the third sector along with the benefits obtained by the government from its cooperation with non-profit organizations, legislation in Russia allows for a wide range of measures aimed at supporting the non-profit sector: subsidies, grants, tax concessions, as well as information support. In 2010, Federal Law introduced the definition of socially oriented non-profit organizations:

Socially oriented non-profit organizations (SO NPOs) are non-profits set up in the forms stipulated by the present Law (except state-owned corporations, state companies, non-governmental organizations acting as political parties) and carrying out activities aimed at solving social issues, developing civil society in the Russian Federation... (Federal Law 2010: Art. 1).

These activities include social services and social welfare, charity, training and education, and the solution of ecological problems. Therefore, a 'significant subsector' which benefits from additional supportive measures has been singled out (Benevolenskiy, Shmulevich 2013: 152). One such measure is providing socially oriented non-profit organizations with advantages during their participation in public procurement.

It is worth noting that, at the time when the Law came into force, current legislation did not contain mechanisms to provide advantages to SO NPOs when they were tendering for a government contract. Besides, there were objective reasons restricting NPOs' access to the government contract. As noted in the NRU HSE report published in 2012, non-profit organizations 'are often unable to comply with some regulatory frameworks' (NRU HSE 2012: 20). Consequently, it was wrong to expect that this form of support could be productive.

In 2014, A Federal Law (2013a) took force and specified mechanisms for giving advantages to SO NPOs in public procurement. In accordance with this law, ordering customers are obliged to make no less than fifteen per cent of the annual volume of purchases exceptionally from small business entities and SO NPOs. Legislation does not define the list of goods, works and services for which the procurement procedure has to establish requirements of attracting SO NPOs. At the same time, it is evident that the non-profit sector possesses substantial experience, staff and best practice in the field of social services; in the future exactly this niche in the public procurement market is sure to be occupied by SO NPOs.

The task of attracting SO NPOs to provide social services was set by the President of the Russian Federation (President 2015). His decree implied that up to 10% of funds allocated by the budget for the provision of social services to citizens should be directed to NPOs. The benefits of such an approach are emphasized by Russian and foreign researchers. For example, Vladimir Benevolenskiy and Ekaterina Shmulevich argue that the partnership between the state and SO NPOs in the social sector makes it possible to 'unite the country's resources with non-budgetary sources of social policy funding, which are available for non-profit organizations, for example, such as charitable donations, voluntary work' (Benevolenskiy, Shmulevich 2013: 161). Raymond Struyk points out that 'beyond improving efficiency in service delivery, contracting out can increase accountability in the use of public resources' (Struyk 2002: 431). While John Chin emphasizes the contributions of service-providing non-profits 'to policy advocacy, drawn from their daily interactions with clients and the service bureaucracy, as well as their use of insider channels to promote apparently small and detailed but at the same time consequential changes to service bureaucracies' (Chin 2018: 43). At the same time NPOs need support from the state since 'the value-based self-sustaining mechanism is insufficient' (Knutsen 2013: 994).

In spite of the benefits connected with involvement of SO NPOs in the provision of social services to the public, this process is slow. Sergey Efremov revealed that 'regions strive to change the status quo, but underestimate the readiness of the market, non-government suppliers as well as their own abilities to regulate non-government suppliers' (Efremov 2013: 115). This view is supported by Kirill Chagin and Raymond Struyk (2004). Analysing the experience of Russian cities in attracting non-profit organizations to provide social services, they assert that the mechanism of monitoring the quality of services provided by NPOs is extremely weak, and even public authority representatives have doubts

about whether this monitoring can be carried out in a satisfactory manner (Struyk: 19). The inertia of officials and complicated reforms lead to the fact that the transition of functions from budgetary institutions to independent suppliers is rather slow. At the same time, as noted by Svetlana Suslova, the list of social services demanded by the authorities 'is a crucial factor for NPOs participation' (Suslova 2014: 72). It is necessary to mention, however, that public procurement is not the only way of attracting the non-profit sector to the provision of social services. In accordance with another Federal Law (2013b), funding for the provision of social services by non-governmental organizations, individual entrepreneurs engaged in social services and socially oriented non-commercial organizations is carried out in the following ways: by providing subsidies; by procurement under the state (municipal) order; with funds from social service receivers in the provision of social services for a fee or partial payment.

Regions independently choose the most appropriate scheme to tackle the given problem. The funding of social services through the state procurement is widely used in the Bashkiria and Perm regions. In Bashkiria, for example, 22% of the funds of the regional state program 'Social protection' were distributed through the state procurement (Vedomosti 2017). This was preceded by the transformation of the state social services budgetary institutions into non-profit organizations as well as by the transfer of a significant number of social services (for example, home-based services for elderly citizens) to the non-state sector. In the republican register of social service providers, 75.9% were non-governmental organizations (Zabolotnaya, Larionov 2017: 77). In the Perm territory all non-stationary services in the social service sector are supplied by the private sector. Both catering services and maintenance services in hospitals are outsourced; cleaning and security services for social service institutions are also procured from the private sector (Vedomosti 2017). In general, 44% of total expenditure on social services in Perm in 2015 was distributed through public procurement (Ministry of Economic Development of the Russian Federation 2016).

Despite existing expertise in purchasing social services through the public procurement system, to date, involvement of the non-profit sector in public procurement is insignificant. In most regions, social services are still provided by budgetary organizations, which are financed from budgetary sources. According to a study conducted by the organization 'All-Russian People's Front', among 52 SO NPOs from 21 regions of Russia in 2016, only 10 per cent of non-profit organizations participated in the auction (ONF 2016). In view of all that has been mentioned so far, there seems to be a need for systematizing mechanisms of involving SO NPOs in the public procurement sphere. In addition, it is necessary to identify factors limiting SO NPOs' participation in public procurement.

Problems associated with the performance of SO NPOs in the Russian public procurement market under current conditions have been repeatedly emphasized by Russian researchers. Olga Belokrylova and Margarita Vahtina

point to SO NPOs' 'lack of due professionalism, shortage of qualified specialists, instability of funding and poor material resources' (Belokrylova, Vahtina 2017: 82). A problem analysis, as viewed by service suppliers, was carried out by Irina Mersiyanova and Vladimir Benevolenskiy. First and foremost, they bring into focus the lack of a personal financial and economic base. The researchers underline that 'only the biggest organizations possessing substantial accumulated capitals have an absolutely sufficient socio-economic activity base' (Mersiyanova, Benevolenskiy 2017: 85). Nevertheless, in spite of the increasing academic interest in questions related to SO NPOs' involvement in the public procurement market, the current study has found no reliable evidence that could closely investigate and describe barriers to SO NPOs' participation. Consequently, there is a need to identify and systematize barriers hindering successful operation of SO NPOs in Russian public procurement market.

An analysis of the mechanisms behind SO NPOs' functioning in the Russian public procurement market

The procedure for giving preferential treatment to SO NPOs in public procurement is regulated by the above-mentioned Federal Law 44-FZ. The law establishes that public procurement authorities should make no less than fifteen per cent of the annual volume of procurement from small business entities and SO NPOs, with the contract price not exceeding twenty million roubles. It should be noted, however, that Law 44-FZ does apply to SO NPOs whose founders are the Russian Federation, constituent entities of the Russian Federation or municipalities.

On 1 January 2019 there was virtually a one-time transition to electronic procedures in the Russian system of public procurement. Prior to that, electronic procedures used to be represented only by electronic auctions. Thus, since 2019 the preferential treatment enjoyed by SO NPOs has been subject to the following competitive proceedings: (1) open tenders in electronic form; (2) tenders with limited participation in electronic form; (3) two-stage tenders in electronic form; (4) electronic auctions; (5) requests for quotation in electronic form; (6) requests for proposals in electronic form; (7) closed tenders in electronic form; (8) closed tenders with limited participation in electronic form; (9) closed two-stage tenders in electronic form; (10) closed auctions in electronic form. In the event that a customer has signed a contract with an SO NPO involved in non-competitive procurement, for instance, small volume procurement, this procurement in accordance with the law is not considered as 'provision of support'. At the end of the year, all customers make a publicly available report on the involvement of small and medium size enterprises (SME) and SO NPOs on the website of the unified information system. It should be pointed out that state officials that failed to fulfil the obligation to purchase from small businesses and SO NPOs bear an administrative liability – a fine in the amount of 50,000 roubles.

Table 1

Ways of granting preferences to SMEs and SO NPOs as specified by Law 44-FZ

<i>Way</i>	<i>Way of granting preferences</i>	
	Procurement for SMEs and SO NPOs	Procurement for all market players with an obligatory condition of attracting subcontractors from SMEs and SO NPOs
Informing market participants at the planning stage	Published procurement schedule contains information on competitive procedures for SME and SO NPOs which the customer plans to carry out during the year.	Absent.
Requirements to procurement parties in procurement	Only SMEs and SO NPOs are allowed.	Any legal bodies and private individuals are allowed, including individual entrepreneurs.
Maximum contract price	Up to 20 mln. rubles.	Without restrictions.
Content of the procurement notice and documentation	It is indicated in the notice that only SMEs or SO NPOs can act as procurement parties.	Requirement to the supplier (contractor, performer) that is not a SME or a SO NPO about engaging subcontractors, co-contractors from SMEs or SO NPOs in contract execution; The volume of business involving SMEs or SO NPOs is indicated as a percentage of the contract price; Information about suppliers' liability (subcontractors, performers) for a failure to comply with the condition of contracting out.
Additional requirements to procurement participants	Declaration about the procurement party's belonging to a SME or a SO NPO.	Not required.
Payment terms under the contract	No more than 15 working days after signing the results acceptance certificate.	No more than 30 working days after signing the results acceptance certificate.

There are a number of features distinguishing procurement from small businesses and SO NPOs. When conducting such purchases, the customer has to indicate in the procurement notice that only such procurement parties as small businesses and SO NPOs are allowed to participate in the process. Procurement parties, in their turn, must declare that they belong to these categories when submitting their applications. It is worth noting that state customers should plan procurement from small businesses and SO NPOs when planning their annual procurement schedule and publish this document in the unified information system. Contracts negotiated with small businesses and SO NPOs contain a mandatory condition about payment under the contract within no more than fifteen working days from the date the acceptance document was signed by the customer.

Legislation also provides for the opportunity to extend preferences by setting in the procurement notice a requirement to the winner to involve subcontractors from small businesses or SO NPOs into contract execution. The winning organization might not fall into this category. The volume to be carried out on the subcontracting basis is determined as a fixed percentage of the contract price. In the event that the winner of the competitive procedure fulfils all contract conditions but at the same time fails to meet obligations about attracting small businesses and SO NPOs, a penalty is enforced. Given the difficulties of preparing such contracts when attracting small businesses and SO NPOs on a subcontract basis, customers are obliged to use a standard contract (secured in legislation form of contract).

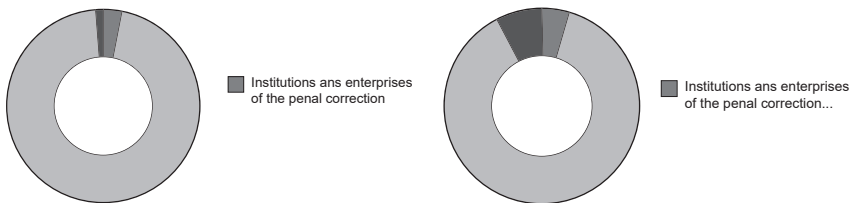


Fig. 1. Distribution of contracts concluded from 01.07.2016 to 30.06.2017 by types of organizations, in quantitative and monetary terms (National Rating of Procurement Transparency 2017).

On the whole, giving preferential treatment through the subcontract mechanism seems to be more complicated in terms of its organization and, therefore, is used mostly by major customers. Table 1 illustrates the ways of granting preferential treatment to SMEs and socially oriented organizations.

Measures envisaged by Law 44-FZ to support SO NPOs certainly give some competitive advantages to non-profit organizations in the public procurement market. However, the volume of purchases made by SO NPOs in Russia through the public procurement system is insignificant.

Methodology

To achieve our research goals, we carried out a qualitative analysis of the situation in the public procurement market as well as of features related to the work of non-profit organizations in this market. In order to identify key barriers to receiving public orders, the authors used expert interviews. The invited experts possess significant experience and knowledge of the legislation. To gather the opinions of experts regarding existing barriers for SO NPOs, a topic-guide was used in the research.

For this study, interviews were conducted with eighteen experts from Nizhny Novgorod and Saint Petersburg, all of whom were SO NPO employees at the time. The research engaged experts with longstanding professional experience of working in SO NPOs. The interviews were carried out during the second half of 2018. Each interview lasted from thirty to forty minutes. The experts were asked the following open-ended questions: What kinds of state and municipal procurement are of greater interest for SO NPOs? What features distinguish SO NPOs' activities in the public procurement market? What barriers prevent SO NPOs from participating in state and municipal procurement? How do you think it is possible to increase the activity of SO NPOs in the market of state and municipal procurement? The authors deliberately formulated open-end questions to let the experts share their own opinions.

Results

The data collected from the interviews and the analysis of the current research literature allowed the authors to identify four kinds of barriers limiting the participation of SO NPOs in public procurement: economic, financial, social, and organizational.

Economic barriers

According to Russian legislation, preferential treatment is granted to small business subjects and SO NPOs in general but not separately for each category. When holding tenders the customer indicates in the procurement notice 'Preferential treatment to small business enterprises and socially oriented non-profit organizations.' Thus, upon entering the public procurement market non-profit organizations are forced to compete with small businesses 'in their field', that is in the sphere of commerce. Given the fact that non-profit organizations do not have stable funding and are non-competitive in many respects compared

to profit making organizations, participation only in tenders with small businesses limits their chances.

In addition, today we are witnessing the emergence of a social entrepreneur class that will undoubtedly occupy a niche in the public procurement market. It is necessary to mention that in other countries it is social enterprises, not SO NPOs, that have the edge in the state procurement market (Munoz 2009: 69).

Undoubtedly, there are market segments where SO NPOs can under certain conditions be competitive in respect to other players. As noted by Suslova, non-profit organizations are most active when involved in public procurement procedures focusing on their core activities (Suslova 2014: 83). Such segments include social services, further education, physical education, and sport.

Financial barriers

Contracts concluded in the public procurement market do not normally involve advance payment. Indeed, an organization that has signed a government contract is supposed to have financial resources or access to loan-based funding in order to meet its obligations under the contract. This is a fundamental difference distinguishing public procurement from funding through grants and subsidies. Considering the ban on the transfer of funds between projects, financial constraints tend to make public procurement virtually impossible for small and medium organizations.

The only financial advantage SO NPOs have over other market players is the relatively low level of overheads. Also, volunteer participation is likely to cut expenses to a certain extent. Nevertheless, these features do not solve the funding problem for SO NPOs. As one interviewee commented: *'Quite often an organization does not have funds in the operating account even for bid securities, not to mention the funds for the execution of the contract.'*

In order to be involved in meaningful competition in the public procurement market SO NPOs need to be 'more business-like' in that they should have a sustainable financial performance and stable staff. Consequently, there is a risk of third-sector organizations becoming commercialized. Putting an organization on a commercial track might result in the organization retreating from the company mission and losing staff who are motivated by this mission (Pagava et al. 2013: 20). This is precisely why, in other countries, where outsourcing of state-guaranteed social services is widespread, mainly social entrepreneurs work in this sphere. Unlike NPOs, the subject of social entrepreneurship is distinguished by 'the presence of a sustainable commercial effect, self-sufficiency, based primarily on the sale of goods or services, but not on fundraising or resources of external charity' (Social Information Agency 2012: 48).

Social barriers

Since the social sector in Russia has traditionally belonged to the sphere of state responsibility, at present we can witness the unwillingness of the

population to use the services of non-governmental organizations. Society is still reluctant to trust non-governmental organizations. The results of an all-Russian representative survey demonstrated that only 38% of Russians trust NPOs of at least one kind (Mersiyanova, Benevolenskiy 2016: 16). Scholars tend to explain the lack of trust in NPOs by the fact that the social orientation of activities is a relatively new phenomenon for the Russian non-profit sector. As one expert put it, Russians, especially in regions, are poorly informed about the activities of NPOs; besides, some of them associate NPOs exclusively with political activity, which is not an accurate representation of NPO activity in Russia. It is not surprising that the authorities are trying to complete tasks in the sphere of social policy with the help of state-financed organizations.

Other possible reasons may be connected with the non-transparency of some organizations and cases of poor organizational management. However, at present according to experts there is reason to expect an increase in confidence in third-sector organizations and the rejection of the use of obsolete and ineffective approaches in the field of social policy.

Organizational barriers

The lack of stable source of financing is made worse by the small size of non-profit organizations. As noted in the Report on the State of Civil Society in the Russian Federation, made by the Civic Chamber of the Russian Federation, most of the sector in Russia is made up of small NPOs with up to five employees (The Civic Chamber of the Russian Federation 2017). Evidently, taking into account such severe staffing constraints non-profit organizations have a modest chance of winning in competitive procedures in the public procurement market. The complexity of the public procurement legislation also contributes to the situation. As noted above, a transition to electronic procedures has taken place in the Russian public procurement system since 2019. This is a step forward, as reduced interaction between customer representatives and participants contributes to increased openness and competition, simplifying the detection of violations and corruption (OECD 2016). On the other hand, work on electronic trading platforms requires new competencies from SO NPOs involved in the procurement.

It should also be noted that the transition of NPOs from 'project approach' work to systematic activities under government contracts demands certain skills from the staff; this might require special training. So, one of the interviewed experts, the head of a Russian SO NPO, remarks that 'in order to participate in public procurement it is crucial to understand how much this or that work or service costs, to have an idea of what requirements are made to the quality of work or services'. To date, there are no such specialists in the organization; therefore, the head of the organization believes that the decision to participate in competitive procedures is associated with a high degree of risk.

Transition to work under state contracts might make a significant difference to the established organizational microclimate. Raising funds under

government contracts can result in the loss of SO NPOs' independence and alienation of the social control functions (Pagava et al. 2013: 7). Eventually, this might require the organization to reevaluate its mission, which will inevitably lead to losing those employees, who are not commerce focused. It should be noted here that there are studies which refute this point of view. Thus, Richard Batley and Pauline Rose notice that there is no contradiction between advocacy and service delivery (Batley, Rose 2011: 237).

Conclusion

This study adds further insights into how Russian SO NPOs operate in the public procurement market and which market segments are the most preferable for them. The research illuminates the mechanisms of giving preferential treatment to SO NPOs in compliance with the Russian legislation. Four barriers restricting SO NPOs' participation in tenders emerged from the analysis of specialist literature and the practice of SO NPOs' involvement: economic, financial, social, and organizational. Furthermore, the results of the study indicate the limited capacity of public procurement legislation to support SO NPOs. The analysis leads to the confirmation of the hypothesis measures aimed to support SO NPOs in the public procurement market fail to meet expectations due to economic, financial, social and organizational barriers.

Undoubtedly, barriers highlighted in the present study are not insurmountable for some SO NPOs. The SO NPO sector is not homogeneous in Russia. Irina Krasnopolskaya and Yulia Sokolova point out high variability in regard to the size of the sector and its financial situation (Krasnopolskaya, Sokolova 2016: 20). For example, Moscow alone accounts for one third of all revenues for socially oriented NPOs. Operating under government contracts is likely to become an important incentive to develop further for major SO NPOs in the Russian capital. Competent and targeted policies by regional authorities can also provide positive results, as evidenced by the experience of Perm and Bashkiria described above. However, as far as most Russian non-profit organizations are concerned, a public contract will still remain an optional source of funding. Overcoming these barriers is possible only if the legislation on public procurement is changed. Legislation should allow for a relatively easy entry into the public procurement market and fair competition. The authors believe that the existing legislation is unlikely to stimulate the activity of SO NPOs. The positive experience of SO NPOs' participation in public procurement in most cases is the success of government agencies in implementing the tasks assigned by the President, but not a natural process of SO NPOs' entry into new markets. We argue that the easing of legislative requirements for NGOs will allow them to become active and competitive players in the market of social service providers.

This study is the first research to identify key barriers to SO NPOs in the Russian public procurement market. Investigating these barriers helps us

work out recommendations to improve the mechanisms of attracting SO NPOs in the field of public procurement. We contend that SO NPOs should be allocated as a separate preferential group in order to compete for the right to obtain state contracts with each other, but not with commercial enterprises. It is also necessary to provide special conditions for financing SO NPOs under government contracts, for example, partial advance payment. The implementation of these measures is likely to contribute to increasing the activity of the non-profit sector in the public procurement market.

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