

## Integrity and Efficiency in Sustainable Public Contracts

Balancing Corruption Concerns in Public Procurement Internationally

Ensuring **efficiency and integrity** throughout the public procurement cycle is essential to a sound allocation of taxpayers' money. Yet public contracts are plagued by **corruption, collusion, favoritism and conflicts of interest**. This book addresses these problems from sophisticated, academic, institutional and practical perspectives.

The book's ambition is to shape the public debate in the procurement community by highlighting how corruption implies **violations of fundamental rights** and undermines the fiduciary **relationship between citizens and public institutions**. The analysis underlines how corruption may stem from - and yet be resolved - through the exercise of discretion in the public procurement system. Focusing on the **effects** of public corruption and private collusion on procurement integrity, the book marks the features of misconduct and suggests needed **counter-measures**. The work also emphasizes that the pursuit of efficiency and integrity in public contracts must be rooted in professional skills, and in ethical regulations and training for public officers.

The research reflected in these pieces comes from sources around the world, and offers an excellent foundation for further development of these topics. Expanding on prior research, this volume builds on a more active transnational academic cooperation and exchanges of ideas on integrity in public contracts for the benefit of citizens.

This book is intended as both a textbook and an edited collection and it is available as e-book too. The authors of the chapters are all specialists in their respective fields, and their different geographical and professional perspectives represent a valuable contribution to the scientific literature.

- ✓ European Law
- ✓ International Law

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Integrity and Efficiency in Sustainable  
Public Contracts

Editors

Gabriella M. RACCA  
Christopher R. YUKINS

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ADMINISTRATIVE LAW  
DIRECTOR JEAN-BERNARD AUBY

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**ADMINISTRATIVE LAW**

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Director « Mutations de l'Action Publique et du Droit Public » Centre

*Scientific Counsel*

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**Integrity and Efficiency  
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in Public Procurement Internationally

**Editors:**

*Scientific Direction*

**Gabriella M. Racca**

Professor at the University of Turin

**Christopher R. Yukins**

Professor at the George Washington University

*Scientific Committee*

Gian Luigi Albano - Head of Research, Consip S.p.A.

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## FOREWORD

It is a great pleasure for our “*Droit Administratif / Administrative Law*” series to welcome this book, edited by Gabriella M. Racca and Christopher R. Yukins and bringing together contributions of international recognized experts.

This book is based on the joint efforts made by the international research network “*Public Contracts in Legal Globalization*” (PCLG)(1) that carried out collective research on a number of topics linked to Public Contracts since 2007. Driven by the “*Governance and Public Law Centre*” (*Chaire “Mutations de l’Action Publique et du Droit Public”*) from Science Po University, the PCLG Network is made of researchers and practitioners, European and non-European. The PCLG’s publication *Comparative Law on Public Contracts* (2010) has shown that Public Procurement and Public Contracts law are very suitable topics for comparative research due to their cross-border implications. The following book *EU Public Contract Law, Public Procurement and Beyond* (2014) has remarkably showed the strategic importance of EU Law in the evolution of public contracts law.

The purpose of this book is thus to improve the outcomes of the aforementioned publications with a specific focus on integrity issues in public contracts. Corruption, collusion, favouritism and conflict of interest seem to undermine the efficiency of a relevant amount of public spending. Such discussion emerged from the workshop “*Integrity and Efficiency in Sustainable Public Contracts*” organized by Gabriella M. Racca ([www.ius-publicum.com](http://www.ius-publicum.com)) of the University of Turin and Christopher R. Yukins of George Washington University (Government Procurement Programme) in Turin on June 8<sup>th</sup>, 2012.

The Turin workshop focused on the link among integrity, objectivity of the award procedure and quality of the contract performance. During the following meeting of the PCLG-Network in Paris on December 19<sup>th</sup>, 2012, the discussion continued more in-depth with the participation also of the Procurement Unit of the Public Governance and Territorial Development office of the Organisation for Economic Co-operation and Development (OECD).

Both the workshops and the following discussions provided the outline for this collective book through an overview on the wide range of means that foster

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(1) The Network site address is: <http://www.public-contracts.net>. Since March 2013, the Network publishes a periodical, the International Journal of Public Contracts: <http://www.direitodoestado.com.br/ijpc>.

integrity and efficiency in the entire cycle of Public Contracts. In particular, the principles of transparency and accountability are both addressed as a prism for evaluating the suitability of Public Contracts and the tools for achieving the “desiderata” of any procurement system. This book highlights the issues to achieve this task from academic, institutional and practical perspectives. The research has been accomplished by different worldwide networks, and might be an excellent basis for further developments on these topics. The authors of the chapters are all specialists in their own fields and their different background, both by a geographical and professional perspective, represent a precious contribution for the scientific achievements reached by the book.

In continuity with the previous books, this research might permit to achieve a more active transnational academic cooperation and circulation of ideas on integrity in Public Contracts for the benefit of public institutions and of the citizens.

*Turin, May 2<sup>nd</sup>, 2014*

Jean-Bernard AUBY

*Professor of Public Law, Sciences Po, Paris*

*Director, Governance and Public Law Center*

*(Chaire “Mutations de l’Action Publique et du Droit Public”)*

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The Editors' gratitude goes also to the University Institute of European Study (IUSE) of Turin, which has supported the research activities at the foundation of the scientific achievements presented in the book.

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## AUTHORS AND EDITORS

**Gian Luigi ALBANO**, is Head of Research at Consip S.p.A., the National Central Purchasing Body, Italy. He obtained his PhD in Economics from the Université catholique de Louvain (Belgium) and a B.A. (Hons) from the Università “L. Bocconi” (Milan, Italy). Before joining Consip, Dr. Albano lectured at the Department of Economics of University College London from 1999 until 2005. His research topics belong to the flourishing field of the law and economics of public procurement, and his research papers are published in several international peer-reviewed journals. He is invited Professor at the University LUISS “G. Carli” (Rome, Italy), where he teaches both at the undergraduate and the postgraduate levels, as well as invited Lecturer at the Italian School of Administration (SNA) and the ITC-ILO (Turin, Italy). Dr. Albano serves as Associate Editor of the *Journal of Public Procurement*. He is an expert on public procurement for the EC, the Inter-American Development Bank, the OECD, SIGMA (joint venture between the OECD and the European Union), the World Bank, the UN and is currently advising the Italian Treasury Department on the “Emission Trading Scheme”.

**Paula BORDALO FAUSTINO**, is currently finishing her PhD research project on *Public Procurement Award Criteria in the EU Member States: A Comparative Case Study* at the School of Law, University of Nottingham (UK). She is also a part-time tutor of European Law and a teaching assistant of the Corruption module in the Executive Postgraduate Programme in Public Procurement Law and Policy at the same University. She is co-editor of the book reviews for the *Public Procurement Law Review* (PPLR). Paula is a Portuguese lawyer with experience in giving legal advice to contracting authorities throughout public procurement procedures (including litigation). She took part in the task force assigned by the Portuguese government to draft the Portuguese *Public Contracts’ Code* (implementing EC Directives 2004/17 and 2004/18). Paula also taught public procurement postgraduate courses at several Portuguese law schools, and worked as a professional trainer on public procurement for the Portuguese Public Administration.

**Roberto CAVALLO PERIN**, is Professor of Administrative Law at the Department of Law of the University of Turin and Lawyer qualified for the access to Italian Supreme Courts. His research interests include Administrative Procedure, Public Utilities Law, Local Authorities Law, Public Contracts and Public Procurement Law, Civil Service Law and Judicial Review, the Ethics of Civil Servants and Integrity Issues. He is member of the Steering Committee of the Italian *Association of Administrative Law Professors* (AIPDA), the Italian *Association of*

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*Administrative Procedural Law Professors*, the Italian Association of City Planning Law and in 2001-2006 he was Member of the Committee for the High Surveillance and Guarantee for the Winter Olympic Games of Turin. He is the Italian Director of the *Ius Publicum Network Review* – [www.ius-publicum.com](http://www.ius-publicum.com) founded in Madrid, on April 26<sup>th</sup>, 2010 by the Editorial Boards of *Die Verwaltung*, *Diritto amministrativo*, *International Journal of Constitutional Law*, *Public Law*, *Revista de Administración Pública* and *Revue Française de Droit Administratif*. The aim of *Ius Publicum Network Review* is to follow the recent developments in each network member country, focusing on the development of Administrative and Public Law in connection with other legal cultures. He is Member of the Scientific Board of the PhD Programme in *Law and Institutions* at the University of Turin, Deputy Director of the Law Review *Diritto Amministrativo* and Member of the Scientific Board of *Foro amministrativo – Consiglio di Stato*. He is a Member of the *European Law Institute* (<http://www.europeanlawinstitute.eu/>), of the *Research Network on EU Administrative Law* (<http://www.reneual.eu/>), of *Public Contracts in Legal Globalization* ([www.contrats-publics.net](http://www.contrats-publics.net)), of the *Procurement Law Academic Network* (<http://www.planpublicprocurement.org/main/>), of the *Association du Droit de la Fonction Publique* (ADFP) and of the *Association of Italian-Spanish Law Professors* (AAIS). He has published in the main international reviews in the field of Public Contracts, including *Public Contract Law Journal*, the *Public Procurement Law Review*, the *European Procurement & Public Private Partnership Law Review*, as well as in many books including in S. Arrowsmith – R. D. Anderson (eds. by), *The WTO Regime on Government Procurement. Challenge and Reform*, Cambridge, 2011. He currently teaches Public Law and Administrative Law.

**Dacian C. DRAGOS**, is Jean Monnet Professor of Administrative and European Law at the Public Administration Department of the Babes Bolyai University, Cluj Napoca, Romania, and Co-director of the Center for Good Governance Studies. He is Vice President of the Research Council of the University, he was also Vice Dean and Acting Dean of the Faculty of Political, Administrative and Communication Sciences (2008-2012); Marie Curie Fellow at Michigan State University (2005-2006); Visiting Scholar at Rockefeller College of Public Administration and Policy, SUNY Albany, USA (2002) and University of Padova (2008). He has been awarded the Romanian Writers Association National Prize for legal research (2003); Scientific Coordinator of the Commission for drafting the Administrative Procedure Code of Romania (2006-2008) and Expert in the Commission for drafting the Administrative Code (2010-2011). He is Chair of the “Law and Administration” Panel of the European Group of Public Administration (since 2010). Member of the editorial board of *European Public Procurement and PPP Law Review*, *International Journal for Court Administration*, *Transylvanian Review of Administrative Sciences*. His research publications include 2 edited books, 7 chapters in international books, 4 books in Romanian as single author and 4 in collaboration, over 30 papers in

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scientific journals. Recent publications: Dragos and Caranta (eds. by), *EU Public Procurement – Outside The Directives, Inside The Treaty?*, Djoef Copenhagen, 2012; Dragos, Neamtu and Hamlin, *Law in Action: Case Studies in Good Governance*, Institute for Public Policy and Social Research, Michigan State University, East Lansing, MI, USA, 2011; Dragos and Neamtu, *LCC in the new directive proposal*, in *European Public Procurement and PPP Law Review*, Lexxion, Germany, special issue, Sustainable public procurement, 2013; Dragos, Neamtu, Cobarzan, *Procedural Transparency in Local Administration: Linking Implementation with Administrative Capacity*, in *International Review of Administrative Sciences*, 2012; Dragos and Neamtu, *Europeanisation of Administrative Law in Romania: Current Developments in Jurisprudence and Legislation*, in *Review of European Administrative Law*, no. 1/2009, Europa Law Publishing; Dragos and Neamtu, *The Implementation of the Services Directive in Romania*, in Stelkens and Weiss (eds. by), *Implementation of Service Directive*, TMC Asser Press – Springer, 2012; Dragos and Neamtu, *Sanctions mechanisms of the World Bank on the matter of international corruption*, in M. Audit and S. Knill, *The Internationalization of Public Contracts*, Bruylant, Bruxelles, 2013; Dragos, Neamtu and Veliscu, *Judicial Review in Romania between Tradition and dialogue*, in Caranta and Gerbrandy (eds. by), *Traditions and Change in European Administrative Law*, Europa Law Publishing, Groningen-Utrecht, 2011; Dragos, Neamtu, Veliscu, *Remedies in Public Procurement in Romania*, in Treumer and Lichere (eds. by), *Enforcement of EU Public Procurement Rules*, Djøf, Copenhagen, 2011; Dragos, Gellen, Kovac and Langbroek (eds. by) *The NISPACEe*, in *Journal of Public Administration and Policy*, Vol. IV, No. 2, 2011/2012, Special Issue: Law and Public Management Revisited.

**Loredana GIANI**, is Professor of Administrative Law at the University of L'Aquila. She is Coordinator of the Master's Degree *Expert in building renovation and environment*. Member of the Arbitration Chamber of the AVCP. Member of the board of the PhD in *Institutions, market, guarantees and protection of individuals* (Department of Industrial and Information Engineering and Economics – University of L'Aquila) and the PhD in *Public, International and Comparative Law* (University of Rome, "La Sapienza"). Member of the Scientific Committee of *Rivista amministrativa degli appalti (Administrative Review Of Public Contracts)* and Co-editor of *Il diritto della cultura (Journal of Cultural Law)*. Member of the Commission for the *Reconstruction of the areas in Abruzzo devastated by the earthquake of 6 April 2009*. Responsible for national and international research projects. Speaker at numerous national and international conferences and seminars. Author of several books and numerous articles in Italian and English on Administrative Law, Administrative Process, Economic Law and Planning Law and Public Procurement.

**Anna GORCZYNSKA**, PhD, is Assistant Professor, is employed in the Chair of the European Economic Law at the Faculty of Law and Administration

of the University of Lodz, Poland. She is the Director of the Centre of Public Procurement and Public-Private Partnership. She read law at the University of Lodz and prepared her dissertation titled “Public procurement in the EU law”. She was also a law student in German universities (Münster, Giessen, Bonn). She has worked in regional lobbying offices in Brussels and regional self-government. Her main scientific interests and publications refer to public procurement law, public-private partnership, European economic law, competition law, regional policy, structure funds of the EU, e-administration, ICT, sports law. Anna Górczynska is an experienced university lecturer (lectures in English and in Polish on Public Procurement Law, European Economic Law, European Legal System, EU Structure Funds Projects) as well as trainer on the courses for both contracting authorities and entrepreneurs.

**Daniel I. GORDON**, is Associate Dean for Government Procurement Law. Before joining GW Law School in January 2012, he was the Administrator for Federal Procurement Policy, a position to which he was nominated by President Obama and confirmed by the Senate. Before that, he worked for 17 years in the Office of General Counsel of the Government Accountability Office (GAO), where he began as a line attorney, rising through the ranks and ultimately holding the positions of Deputy General Counsel and then Acting General Counsel. Among his other work at GAO, he headed the bid protest unit for a number of years, and served as counsel to the congressionally-chartered Commercial Activities Panel, which looked into questions regarding the use of contractors and federal employees to provide commercial-type services. Before joining GAO, he served as a court law clerk at the U.S. Court of Appeals for the District of Columbia Circuit and then practiced for a number of years with a private law firm in Washington, DC. Dean Gordon has frequently testified on acquisition issues before Congress, and he has published law review articles and book chapters on various aspects of procurement law and policy. During his tenure at GAO, he served for many years as a member of the Law School’s adjunct faculty. Dan Gordon has worked with many U.S., foreign, and international entities in efforts to improve acquisition policies, practices, and training, including federal agencies, the World Trade Organization, the United Nations Commission on International Trade Law, and the World Bank.

**Erling HJELMENG**, is Professor at the Department of Private Law of the University of Oslo. He is affiliated with the Centre for European Law. He is also a Visiting Professor at the Norwegian School of Economics, Bergen. His main research and teaching have been in the field of competition law and EU law, with particular focus on enforcement both on a national and international level. He has also published books and articles in the field of tort law. Since 2009, he is a co-editor of *Tidsskrift for rettsvitenskap* (Journal of Legal Science). Currently, he is the leader of the research group *Markets – Innovation – Competition* at the University of Oslo. He is regularly involved in consulting for law firms and companies as

well as public authorities, and is widely used as a speaker. He was the Chairman of the committee reviewing the Norwegian Competition Act (2011-2012).

**Ridha JENAYAH**, has a chair of Public Law and is the Dean of the PhD School at the Faculty of Law and Political Sciences of Sousse (Tunisia). He is the author of several publications in the field of Administrative Law, including a handbook of Administrative Law, (Second Ed., CPU, Tunis, 2008) and a Collection of major decisions of Tunisian Administrative Jurisprudence (CPU, Tunis 2007).

**Paolo LAZZARA**, PhD, is Associate Professor of Administrative Law at the University of “Roma Tre”. He is qualified as full Professor in Administrative law (2010). In 2008, he joined the University of “Roma Tre” as Associate Professor where he teaches Administrative Law and Environmental Law. He was Research Scholar in the “Università Sapienza” of Rome, LUISS “Guido Carli” of Rome, and in «Max Planck Institute for Comparative Public Law and International Law» in Heidelberg. His scientific activities have, above all, focused on the themes of public contracts, discretionary power and judicial review, Independent Agencies and European Law, administrative procedures. He has been lecturer and taught Administrative Law in the most important Italian Universities. He takes part in the Scientific Committee of *Diritto Amministrativo*, (Giuffrè), and in the Editing Committee of *Foro Amministrativo* (Giuffrè).

**Antonio LÓPEZ MIÑO**, is a Lawyer of the Xunta of Galicia and the current Director of Investigation of the Consello Galego da Competencia (regional competition authority). He is Professor by contract on Public Procurement for the University of Vigo, as well. During his tenure as regional lawyer he used to advise the Xunta on public contract awarding and implementation. Mr. López Miño is also a member of the Spanish Public Procurement Observatory. His current research focuses mainly on two topics: antitrust practices in the field of public procurement and innovative public procurement (pre-commercial procurement and innovation partnership).

**Jeremy McCrARY**, is Senior Policy Analyst and Public Procurement Portfolio Manager, Organisation for Economic Co-operation and Development, Governance and Territorial Development Directorate, Public Sector Integrity Division.

**Paulo MAGINA**, is Policy Analyst (Procurement), Organisation for Economic Co-operation and Development, Governance and Territorial Development Directorate, Public Sector Integrity Division.

**Francesco MANGANARO**, is Professor of Administrative Law at the University Mediterranea of Reggio Calabria where he teaches Administrative Law. He is the Scientific Coordinator of the PhD Programme in *Law and Economics* at the University Mediterranea of Reggio Calabria. He is also the scientific responsible of the Master in *Management of Local Governments*. He has taught at the Sorbonne University, in Paris and at Santiago de Compostela. He is Member of

the Steering Committee of the Italian *Association of Administrative Law Professors* (AIPDA). He is the scientific responsible of editorial series of reviews: *Percorsi di diritto amministrativo* (Routes of Administrative Law). He is a Member of scientific boards of National and International reviews. He wrote on the principle of *bona fide* in Administrative Law and on the participation in the Italian administrative proceedings and on the motivation of the administrative act. His research interests include also the inactivity of Public Administration, the coordination and cooperation among public entities especially concerning the agreement of program, the interlocutory judgment towards of public entities, the local entities and the administrative simplification.

**Bernardo G. MATTARELLA**, is Professor of Administrative Law at the University of Siena Law School and in the Luiss “Guido Carli” University Law School, Rome. Head of the Legislative Office of the Italian Minister of Public Administration. He was awarded the “Giuseppe Mantellini” Prize of the Accademia Nazionale dei Lincei for public administration studies (2008). Clerk at the Italian Constitutional Court (1995-1996 and 2007-2009). Member of several study commissions appointed by the Italian Government, including the Commission on Transparency and Corruption in Public Administration (2012). Member of the Group of Specialists on Public Ethics at Local Level of the Council of Europe. Participant and director of many group researches. Rapporteur in over 150 symposiums and seminars in Italy and abroad. Author of over 300 scientific publications from 1993 to 2014. Deputy Editor of the *Rivista trimestrale di diritto pubblico*.

**Peter T. MCKEEN**, is Adjunct Faculty at the University of Virginia (U.S.). Peter T. McKeen’s public procurement experience spans a period of more than 25 years. Mr. McKeen’s experience includes work in the administration of public contracts and as a procurement analyst for a number of U.S. based national law firms specializing in public procurement law, where he performs research and analysis on the full spectrum of procurement law issues. Mr. McKeen has served as a member of the adjunct faculty for the University of Virginia’s Procurement and Contracts Management Program since 2002. Mr. McKeen has authored course materials and texts, academic papers and articles on procurement law and contract management topics and he participates in academic workshops and conferences promoting the study and reform of national procurement systems. Mr. McKeen is co-author with Michael E. Giboney of *Federal Procurement Law For The Contracts Professional*. Mr. McKeen received his B.A. from the University of Southern Maine and his M.A. from the George Washington University.

**Bogdana NEAMTU**, PhD, is Associate Professor at the Public Administration Department of the Babes Bolyai University, Cluj Napoca, Romania, and co-director of the Center for Good Governance Studies. Her academic background includes a BA in public administration (2002) and a M.A. in European law (2003) from Babes Bolyai, as well as a M.A. in urban planning from Michigan State

University, USA (2006). She obtained her PhD in Sociology in 2008, with a topic on urban growth management in Romania. Since 2009, she has been involved in several researches on public procurement. Her publications include 5 chapters in international books, 3 books as single author and 2 co-edited, over 20 articles in journals. Recent publications: Dragos and Neamtu, *Effectiveness of administrative appeals – Empirical evidence from Romanian local administration*, in *Lex Localis-Journal of Local Self Governmeent*, vol.1/1, 2013; Dragos and Neamtu, *LCC in the new directive proposal*, in *European Public Procurement and PPP Law Review*, Lexxion, 2013; Neamtu, *Measuring the social sustainability of urban communities: the role of local authorities*, in *Transylvanian Review of Administrative Sciences*, 2012, no. 37E, 112-127; Dragos, Neamtu and Cobarzan, *Procedural transparency in rural Romania: Linking implementation with administrative capacity?*, in *IRAS*, 2012, 78(1), 134-157; Dragos and Neamtu, *The Implementation of the Services Directive in Romania*, in Stelkens and Weiss (eds), *Implementation of Service Directive*, TMC Asser Press – Springer, 2012; Dragos, Neamtu and Hamlin, *Law in Action: Case Studies in Good Governance*, IPPSR & Center for Good governance Studies, East Lansing, Michigan, USA, 2011; Dragos and Neamtu, *Europeanisation of Administrative Law in Romania: Current Developments in Jurisprudence and Legislation*, in *Review of European Administrative Law*, no. 1/2009, Europa Law Publishing.

**Gabriella M. RACCA**, is Professor of Administrative Law and Deputy Director of the Department of Management at the University of Turin. Her research interests include Administrative Procedure, Public Services, Public Contracts and Public Procurement, Concessions, PPP, Public Accountability and Integrity issues. She is in charge of the Italian Unit of the EU project on Public Procurement for Innovation (PPI), *Healthy Ageing in Public Procurement of Innovation* – <http://www.happi-project.eu/>, funded by the EU Commission (DG Enterprises – Call ENT/CIP/11/C/N02C011) for the drafting of an innovative EU joint procurement system in the Healthcare sector. She is Member of the Scientific Board of the *Master Programme on Public Procurement Management for Sustainable Development* of the International Training Centre of International Labour Organization (ITC – ILO) in partnership with the University of Turin, as well as Member of the *Master en Gouvernance et Management des Marchés Publics en Appui au Développement Durable* of the ITC – ILO, the University of Turin and SciencesPo (Paris). She has been consultant to the Organisation for Economic Co-operation and Development (OECD). She coordinates the *Ius Publicum Network Review* – [www.ius-publicum.com](http://www.ius-publicum.com) founded by *Die Verwaltung*, *Diritto amministrativo*, *International Journal of Constitutional Law*, *Public Law*, *Revista de Administración Pública* and *Revue Française de Droit Administratif*. She is Member of the *International Society of Public Law-ICON-S* ([www.icon-society.org](http://www.icon-society.org)), of the Scientific Board of the PhD Programme in *Law and Institutions* at the University of Turin, and of the Scientific Committee of

the reviews *Diritto Amministrativo* and *Foro Amministrativo – Consiglio di Stato*. She is a Member of the *European Law Institute*, of the *Research Network on EU Administrative Law*, of *Public Contracts in Legal Globalization*, of the *Procurement Law Academic Network*, of the *European Procurement Law Group*, of the *British Institute of International and Comparative Law* and of the *Istituto Italiano di Scienze Amministrative*. She has recently published in *Public Procurement Law Review*, “Collaborative procurement and contract performance in the Italian Healthcare Sector: illustration of a common problem in European procurement”, 2010, 119; in *Public Contract Law Journal*, “Competition in the execution phase of public procurement”, vol. 41, 2011, 89; in *Ius Publicum Network Review – www.ius-publicum.com*, “The Electronic Award and Execution of Public Procurement”, 2012; in *European Procurement & Public Private Partnership Law Review*, “Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption” (with R. Cavallo Perin), 2013, 279-293; in S. Arrowsmith – S. Treumer (eds. by), *Competitive Dialogue*, Cambridge, 2012, “Competitive dialogue in Italy”; in C. Harland – G. Nissimbeni – E. Schneller (eds. by), *Strategic Supply Management (SAGE Handbook)*, London, 2013, “Collaborative Public Procurement and Supply Chain in the EU experience”; in R. Caranta and M. Trybus (eds. by) *The Law of Green and Social Procurement in Europe (European Procurement Law Series)*, Copenhagen, 2010, “Aggregate Models of Public Procurement and Secondary Consideration: an Italian Perspective”; in S. Treumer – F. Lichère (eds. by) *Enforcement of the EU Public Procurement Rules*, Copenhagen, 2011, “Derogations from the standstill period, ineffectiveness and remedies in the new tendering procedures: efficiency gains vs. risks of increasing litigation”; in D. Dragos – R. Caranta (eds. by) *Outside the EU Procurement Directives – Inside the Treaty?*, Copenhagen, 2012, “The Role of IT solutions in the Award and Execution of Public Procurement below Threshold and List B Services Overcoming E-Barriers”; in M. Comba – S. Treumer (eds. by) *Award of Contracts in EU Procurements*, Copenhagen, 2013, “The Electronic Award of Public Procurement”.

**Bushra RAHMAN**, is a graduate medical student (Class of 2017) at the University of Arizona, Tucson, AZ. She worked as a Research Associate and Administrator for the Health Sector Supply Chain Research Consortium (HSRC-ASU) between 2008-2013. Her educational background includes a Masters in Business Administration and Masters in Health Sector Management, W.P. Carey School of Business, ASU, AZ. She has also worked in the Pharmaceutical industry in India and looks forward to practicing clinical medicine in the future.

**Antonio ROMANO-TASSONE**, was Professor of Administrative Law at the University of Messina (from 2005). Previously he was Professor of Administrative Law at the University of Reggio Calabria (since 1990) and Catanzaro (1997). He was *Professeur invité* at the University of Paris 1 (Sorbonne) and 3 Lyon (Jean Moulin).

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He was Member of the Board of Directors of *Ius Publicum Network Review* – [www.ius-publicum.com](http://www.ius-publicum.com) and Member of the Scientific Committee of several Italian Public Law Review such as *Diritto Amministrativo*, *Diritto e Processo Amministrativo*, *Foro Amministrativo*, *Sanità Pubblica e Privata*). He was Member of the Steering Committee of the *Association of Italian-Argentinian Administrative Law Professors* and of the Italian *Association of Administrative Law Professors* (AIPDA).

**Anna ROMEO**, is Associate Professor of Administrative Law at the Department of Law at the University of Messina where she is also Member of the Scientific Board of the PhD Programme in *Juridical Sciences*. She attained the national scientific qualification as full Professor. She taught Administrative European Law and Public Law of Economics at the LUSPIO – Rome where she was researcher from 2008 to 2011. She is Member of the Editing Committee of the Journal *Diritto e processo amministrativo* (*Law and Administrative Process*), published by ESI, and author of two books: *L'impugnabilità degli atti amministrativi* (Actionability of administrative acts) and *Collegialità e ruolo presidenziale nella sentenza amministrativa* (Collegiality and presidential role in the administrative judgment) as well as of various articles on administrative procedure, silence of public administration, public procurement, electoral disputes, expropriation.

**André SADDY**, PhD, Postdoctoral fellow at the University of Oxford; PhD in Administrative Law from the University Complutense at Madrid; Master in Public Administration from the University of Lisbon and Postgraduate in Public Regulation and Competition at the University of Coimbra. He is an adjunct professor at the Fluminense Federal University (Niterói, Brazil) and Professor of the Master in Constitutional Law in this same institution. He is currently CEO of the Centre for Empirical Legal Studies – CEEJ and founding partner of the office Saddy Lawyers. He has published several articles in Brazilian and International journals, is coordinator of several collective books and has recently published three books: *Administrative discretion in the rule of law*; *Forms of action and intervention of the Brazilian state in the economy*; *Administrative silence in the Brazilian system*.

**Albert SÁNCHEZ GRAELLS** joined the Law School of the University of Leicester as Senior Lecturer in Commercial Law in October 2013. Until September 2013 he was Lecturer in Law at the University of Hull, where he was Director of the Hull Commercial Law and Policy Centre. Prior to this appointment and since October 2009, Albert was Lecturer in European and Commercial Law at the Law Faculty of the Comillas Pontifical University (Madrid, Spain), as well as Director of its Master in International and European Business Law. Albert has spent significant research time at the Library of Congress (Washington, USA), the Centre for Competition Law and Policy of the University of Oxford (UK) and the Law Department of the Copenhagen Business School (DK). His main publication to date is *Public Procurement and the EU Competition Rules* (Oxford, Hart, 2011), of which he is preparing a second edition.

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**Eugene S. SCHNELLER**, is Professor of Supply Chain Management, W.P. Carey School of Business, Arizona State University. He is Co-Director of the Health Sector Supply Chain Research Consortium. His research and consulting bring the most recent strategic thinking into practice for hospitals, group purchasing organizations and distributors. His book, *Strategic Management of the Health Care Supply Chain*, is the recognized standard for analysis of health care supply chain management in the U.S. His book, *Orchestrating Change in the Public Services*, provides a penetrating analysis of large scale innovation in both the health and educational sectors in the U.S., England and Canada. He is a co-author of *The Sage Handbook of Strategic Supply Management*. He was named, in 2007, one of the most influential individuals in the area of health sector supply chain management. He is a frequent key-note speaker at professional and trade meetings in the US, Canada and Europe.

**Tina SØREIDE**, PhD, is a postdoc researcher in Law and Economics at the Faculty of Law, University of Bergen in Norway, on leave from Chr. Michelsen Institute (CMI). She holds a PhD in Economics from the Norwegian School of Economics and Business Administration (NHH) and a Master from the Department of Economics, University of Bergen. Previously she worked at the World Bank in Washington DC. She teaches several courses, including Political Economy and the Economics of Corruption. Her publications address primarily criminal law and corruption-related issues in governance and sector regulation.

**Patricia VALCÁRCEL**, is Associate Professor of Administrative Law at the University of Vigo. She worked as a lawyer specialised in Administrative Law for *Garrigues Abogados y Asesores Tributarios*, where she achieved experience in the field of national and international public contracts. Professor Valcárcel has widely published on execution and financing of Public Works and Public Private Partnership. Her current research focuses on three main topics: Central Purchasing Bodies; Definition of Awarding Procedure Rules; Enforcement of Public Procurement Law. Professor Valcárcel has been a Member of the Spanish Public Procurement Observatory since it was created. She is also Member of several international research networks on this field.

**Francisco Javier VÁZQUEZ MATILLA**, PhD, is Member of the Procurement Administrative Court of Navarre. Legal Counsel of the City of Pamplona (Spain). Masters in Specialization and Research in Law. PhD student in public procurement. Member Group Technical Committee on Information Society and New Technologies of the Spanish Federation of Municipalities. Secretary of the Committee on Contracting Oversight Pamplona City Council. He has spoken at numerous presentations on good practices in public procurement, new directives, contract modifications for various Spanish and foreign universities and various administrations, federations, institutes and public agencies. He has twenty publications including books and journal articles. He has been editor of various

laws for adaptation in Spain of the public procurement directives and of the different administrations expressed opinions on contractual changes.

**Natalia WILSON, MD, MPH** is co-director of the Health Sector Supply Chain Research Consortium at Arizona State University (HSRC-ASU) and research assistant professor in the College of Health Solutions. Dr. Wilson's clinical experience has included partnership in a community-based private internal medicine practice where she focused on preventive medicine and women's health. Her current areas of research include unique device identification, building collaborative relationships in health care and physician engagement in the health care supply chain. Recent publications include *Revision Total Hip and Knee Arthroplasty Implant Identification: Implications for Use of Unique Device Identification*, *Value of Unique Device Identification in the Digital Health Infrastructure*, *Engaging Physicians in Collaborative Supply Cost Management*, *Aligning Stakeholder Incentives in Orthopaedics*, and *Hip and Knee Implants: Current Trends and Policy Considerations*.

**Christopher R. YUKINS** is Professor in Government Procurement Law at the George Washington University and Co-Director of the Government Procurement Law Program. He has many years of experience in public procurement law. He was for several years a trial attorney with the U.S. Department of Justice, where he handled trials and appeals involving bid protests and contract claims against the U.S. government. He teaches on government contract formations and performance issues, bid protests, Contract Disputes Act litigation, and comparative issues in public procurement, and focuses especially on emerging public policy questions in U.S. procurement.

He is an active member of the Public Contract Law Section of the American Bar Association, serves on the steering committee to the International Procurement Committee of the ABA International Law Section, and previously served as the president of the Tysons Corner Chapter of the National Contract Management Association. He is a faculty advisor to the Public Contract Law Journal, and has contributed pieces on procurement reform, international procurement, electronic commerce and information technology to a broad range of journals, including Washington Technology, Government Contractor, Legal Times, and Federal Computer Week. He has published on procurement reform in scholarly journals, including the Public Contract Law Journal, Georgetown Journal of International Law, and Public Procurement Law Review (United Kingdom). Together with Professor Steven Schooner, he runs a popular *colloquium* series on procurement reform at The George Washington University Law School. In private practice, Professor Yukins has been an associate, partner, and of counsel at leading national firms; he is currently of counsel to the firm of Arnold & Porter LLP. He was an advisor to the U.S. delegation to the working group on reform of the United Nations Commission on International Trade Law (UNCITRAL) Model Procurement Law, and he teaches and speaks often on issues of comparative and international procurement law.



# Introduction.

## Steps for integrity in public contracts

BY

Gabriella M. RACCA

Professor of Administrative Law, University of Turin

Christopher R. YUKINS

Professor in Government Procurement Law,  
George Washington University

### 1. Introduction

Integrity of public procurement processes is universally recognized as a necessary condition to achieve public objectives, and thus to make proper use of precious taxpayer resources.(1) Lack of integrity in public procurement at any level of Government is, however, a well-documented phenomenon, which takes several and sometimes surprising forms.(2) The (estimated) economic cost of corrupt procurement is staggering,(3) and it exerts a profoundly negative impact not only on the economy of States but also on citizens' rights.(4)

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(1) P. TREPTE, *Regulating Procurement. Understanding the Ends and Means of Public Procurement Regulation*, Oxford University Press, 2004; P. TREPTE, *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Procurement: Possibilities and Limitations*, 2005, available at [https://bvc.cgu.gov.br/bitstream/123456789/transparency\\_and\\_accountability\\_tools.pdf](https://bvc.cgu.gov.br/bitstream/123456789/transparency_and_accountability_tools.pdf); J.-B. AUBY – E. BREEN – T. PERRAUD, *Corruption And Conflicts Of Interest. A Comparative Law Approach*, Edward Elgar Publishing, 2014; S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform*, Cambridge, 1999, 4 and 9-25; S. ROSE-ACKERMAN, *Introduction: The Role of International Actors in Fighting Corruption*, in S. Rose-Ackerman & P. Carrington (eds.), *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, Carolina Academic Press, 2013, 8-9; OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, 2013, available at <http://www.oecd-ilibrary.org/>, 77-88.

(2) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, 3 February 2014, 8 et seq.

(3) It is estimated that corruption represents 5 % of global GDP (USD 2.6 trillion), with over USD 1 trillion paid in bribes each year; it is further estimated that corruption adds up to 10 % of the total cost of doing business on a global basis and 25 % of the cost of procurement contracts in developing countries. The economic costs incurred by corruption in the EU possibly amount to EUR 120 billion per year. See: OECD, CleanGovBiz, *Integrity in Practice*, 2014 available at <http://www.oecd.org/cleangovbiz/49693613.pdf>, 4. This is one percent of the EU GDP, representing only a little less than the annual budget of the EU. See OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 78; EU Home Affairs Department, data available at the home page of DG Home affairs: [http://ec.europa.eu/dgs/home-affairs/what-we-do/agencies/index\\_en.htm](http://ec.europa.eu/dgs/home-affairs/what-we-do/agencies/index_en.htm).

(4) Transparency International estimates that “systematic corruption can add at least 20-25 % to the cost of government procurement” see: International Council on Human Rights Policy – Transparency International, *Integrating Human Rights in the Anti-corruption Agenda. Challenges, Possibilities and Opportunities*, 2010, available at [http://www.ichrp.org/files/reports/58/131b\\_report.pdf](http://www.ichrp.org/files/reports/58/131b_report.pdf), 43; EU Agency for

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In order to understand corruption in public procurement, it is important to comprehend the procurement process. Public contracting processes broadly follow the same general steps. There are generally three phases of the public procurement process: the pre-tender stage, the tendering stage and the post-tender stage. Corruption risks exist throughout the entire procurement cycle.<sup>(5)</sup>

It is important to note that the tendering stage in public procurement, in particular, is highly regulated. International texts on procurement, especially the UNCITRAL Model Law, the WTO Government Procurement Agreement (GPA) and the EU Procurement Directives, focus on this stage. Practice, however, shows that corruption risks in the procurement cycle can be equally high before the tender process even begins (in the pre-tender or planning stage) or once the contract has been awarded (in the post-tender stage).<sup>(6)</sup>

Policymakers crafting a sound procurement system must balance a number of goals.<sup>(7)</sup> Of those goals, experience has shown that competition, transparency and integrity are probably the most important ones.<sup>(8)</sup> If a government's procurement system reflects all three elements, the system is much more likely to achieve best value in procurement and to maintain political legitimacy.<sup>(9)</sup> These central goals, moreover, complement one another. A fully transparent procurement system is far

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Fundamental Rights (FRA), *Fundamental rights: challenges and achievements in 2012*, 2013, available at <http://fra.europa.eu/en/press-release/2013/eu-agency-fundamental-rights-fra-presents-its-annual-report>, 12 et seq.; International Council on Human Rights Policy, *Corruption and Human Rights: Making the connection*, 2009, available at [http://www.ichrp.org/files/reports/40/131\\_web.pdf](http://www.ichrp.org/files/reports/40/131_web.pdf). See: R. CAVALLO PERIN – G. M. RACCA, *Corruption as a violation of fundamental rights: reputation risk as a deterrent to the lack of loyalty*, in this volume.

(5) OECD, *Recommendation of the Council on Enhancing Integrity in Public Procurement*, C(2008)105, 2008, available at <http://acts.oecd.org/>; United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, September 2013, available at <https://www.unodc.org/>, 1; S. WILLIAMS-ELEGBE, *Fighting Corruption in Public Procurement: A Comparative Analysis of Disqualification Measures*, Hart Publishing, 2012, 38 et seq.

(6) United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit.

(7) S. L. SCHOONER, *Desiderata: objectives for a system of government contract law*, in *PPLR*, 2002, 107, in that article, Schooner outlined nine objectives, or desiderata, of public procurement systems: competition, integrity, transparency, efficiency, customer satisfaction, best value, wealth distribution, risk avoidance, and uniformity. C. H. BOVIS, *EU Public Procurement Law*, 2007, 72 et seq. In order to achieve the secondary goals see: S. ARROWSMITH – P. KUNZLIK, *Social and Environmental Policies in EC Procurement Law: New Directives and New Directions*, Cambridge, 2009. For ensuring sound procedures see: *Modernisation Green paper*, para. 5, 48 et seq.

(8) C. R. YUKINS, *Integrating Integrity and Procurement: The United Nations Convention Against Corruption and the UNCITRAL Model Procurement Law*, in *PCLJ*, 2007, 308; P. TREPTE, *Regulating Procurement. Understanding the Ends and Means of Public Procurement Regulation*, Oxford University Press, 2004; ID., *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Procurement: Possibilities and Limitations*, 2005, cit.

(9) OECD, *Fighting Corruption and Promoting Integrity in Public Procurement*, 2005, 22 et seq.; R. HODESS, *Civil Society and Nongovernmental Organisations as International Actors in Anti-Corruption Advocacy*, in R. S. Ackerman – P. Carrington (ed. by) *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, cit., 75 et seq.

less likely to have problems with integrity, as many more stakeholders can exercise oversight in a transparent procurement system.<sup>(10)</sup> The reverse is also true: a system with weak strategies to enforce integrity will probably have shoddy competition, and transparency is likely to erode as corruption drains the procurement system of political legitimacy.<sup>(11)</sup> Too often competition and transparency have been dealt with as issues of procurement reform, while integrity has been addressed separately, as part of anti-corruption initiatives.<sup>(12)</sup>

This book aims at examining the integrity issues together with the procurement rules and practices in order to highlight the criticalities and the possible solutions.

Safeguarding efficiency of public spending requires a mindset shift among public officials and in public entities' organizational models. To ensure legitimate procurement procedures and adequate public records, many elements are required: the establishment of a sound procurement system; transparency in procurement; objective decision-making in procurement; domestic review, or bid challenge, systems; integrity of public officials; and soundness of public records and finance. Efforts to promote such principles and instruments in order to prevent corruption must be maintained throughout the cycle of public procurement, from the beginning of the procurement procedure to the conclusion of the performance phase.<sup>(13)</sup>

Corruption in the field of public procurement usually involves a series of actors. The key actors facilitating corruption in public contracts are the entity paying the bribe and the recipient of the bribe. The briber is usually the legal entity competing for and delivering on contracts (e.g., the bidder, including consortium partners, subcontractors or suppliers).<sup>(14)</sup> The recipient

(10) EU Commission, *Fighting corruption in the EU*, 6 June 2011, COM (2011) 308 final, in <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52011DC0308:EN:NOT>, 10-14; C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, in *PCLJ*, 2010, 71-79.

(11) EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, 2013, in <http://bookshop.europa.eu/>, 29 et seq. United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 2.

(12) United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit.

(13) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 26-27; G. M. RACCA – R. CAVALLO PERIN – G.L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011, 89-108, also available at: [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2011114](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2011114); G. M. RACCA – R. CAVALLO PERIN, *Material Amendments of Public Contracts during their Terms: From violations of Competitions to Symptoms of Corruption*, in *European Procurement & Public Private Partnership Law Review*, 2013, 279-293; C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, cit., 70-71.

(14) EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, cit., 23-29.

of the bribe is usually a procurement official with the procuring entity who is responsible for awarding and/or managing the public contract. Frequently, bribes do not flow directly between the bidder and the procuring personnel but instead through an agent, consultant or other intermediary. Corruption – broadly understood here to mean a breakdown in the best-value procurement process – may take place even when no procurement officer is involved. A good example of this are anti-competitive agreements, such as price fixing between bidders.<sup>(15)</sup> Similarly, politicians tainted by corruption can attempt to influence a decision to initiate a procurement procedure, or to award a particular contract to a certain company.<sup>(16)</sup> Sound legal frameworks for public procurement and anti-corruption are important pillars in the fight to reduce corruption.<sup>(17)</sup> Both are prerequisites for a transparent, competitive and objective procurement system. Respect for the rule of law is essential. Experience has shown, however, that legislation alone is not sufficient to prevent corruption in public procurement. If that were the case, corruption in public procurement would barely exist in countries with advanced legal regimes based, for example, on the UNCITRAL Model Law or the EU Directives; indeed, on the contrary, excessive regulation can favor a lack of integrity.<sup>(18)</sup> It is essential that legal frameworks be supported by other efforts to ensure qualities such as accountability and integrity. Various additional strategies have proven to be particularly useful in fighting corruption in public procurement.<sup>(19)</sup>

It is very difficult to create “incentives” in public procurement for public officials as there is too little political support for high government pay, or for large bounties for “good” contractors.<sup>(20)</sup> The real dichotomy, therefore, is not between “incentives” and “disciplinary measures”, but rather between “transparency” and “disciplinary measures”. Of the two, in the long run transparency seems to be the better course. It forces officials to act with far less corruption, and it opens the procurement process to more stakeholders, which ultimately makes the procurement system much stronger. While disciplinary measures

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(15) OECD, *Guidelines for Fighting Bid Rigging in Public Procurement* OECD, 2009; OECD, *Recommendation of the Council on Fighting Bid Rigging in Public Procurement*, 17 July 2012, in <http://acts.oecd.org/>.

(16) S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform*, cit., 27-38; EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 8-9.

(17) EU Commission, *Fighting corruption in the EU*, cit., 12 et seq.

(18) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report, Italy annex*, COM(2014) 38 final.

(19) United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 24.

(20) OECD, *Integrity in Public Procurement: Good Practice From A to Z*, in <http://www.oecd.org/>, 2007, 56.

are important and inevitable, it seems that transparency should always be the first choice, as it enhances both competition and integrity.(21)

Ethics regulations for officers and employees of procuring entities usually require procurement officials to pursue ethical, fair and impartial procurement procedures in line with applicable legislation and tendering rules for a particular procurement.(22) Public officials should promote and maintain the highest standards of probity and integrity in all their dealings. In assessing ethics requirement for public officials, including procurement officials, policymakers may wish to consider that ethics rules and screening procedures are almost always part of a broader fabric of social norms, laws and mechanisms for ensuring social harmony. In that light, the ethics rules crafted to protect the procurement system should complement the broader set of norms and rules, and may well draw upon other formal and informal mechanisms for maintaining social order.(23)

The key puzzle in public procurement is, in fact, what economists would call a “principal-agent” problem. In public procurement governments regularly use agents, contracting officials, as intermediaries. This occurs because governments are unsure of who the principal is – either the legislature, or the people, or the agency itself – and so the contracting official can serve as a sort of proxy for the collective goals of the uncertain principal. The contracting official, while ostensibly the agent, in fact becomes a proxy for the principal.(24)

The principal-agent model lends new clarity to concerns about integrity and corruption.(25) Someone could argue that the anticorruption regime is

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(21) The UNCITRAL Model Law is designed so that, as countries evolve (develop more sophisticated anti-corruption systems, for example), those countries will be able to deploy more sophisticated procurement systems, to achieve better value.

(22) P. TREPTE, *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Procurement: Possibilities and Limitations*, cit., 25 and 36; Transparency International, *Handbook for Curbing Corruption in Public Procurement*, available at <http://www.transparency.org/>, 2006, 65-72.

(23) United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 11-12.

(24) The contracting officer can buy a reasonably fast jet plane for the government, whereas the pilot (left to his own devices) would buy an outrageously expensive plane, while a taxpaying citizen (who has to pay for the plane) might buy a dangerously slow jet plane. “A strongly hierarchical organizational mechanism suggests that the ‘principal’ is the bureaucracy itself – that there are not clear lines of accountability to those outside the government organization. As a governance mechanism, this probably is not optimal. The alternative is to ‘flatten’ the government, to give contracting officials more authority, but at the same time to make them more accountable to members of the public outside government. This can be done by making each stage of the procurement process – planning, solicitation, competition and award – more transparent, so that others can view the procurement process as it unfolds. It can also be done by establishing sound systems for review, such as remedies systems that allow for challenges by affected third parties”. See also: P. TREPTE, *Regulating Procurement*, cit., 129-132.

(25) C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, cit., 70. OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, 2013, available at <http://www.oecd-ilibrary.org/>, 32 et seq.

sometimes overly cumbersome and inefficient because, beyond normal anti-bribery provisions, a vast array of lesser anticorruption rules impose additional constraints on procurement officials to discourage gratuities, constrain “revolving door” contacts, and bar the distribution of sensitive information.<sup>(26)</sup> Agency theory suggests, however, that those additional constraints are necessary because as the chain of authority stretches from principal to agent, and from this latter to subagent, the risk that the procurement actions will diverge from the principal’s goals rises dramatically, and so there must be special legal controls to dampen the corrupt conflicts of interest that could otherwise arise.<sup>(27)</sup>

By applying the principal-agent model it is possible to adopt an extensive oversight mechanism (as in place in the U.S. system) reflecting “monitoring” and “bonding”, undertaken in order to align procurement (the actual purchasing of goods and services) with the “principal’s” (or “the public’s”) interests. Again applying this model, an active press can provide low-cost monitoring (and thus reduce risk), much as whistleblowers serve as surrogate monitors and enforcers of the principal’s interest. Bid protests, under this model, are arguably another means of monitoring and of forcing procurement officials to adhere closely to the principal’s goals, as defined by the procurement rules, including the conflict-of-interest rules.<sup>(28)</sup>

Extending the agency model, fraud actions brought by whistleblowers are arguably stopgap solutions to enforce monitoring and bonding on the principal’s behalf where contracting officials have failed to detect fraud or malfeasance. Finally, under this model, those who admonish procuring officials to follow the rules, including those in the “accountability” community (auditors, lawyers, courts, and for example, the U.S. Government Accountability Office) are merely reinforcing that same monitoring role.<sup>(29)</sup>

Conflicts of interest, as economists understand them, are a natural result of a principal-agent relationship. An agent (here, a contracting official) may exploit his information asymmetry (his greater knowledge) to take advantage of an opportunity that may well be at odds with the goals of the principal.<sup>(30)</sup>

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(26) C. R. YUKINS, *Integrating Integrity and Procurement: The United Nations Convention Against Corruption and the UNCITRAL Model Procurement Law*, *cit.*, 321-323.

(27) C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, *cit.*, 63 et seq.

(28) D. I. GORDON, *Bid Protests: The Costs are Real, but the Benefits Outweigh Them*, in *PCLJ*, 2013, also in *GW Law School Public Law and Legal Theory Paper*, No. 2013-41, 43 et seq.; D. I. GORDON, *Constructing a Bid Protest Process: Choices Every Procurement Challenge System Must Make*, in *PCLJ*, 2006, 434.

(29) C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, *cit.*, 2010, 70.

(30) P. TREPTE, *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Procurement: Possibilities and Limitations*, *cit.*, 6 et seq.

To combat this – to force the agent/contracting official to pursue the principal's ends – economists suggest the use of monitoring (transparency) or sanctions (discipline).(31) Of the two, monitoring and increased transparency in the procurement process ensure that the official follows the principal's goals (the goals of the people, or the legislature, whoever is considered the “principal”) honestly and effectively. For these reasons, ethics rules typically require public officials to disclose gifts that they might receive, or outside financial interests that might tie them to prospective contractors.(32)

Another, emerging approach is to force self-reporting by highly motivated organizations – including contracting firms. In the United States federal system, the government recently initiated a system of mandatory self-reporting by contractors, if they discover, among other things, fraud or certain criminal activities internally (through rapidly maturing ethics and compliance systems).(33)

Whistleblowing allows insiders to provide information to other individuals or organizations, such as the compliance officer within the corporate structure of a private company participating in a public tender or a public anti-corruption authority, so they can take the necessary ameliorative steps. It is absolutely essential to have effective whistle-blower protection systems in place in order to encourage reporting of corruption.(34)

In order to accomplish these broader integrity goals, this book highlights the importance of education in establishing a cadre of professional procurement personnel. Their specialized knowledge sets them apart, and creates a community – that is, “self-cleaning” members of the cadre will monitor one another, and so will discourage corruption. Training will vary from organization to organization within the procurement system. Leaders in the system need to make very clear the core principles in a successful system – transparency, integrity, and effective competition – to guide the training undertaken by individual organizations within the system.

Along these same lines, electronic procurement is emerging as another tool for improving public procurement systems. The use of electronic procurement can be very efficient in increasing competition and transparency and

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(31) OECD, *Integrity in Public Procurement: Good Practice From A to Z*, cit., 29 and 89 et seq.

(32) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, 29; EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, cit., 55.

(33) L. E. HALCHIN, CRS Report for Congress Prepared for Members and Committees of Congress, *Transforming Government Acquisition Systems: Overview and Selected Issues*, 20 June 2013, available at: <https://www.fas.org/sgp/crs/misc/R43111.pdf>.

(34) United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 27.

in reducing corruption in public procurement.(35) E-procurement in the area of anti-corruption is also important for other reasons. In particular, e-procurement has the advantage of allowing for easy data generation and data management.(36) This could in particular be helpful in the assessment of offered prices, to assess whether bid prices are reasonable and in line with market rates, by benchmarking collected data such as prices/price items in an electronic database with offered prices in a particular tender procedure in order to detect overpricing or bid rigging.(37)

“Blacklisting”, or debarment, is also considered a useful instrument to fight corruption in public procurement,(38) but there are several different models: a highly discretionary model, with rigorous but informal procedures, focused first on issues of performance risk (e.g., the United States);(39) a more structured and adjudicative approach, focused on issues of fiduciary loss (“leakage” through corruption) and reputational risk (e.g., the World Bank sanctions process)(40) and, the European approach, which remains a somewhat uneven hybrid of the discretionary and the compulsory, with only loosely described procedures.(41) Discussions between officials in the various procurement communities and discussions including debarment officials and their stakeholders, would be a very useful way to harmonize sanctions systems, and to regularize the incentives and deterrents regarding fraud, corruption and poor performance.(42)

Civil society plays a vital role in monitoring procurement. Because of the complexity of procurement, however, members of civil society – professors,

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(35) G. M. RACCA, *The role of IT solutions in the award and execution of public procurement below threshold and list B services: overcoming e-barriers*, in D. Dragos – R. Caranta (eds. by) *Outside the EU Procurement Directives – Inside the Treaty?*, Djøf Publishing, Copenhagen, 2012, 373-395.

(36) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 31-32.

(37) G. M. RACCA, *The Electronic Award and Execution of Public Procurement*, in *Ius Publicum Network Review*, 2012, available at [www.ius-publicum.com/repository/uploads/17\\_05\\_2013\\_19\\_31-Racca\\_IT\\_IUS-PUBLICUM-EN.pdf](http://www.ius-publicum.com/repository/uploads/17_05_2013_19_31-Racca_IT_IUS-PUBLICUM-EN.pdf), 16 et seq.; United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 27. All the tools of e-procurement (e.g. e-communication, e-submission, e-tendering, etc.) have one essential effect: they eliminate or minimize the direct human interactions between bidders and the procurement personnel, interactions which are one of the main sources of corrupt behavior in public procurement.

(38) S. WILLIAMS-ELEGBE, *Fighting Corruption in Public Procurement: A Comparative Analysis of Disqualification Measures*, cit., 38 et seq. S. SCHOONER, *The Paper Tiger Stirs: Rethinking Exclusion and Debarment*, in *PPLR*, 2004, 211-216.

(39) U.S. Gov’t Accountability Office, GAO Report, *Suspension and Debarment*, September 2012, available at: [www.gao.gov/assets/650/648577.pdf](http://www.gao.gov/assets/650/648577.pdf).

(40) C. R. YUKINS, *Rethinking the World Bank’s Sanctions System*, November 2013, *GWU Legal Studies Research Paper No. 2013-132*, available at <http://ssrn.com/abstract=2357691>.

(41) H. PUNDER – H.-J. PRIESS – S. ARROWSMITH (eds. by), *Self-Cleaning in Public Procurement Law*, Carl Heymanns, 2009.

(42) C. R. YUKINS, *The European Procurement Directives and the Transatlantic Trade & Investment Partnership (T-TIP): Advancing U.S. – European Trade and Cooperation in Procurement*, forthcoming.

journalists, non-governmental organizations, users, etc. – are less effective in forcing transparency and professional standards at the operational level.(43) The monitoring of the entire procurement cycle by the unsuccessful tenderers, by social witnesses,(44) NGOs, the press, citizens, might cumulatively help assure correct performance, and might well create an incentive for proper conduct by officials and contractors during the award and execution of a contract.(45)

It is therefore vital that anti-corruption initiatives and procurement reform work more closely together. Within the EU legal framework the national implementation of the three new (2014) EU Directives on public procurement and concessions may represent a chance of the utmost importance to effectively enforce integrity in the public procurement process.(46)

Promoting professionalism and stressing the ethical requirements binding procurement officials inside complex organizations, such as central purchasing bodies, will be useful means of pursuing the financial and economic benefits of transparent, efficient and competitive procurement.(47) Efficient spending through good public procurement practices is a key lever to improve the quantity and quality of public entities activity.(48)

It seems that adopting anti-corruption laws and model procurement codes will only partially solve the problem. More focus should be placed on supporting the rules by norms such as accountability and integrity – in other words, the ideals of anti-corruption must be brought into the fabric of the procurement community.(49)

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(43) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 119, in which principle No. 10 provides that “Member countries should empower civil society organisations, media and the wider public to scrutinise public procurement. Governments should disclose public information on the key terms of major contracts to civil society organisations, media and the wider public. The reports of oversight institutions should also be made widely available to enhance public scrutiny. To complement these traditional accountability mechanisms, governments should consider involving representatives from civil society organisations and the wider public in monitoring high-value or complex procurements that entail significant risks of mismanagement and corruption”.

(44) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, 2013, cit., 84.

(45) R. HODESS, *Civil Society and Nongovernmental Organisations as International Actors in Anti-Corruption Advocacy*, 77-78; United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 26-27.

(46) Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC; Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC; Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts.

(47) See the chapter in this book: G. M. RACCA – R. CAVALLO PERIN, *Corruption as a Violation of Fundamental Rights: Reputation Risk as a Deterrent to the Lack of Loyalty*.

(48) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 22, concerning the healthcare spending.

(49) United Nations Office on Drugs and Crime – UNODC, *Guidebook on anti-corruption in Public Procurement and the management of public finances. Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 1-2.

This book aims to enter the fabric of the procurement community and through its chapters highlights how corruption can determine violations of fundamental rights and undermine the fiduciary relationship between citizens and public institutions. The discussion on the different models of procurement systems underlines the important issues on objective or subjective award criteria and how a correct choice of the best tenderer can assure the best use of public funds, provided that proper execution is monitored too.

While displaying a wide scope of application, the tools for fighting corruption are nonetheless limited by several features that hamper their potential to address the problem effectively. Transparency, efficiency and monitoring must be correctly addressed. Moreover, the risks of overregulating the procurement process are high, and overregulation leads to waste and litigation and can simply reinforce a failure in integrity. Improving the instruments to prevent collusion between the tenderers is a crucial issue too and requires special capacity. To this purpose, the need of professional capacity becomes evident, as the main source of waste in public procurement seems to be incompetence rather than corruption. Highly trained and diverse professionals are required to assure the quality of spending for the benefit of the citizens. Correctly addressed, forms of aggregation of the procurement and of networks between procurement agencies could assure the needed mix of professional skills required to use procurement as a strategic tool for public interest and economic development.

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## Applying OECD public procurement principles

BY

Paulo MAGINA

OECD, Senior Policy Analyst, Public Sector Integrity Division

Jeremy MCCRARY

OECD, Senior Policy Analyst, Public Sector Integrity Division

### ***1. Why Focus on Public Procurement: Background***

Public procurement accounts for 13% of GDP, on average, across OECD countries, which translates to approximately €4.3T annually. Given the size of public procurement, the financial stakes involved in cutting waste and fighting corruption are clear. As governments look to cut operational expenses, efficiency gains in procurement can help governments to “do more with less.” Additionally, citizens and businesses expect clean and effective procurement. In 2008, OECD countries adopted guidelines to enhance transparency, accountability and integrity in procurement in the *Recommendation on Enhancing Integrity in Public Procurement* (the *Recommendation*).

The principles set out in the *Recommendation* are anchored in four pillars: transparency, good management, prevention of misconduct, and accountability and control. Collectively, these pillars address governance in public procurement. The *Recommendation* also acknowledges that sound procurement rules alone are not sufficient to ensure good stewardship of public funds and avoid waste and corruption. Implementing such rules requires a wider governance framework that encompasses: an adequate institutional and administrative infrastructure; an effective review and accountability regime; mechanisms to identify and close off opportunities for corruption; and adequate human, financial and technological resources to support all of the elements of the system. This must all be supported by a sustained political commitment to apply these rules and regularly update them.

The *Recommendation* and the principles that it contains have played an influential role in shaping policy debate in OECD and partner countries. They have been used as a basis for dialogue between procurement officials and other policy communities, for instance, audit bodies, internal control staff and competition authorities. The *Recommendation* has been used as an international benchmark

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in the formulation and review of public procurement regulations and policies to provide options for reforms based on the experiences of other countries.

Leading OECD and G20 economies, including Brazil, Mexico and the United States have requested the OECD to provide peer reviews of their procurement systems. Countries such as Chile, Colombia, Estonia, Ireland and Mexico used the principles from the *Recommendation* in the drafting of new regulations and policies. In Chile the principles played a guiding role in the development of the 2009 Decree to enhance transparency in public procurement. They also supported the evaluation of existing public procurement laws or policies in Hungary, Italy, Norway and Turkey.

To help procurement officials put the principles set out in the *Recommendation* into practice at each stage of the public procurement cycle, a Checklist and an online Toolbox were developed.<sup>(1)</sup> These tools support public officials in developing guidance and procedures at various points throughout the procurement cycle based on identified good practices. They have also been used in the training of procurement officials, both within OECD countries and beyond, for instance in Belgium, Finland, Hungary, Ireland, Mexico, Norway, Portugal, Sweden, and Turkey, as well as Morocco.

In 2013, the OECD published a report, *Implementing the OECD Principles for Integrity in Public Procurement: Progress Since 2008*,<sup>(2)</sup> which surveys the progress made by countries in implementing the *Recommendation*. What follows is a condensed adaptation of this report, which identifies key areas through which procurement can promote value for money with integrity. These include consolidation and professionalization of the procurement function, and its identification as a strategic activity; introduction of systematic performance monitoring; integration of existing e-procurement systems; and development of monitoring mechanisms to supervise innovative forms of public service delivery, including public-private partnerships (PPPs), concessions and sponsorships.

## ***2. Six lessons learnt from the OECD Public Procurement Reviews(3)***

As mentioned above, the OECD has conducted independent assessments of the public procurement systems of a number of OECD and G20 countries, to benchmark with international good practice. The reviews have identified

(1) Available at: <http://www.oecd.org/corruption/ethics/enhancingintegrityinpublicprocurementchecklist.htm>, and <http://www.oecd.org/governance/procurement/toolbox/>.

(2) OECD, *Implementing the OECD Principles for Integrity in Public Procurement: Progress since 2008*, OECD Public Governance Reviews, available at <http://dx.doi.org/10.1787/9789264201385-en>, 2013.

(3) OECD, *Public procurement for sustainable and inclusive growth: Enabling reforms through evidence and peer reviews*. 2012, Paris, <http://www.oecd.org/gov/ethics/PublicProcurementRev9.pdf>.

a number of lessons that can help governments transform procurement into a strategic function while pursuing value for money across the whole project cycle. This section contains specific lessons learned in the course of country reviews, while the following sections will take a broader view regarding important features of public procurement systems.

1. *Moving away from strict compliance to a more managerial approach across the whole project cycle.*

Poor project planning and lack of monitoring of performance in contract management are common challenges among countries. Reviews identified ways to mitigate risks of waste and integrity throughout the procurement cycle, such as appropriate market research and consultation with potential suppliers.

2. *Ensuring a strategic position for the procurement function.*

In Mexico, the procurement function is still handled as an administrative service in support of technical areas in many organisations. As part of the review process, the Commission for Electricity (CFE) has taken the initiative to draw up an action plan, together with the OECD, to provide a roadmap for reform, transforming procurement into a strategic function which will contribute to CFE's objectives and priorities.

3. *Developing evidence to monitor the performance of the procurement system.*

The e-procurement system for federal public procurement in the United States brings together nine distinct systems to provide an integrated interface for users. The OECD peer review provided recommendations to help the United States federal government generate better quality data on procurement and promote performance analysis.

4. *Tapping into the potential of consolidation with a view to achieving efficiency gains.*

The Mexican Institute of Social Security (IMSS) procures a wide range of products and services through a highly decentralised procurement function. The OECD Review provided recommendations on centralisation of the purchase of medicines and increasing the use of reverse auctions in order to achieve efficiency gains, which have since been followed by IMSS.

5. *Investing in professionalisation.*

The government of Morocco has set up a specific procurement unit in the Treasury in order to equip the government with a team of procurement specialists, following an OECD Joint Learning Study of Morocco.

6. *Keeping control of the use of exceptions to competitive tendering (e.g. for reasons of extreme urgency).*

In Brazil, the extensive use of exemptions and below-threshold procurements suggested that the government was not leveraging its bulk purchasing

power. The OECD Review recommended controlling more strictly the use of these exceptions and reforming the complaint system to avoid undue pressure from the private sector.

As evidenced by these examples, OECD reviews help policy makers improve policies, adopt good practices and implement established principles and standards. They provide an assessment of a country's or an entity's procurement system by peers working in administrations in OECD countries as well as concrete proposals to improve policies and practices in line with international good practice. OECD reviews also provide a platform for developing stakeholder consensus on reform agendas to facilitate their implementation.

### *3. Reforming the Whole Procurement Cycle*

In addition to the lessons learned from OECD reviews, broader trends in public procurement can be identified over time. Reform efforts are often focused only on the tendering phase, when tenders from suppliers are solicited and evaluated. While enforcing integrity and implementing good practices in the award of contracts is critical to a successful procurement system, the lack of attention dedicated to risks in the needs assessment and contract management phases was recognised as a key concern in the *Recommendation*.

In response, by 2012, a number of countries had introduced reforms that address the whole public procurement cycle, from the needs assessment throughout the award and contract management. Examples of such measures include:

- *Using new technologies to enhance transparency in the whole procurement cycle:* Compranet, the e-procurement system used by the public administration at the federal level in Mexico, supports back-office integration among procurement, budget and accounting information management systems as well as enhances transparency in government operations.
- *Strengthening the management of contracts, especially for non-competitive tendering procedures:* In the United States, the President issued a memorandum at the beginning of his term in March 2009 instructing agencies to review high-risk contracting methods and to strengthen the management and oversight of these contracts in order to reduce wasteful spending.
- *Improving access to information on sub-contractors:* In Australia, the Commonwealth Procurement Guidelines were revised to ensure that

agencies make available, upon request, the names of any sub-contractor engaged by a contractor in respect of a procurement contract.

- *Recourse before and after the contract signature:* Ordonnance n. 2009-515 in France enables a judge to intervene not only before but also after the contract signature while making the recourse suspensive.
- *Limiting the modifications of public contracts after award:* The Spanish Law on Public Sector Procurement was amended in 2011 to limit the capacity to modify contracts after they have been awarded.
- *Managing risks to integrity in the whole procurement cycle:* In Italy, reform L. 136/2010 provides measures to trace out all the financial flows in public administrations in order to help prevent corruption in public procurement.

Despite this progress made since 2008, work is still necessary in many countries to reform the pre-tendering phase. To maximise value for money in complex procurements, it is essential to understand whole life-cycle costs of owning and operating equipment being purchased. If bid criteria do not take into account total ownership costs, this can skew results away from the most effective solution. Moreover, incorporating total life-cycle cost in the bid criteria is an effective way to promote environmental protection through procurement. Additional common risks identified in the needs assessment phase include:

- failure to budget realistically;
- misalignment of procurement with overall public investment; and,
- interference in the decision to procure or informal agreements on contracts. For instance, when assessing whether a new road or airport is needed, political considerations may prevail.

Similarly, more progress is necessary in the contract management phase. Once the contract has been awarded, waste and corruption can take place if there is no sound system to monitor the progress of work and ensure that the contractor performs its tasks. Common risks identified in OECD countries include: failure to monitor a contractor's performance, in particular lack of supervision over the quality and timing of the process; subcontractors chosen in a non-transparent way or not being kept accountable; deficient separation of duties with the risk of false accounting or late payment. For example, the OECD review of the public procurement system in the United States highlighted that in the 1990s, commercial pressure to buy at best value led to a resource shift away from contract management and potential over-reliance on private sector contractors. Also, one of the risks in contract management is the use of extensions of public contracts, which may restrict the possibility for new firms to compete for the additional work.

Despite the risks involved in the contract management phase (e.g. change in the price of the contract, the use of subcontractors and intermediaries to hide corrupt transactions, etc.), few countries have taken active steps to supervise contractors' performance and integrity, which is left at the discretion of the contracting authority on a case-to-case basis. Many countries report that the following measures are not necessarily or not always required:

- monitoring a contractor's performance against pre-specified targets;
- regularly organising inspection of work in progress;
- conducting random sample checks;
- monitoring progress of contract and payment through electronic systems;
- third-party scrutiny of high-value or high-risk contracts;
- testing the product, system or results in the real world before the delivery of the work.

Finally, the level of transparency is often limited in the contract management phase. Few countries publish information about events that occur post-award. Information on the justification for awarding contracts is available in 13 OECD countries, contract modifications are publicised in 11 countries and only 6 countries provide information that allows the tracking of procurement spending. One solution, especially in times of constrained resources, is reliance on stakeholders to provide third-party scrutiny of high-value or high-risk contracts, including during contract management. For instance, social witnesses in Mexico play a vital role in scrutinising the integrity and efficiency of the procurement cycle by providing proposals for improving the processes in place.

#### ***4. A Strategic Role for Public Procurement***

Public procurement is organised as an administrative, rather than a strategic function in many OECD countries. Ultimately it is essential that governments verify that the objectives of procurement are achieved, whether these are value for money or other objectives such as sustainable development, international trade, or innovation. Providing a strategic role for procurement, and providing institutions that support such a role, will help ensure that the objectives of procurement are met while also addressing many of the concerns outlined above.

##### **Innovation as an Example**

The potential of public procurement to support innovation was highlighted in the OECD Strategy on Innovation. Procurement is one instrument that many governments use to unleash innovation, to complement getting prices

right, opening markets for competition and devising innovation-inducing standards and smart regulations. In particular:

- procurement practices can foster innovation in markets by investing in sectors where government is a significant purchaser, such as health or defence;
- governments can influence private purchasing, which has potentially a much larger impact – for instance, by being early or lead users of innovations, investing in pre-commercial innovations and creating new markets.

Almost all OECD countries use public procurement as an instrument to support innovation. Their primary objectives are, in order of reported importance:

- ensuring a level playing field for innovative companies, in particular for SMEs or disadvantaged communities;
- driving green product innovation, notably through the development of energy-efficient clothes dryers, office copiers, computers and lighting;
- providing innovative goods and services for the government;
- developing lead markets, although this requires reaching a critical mass to be effective; and, more generally,
- promoting competitiveness in the economy.

### Data

Supporting the strategic role for public procurement requires the development of an evidence-based approach to monitor the performance of the system and make sure that the objectives are achieved – whether they are value for money or broader policy objectives.

Few countries analyse public procurement to support systemic improvement. Although most countries collect basic data on a regular basis on the number of bids, contract awards and the use of open vs. non-competitive procedures, few countries actually make a systematic analysis of this information.

State audit offices, internal control mechanisms and procurement oversight bodies are also important sources of procurement data analyses. For instance, the General Accountability Office in the United States examines contracts that are awarded non-competitively on a regular basis. A system designed to cross-check data from various sources against each other could be effective. One example is the Public Spending Observatory in Brazil, which compares procurement expenditure data with other sources to identify atypical situations that warrant further examination.

Because most countries do not invest in analysing procurement data in a systemic manner, they do not have a full appreciation of complex policy challenges: the likely benefits, costs and effects of their decisions. Because the key to evidence-based policy making is using knowledge produced through data and analysis, the OECD is working to develop a set of key procurement indicators to measure performance over time, and track systemic improvement.

### Capacity

Implementation of a strategic role for public procurement requires procurement officials that meet high standards of knowledge, skills, and integrity. Procurement officials are expected to comply with increasingly complex rules and pursue value for money, while also taking into account economic, social and environmental considerations. Countries report that procurement officials are facing the following challenges:

- understanding the increasing complexity of public procurement rules;
- facing conflicting objectives when using procurement to support broader policy objectives such as socio-economic and environmental goals;
- lacking guidance on how to take into account environmental criteria in public procurement; and,
- keeping abreast of developments of e-procurement systems and ensuring their effective implementation.

For these reasons, improving the knowledge and skills of the procurement workforce has been identified as a primary area for improvement. Where possible, a systematic approach to learning and development for procurement officials should be used to build and update knowledge and skills.

## 5. Conclusion

As a major economic activity of any government, public procurement must be conducted with integrity, efficiency, and professionalism. For over a decade, the OECD has supported governments in reforming their public procurement systems to ensure long-term sustainable and inclusive trust by providing international standards on public procurement; undertaking hands-on peer reviews that provide an assessment of the public procurement systems, either national or sectorial; bringing together a community of practice on procurement to shape directions for future reforms; organising policy dialogue on the co-operation between government and the private sector in the framework of the G20; and collecting evidence across OECD countries on the performance of procurement operations as well as the impact of procurement on broader public policy objectives.

To reflect progress in the transformation of procurement as an instrument to support strategic government objectives, the OECD is undertaking to apply this experience in revising and updating the principles as set out in the *Recommendation*. These updates will recognize that, when integrated strategically in law and practice, a sound procurement system must encompass the entire procurement cycle, and involves: a) procurement rules and procedures that are simple, clear and ensure access to procurement opportunities; b) effective institutions to conduct procurement procedures and conclude, manage and monitor public contracts; c) appropriate electronic tools; d) suitable and trained human resources to plan and carry out procurements; and e) competent contract management.



**PART I**

**Corruption as a Violation  
of Fundamental Rights**

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**CHAPTER 1**  
**Corruption as a violation of fundamental rights:  
reputation risk as a deterrent against the lack of loyalty**

BY

Gabiella M. RACCA

Professor of Administrative Law, University of Turin

Roberto CAVALLO PERIN

Professor of Administrative Law, University of Turin

**1. Introduction**

It is a commonly shared view that poor integrity undermines the main objectives of private and public activities and distracts from their main goals.<sup>(1)</sup> The lack of integrity affects human rights<sup>(2)</sup> and is even more unacceptable and serious when perpetrated by public authorities. In that event, corruption erodes the pillars of democracy. People's representatives are all too often captured by non-transparent economic interests and divert the pursuit of public and citizens'

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(1) S. ROSE-ACKERMAN, *Corruption and conflicts of interest*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, Edward Elgar Publishing, 2014, 5-10; G. SWEENEY, *Linking acts of corruption with specific human rights*, in *Corruption and human rights in third countries*, Workshop of the European Parliament, 28 February 2013, available at <http://bookshop.europa.eu/>, 8. OECD, *Investing in Trust: Leveraging Institutions For Inclusive Policy Making*, Background Paper of the conference *Restoring Trust in Government: Addressing Money and Influence in Public Decision Making*, Paris 14-15 November 2013, available at <http://www.oecd.org/gov/ethics/Investing-in-trust.pdf>, 2013, 2. "A policy making process conducive to trust (i) secures the inclusiveness of the information available to decision makers, to ensure adequate participation of all actors with a stake in the policy problem at hand; (ii) safeguards the public interest and avoids capture, while effectively aggregating competing, but often legitimate interests; and (iii) is aligned with broader principles and high standards of behaviour".

(2) Council of Europe, Civil Law Convention on Corruption, Art. 13, signed on 4 November 1999, entered into force on 1 November 2003, Preamble, § 4, "corruption represents a major threat to the rule of law, democracy and human rights, fairness and social justice, hinders economic development and endangers the proper and fair functioning of market economies"; Council of Europe, Criminal Law Convention on Corruption, signed on 27 January 1999, entered into force on 1 July 2002, Preamble, § 5, "corruption threatens the rule of law, democracy and human rights, undermines good governance, fairness and social justice, distorts competition, hinders economic development and endangers the stability of democratic institutions and the moral foundations of society". International Council on Human Rights Policy, *Corruption and Human Rights: Making the connection*, 2009, available at [http://www.ichrp.org/files/reports/40/131\\_web.pdf](http://www.ichrp.org/files/reports/40/131_web.pdf). The report highlights the links between acts of corruption and violations of rights. See also: OECD, *Recommendation of the Council on Enhancing Integrity in Public Procurement*, C(2008)105, 2008, available at <http://acts.oecd.org/>, "the Recommendation provides policy makers with Principles for enhancing integrity throughout the entire public procurement cycle, taking into account international laws, as well as national laws and organisational structures of Member countries".

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interests.(3) Illegal behavior buys the loyalty that politicians should have towards citizens, and captures the independent exercise of sovereignty for the benefit of maintaining privileges among the corrupt. Corruption in the public procurement sector represents an emblematic case of such diversion.

## **2. The lack of integrity as a violation of fundamental rights**

The corruption of politicians is particularly serious since it becomes pervasive and widespread in both public and private sector activities. Political corruption may influence legislation, its implementation, the public officials involved, competition in the relevant market, and, in the end, fairness and the economic growth of business organizations. It undermines the fundamental rights of the citizens.(4) Corruption undermines a variety of human rights.(5)

The relationship of trust between citizens and the Government is threatened as corruption leads to gains for political parties or interest groups, and undermines public interests and the quality of spending.(6) A ‘crisis of

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(3) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, 6. Around three quarters of Europeans (73 %) say that bribery and the use of connections is often the easiest way of obtaining certain public services in their country. Similarly, to 2011, around two in three Europeans (67 %) think the financing of political parties is not sufficiently transparent and supervised. See also the Eurobarometer in <http://ec.europa.eu/>.

(4) International council on Human Rights Policy, *Corruption and Human Rights: Making the connection*, cit., 9 et seq. “While corruption violates the rights of all those affected by it, it has a disproportionate impact on people that belong to groups that are exposed to particular risks (such as minorities, indigenous peoples, migrant workers, disabled people, those with HIV/AIDS, refugees, prisoners and those who are poor). It also disproportionately affects women and children. Those who commit corrupt acts will attempt to protect themselves from detection and maintain their positions of power. In doing so, they are likely to further oppress people who are not in positions of power, including most members of the groups listed above. The latter tend both to be more exploited, and less able to defend themselves: in this sense, corruption reinforces their exclusion and the discrimination to which they are exposed”.

(5) As posited by S. ROSE-ACKERMAN, *International Actors and the Promises and Pitfalls of Anti-Corruption Reform*, in *Pennsylvania Journal of International Law*, 2013, 449, who noted that corruption can undermine human rights but should not be treated as a per se human rights violation, and refers to J. DUGARD, *Corruption: Is there a Need for a New Convention?*, in S. R. Ackerman – P. Carrington (ed. by) *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, Carolina Academic Press, 2013, 159; C. RAJ KUMAR, *Corruption and Human Rights in India. Comparative Perspectives on Transparency and Good Governance*, Oxford University Press, 2011.

(6) S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform*, Cambridge, 1999, 30 et seq. on the relationships among corruption and political organizations, as “democratic election are not invariably a cure for corruption” (128 et seq.); Id. *Political corruption and democratic structures*, in A. K. Jain (ed. by) *The Political Economy of Corruption*, London, 2001, 35 et seq.; B. G. MATTARELLA, *Le regole dell’onestà*, Bologna, 2007, 25 et seq.; Id., *The conflicts of interests of public officers: Rules, checks and penalties*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 30-31. See also: OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, 2013, available at <http://www.oecd-ilibrary.org/>, 24 et seq. See also: OECD, *OECD Principles for Integrity in Public Procurement*, 2009, available at <http://www.oecd.org/gov/ethics/48994520.pdf>. EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, in <http://ec.europa.eu/dgs/home-affairs/what-we-do/policies/>

trust'(7) is growing and new strategies and measures are required to tackle it.(8)

A basic distinction has recently been drawn between cases where politicians make decisions based on their discretionary power, and intermediation of favours which typically includes the transgression of laws and regulations.(9) Lawmakers and governments shape laws and regulations concerning economic activities, taking into account the demands and interests of campaign donors, as well as those of lobbyists, public opinion, guidelines from political parties and their own convictions.(10) In the second case, "elected officeholders use their influence on civil service to arrange for donors to earn contracts, get access to public loans or earn other benefits. This involves undue political influence on public service and unlawful behaviour of public servants involved in public procurement, licensing, permissions or other areas where companies expect illegal favours in return for campaign donations".(11)

All possible links between politicians, members of a Government and public officials can be affected by corruption. Each of them may have a distorted relationship with economic operators interested in public procurement.(12) Moreover, corrupt relationships among undertakings can trigger collusion to the detriment of public interest, collusion, of which public officials are often unaware. Nor is corruption purely "criminal" in the commonly understood sense: it has been estimated that, for 80% of the time, waste in public

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*organized-crime-and-human-trafficking/corruption/anti-corruption-report/docs/2014\_acr\_france\_chapter\_en.pdf*, 8 "Provoked by the crisis, social protests have targeted not only economic and social policies, but also the integrity and accountability of political elites. High-profile scandals associated with corruption, misuse of public funds or unethical behavior by politicians have contributed to public discontent and mistrust of the political system".

(7) EU Commission, *France annex to the Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report, cit.*, 2014, 2.

(8) EU Commission, Report from the Commission to the Council and the European Parliament, *EU Anti-Corruption Report*, COM(2014) 38 final, 8. Measures such as: limiting presidential immunity, strengthening the rules on financing of political parties and electoral campaigns, restricting multiple office – holding by politicians, and developing a strategy to prevent conflicts of interest, as provided in the Jospin committee set up in France in July 2012 to prepare a reform on ethical standards in public life.

(9) OECD, *Money in Politics: Sound Political Competition and Trust in Government*, Background Paper of the conference *Restoring Trust in Government: Addressing Money and Influence in Public Decision Making*, Paris 14-15 November 2013, available at <http://www.oecd.org/gov/ethics/Money-in-politics.pdf>, 18.

(10) G. HOUILLOIN, *Corruption and conflict of interest: Future prospects on lobbying*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 53 et seq.

(11) OECD, *Money in Politics: Sound Political Competition and Trust in Government*, Background Paper of the conference *Restoring Trust in Government: Addressing Money and Influence in Public Decision Making*, Paris 14-15 November 2013, cit., 18.

(12) Y. LENGWILER – E. WOLFSTETTER, *Corruption in procurement auctions*, in N. Dmitri – G. Piga – G. Spagnolo (ed. by) *Handbook of Procurement*, Cambridge, 2006, 412 et seq. See also: OECD policy roundtables, *Collusion and Corruption in Public Procurement*, 2010, available at <http://www.oecd.org/competition/cartels/46235884.pdf>.

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procurement could be traced to incompetence, and to classic criminal corruption for the remaining 20% of the time.(13)

Informational asymmetries among all stakeholders involved in a procurement system provide opportunities for corrupt practices.(14) The allocation of public resources in the public interest through public contracts and procurement functions provides a large number of opportunities for corruption.(15) The waste of public funds is mainly related to cost overruns, delays of implementation and the loss of effectiveness (including inferior quality and questionable usefulness).(16)

All procurement systems include resources to be allocated by public authorities, and thus hold an evident political function. The ‘desiderata’(17) of a procurement system are well-known: competition; integrity; transparency; efficiency; customer satisfaction; best value; wealth distribution; risk avoidance; and uniformity. Public resources should be allocated by public authorities in the best possible way, by proactive and ethical procurement officials aiming at the highest satisfaction of citizens’ needs, and through private organizations that consider it an honor to serve public bodies and to provide the best performance in a transparent, efficient and competitive procurement system. However, as is known, each facet of such relationships between the stakeholders in a procurement system can be distorted towards different goals. The fundamental rights of citizens fall behind all other interests, and are betrayed.(18)

(13) O. BANDIERA – A. PRAT – T. VALLETTI *Active and passive waste in government spending: Evidence from a policy experiment*, *American Economic Review*, 2009, 1278-1308.

(14) P. TREPTE, *Regulating Procurement. Understanding the Ends and Means of Public Procurement Regulation*, Oxford, Oxford University Press; ID., *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Procurement: Possibilities and Limitations*, in OECD Expert Group Meeting on Integrity in Public Procurement, Château de la Muette, Paris, 20 and 21 June 2005, in [https://bvc.cgu.gov.br/bitstream/123456789/3500/1/transparency\\_and\\_accountability\\_tools.pdf](https://bvc.cgu.gov.br/bitstream/123456789/3500/1/transparency_and_accountability_tools.pdf); OECD, *Recommendation on Enhancing Integrity in Public Procurement*, 2008, in <http://www.oecd.org/corruption/keyocedanti-corruptiondocuments.htm>, 38. See also: Transparency International, *Corruption and Human Rights: Making the Connection*, 2009, in [http://www.ichrp.org/files/reports/40/131\\_web.pdf](http://www.ichrp.org/files/reports/40/131_web.pdf); C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, in *PCLJ*, Vol. 40, No. 1, 2010, 63, the article is available also at [www.ssrn.com](http://www.ssrn.com).

(15) For an analysis of the different forms of corruption see: United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, 2013, available at [https://www.unodc.org/documents/corruption/Publications/2013/Guidebook\\_on\\_anti-corruption\\_in\\_public\\_procurement\\_and\\_the\\_management\\_of\\_public\\_finances.pdf](https://www.unodc.org/documents/corruption/Publications/2013/Guidebook_on_anti-corruption_in_public_procurement_and_the_management_of_public_finances.pdf), 4 et seq.

(16) Moreover the highest direct public losses concerns corrupt training projects (44% of budget volume lost in projects affected, 29% in urban/utility construction, 20% in road & rail, 16% in water & waste and 5% in Research & Development), PricewaterhouseCoopers study prepared for the European Anti-Fraud office (OLAF), *Identifying and Reducing Corruption in Public Procurement in the EU*, 2013, available at [http://ec.europa.eu/anti\\_fraud/](http://ec.europa.eu/anti_fraud/), 174 et seq.

(17) S. L. SCHOONER, *Desiderata: Objectives for a System of Government Contract Law*, in *PPLR*, 2002, 103 et seq., where the author introduces nine goals frequently identified for government procurement systems: (1) competition; (2) integrity; (3) transparency; (4) efficiency; (5) customer satisfaction; (6) best value; (7) wealth distribution; (8) risk avoidance; and (9) uniformity.

(18) T. SØREIDE, *Democracy’s shortcomings in anti-corruption*, in *www.u4.no*, 2012.

Stakeholders may be kept unaware of such distortions due to a lack of transparency, information asymmetries, or undeveloped competence.<sup>(19)</sup> A number of factors that encourage corruption in the public procurement sector have been pointed out: political rent-seeking, commercial usage, culture, state of market development, low pay of procurement officials and low capacity.<sup>(20)</sup>

A cumbersome set of procurement rules approved by citizens' representatives may restrict competitions among economic operators or prevent others from participating in the award procedures. Inadequate internal and external audits may favor certain special interests. A lack of accountability in procurement officials permits the waste of public funds, in either the selection or the execution of a public contract.<sup>(21)</sup>

## 2.1. Social, political, economic solidarity

A pillar of anticorruption should be the value that holds citizens together in any legal system, from the national to the European<sup>(22)</sup> level and, from a different perspective, also in international relationships. The value of solidarity should exclude any tolerance for corruption, as corruption undermines the common recognition of fundamental rights.<sup>(23)</sup>

(19) EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, 2013, in <http://bookshop.europa.eu/>, on the problem of political and other forms of corruption in public procurement in the European Union. It identifies weaknesses in all the stages of the public procurement cycle, allowing corruption to undermine the objectives of integrity and value for money and eventually jeopardise the whole EU internal market policy. The document recommends that Member States strengthen national public administration arrangements and implement effective anti-corruption tools covering transparency, accountability and professionalism in public procurement.

(20) International Council on Human Rights Policy – Transparency International, *Integrating Human Rights in the Anti-corruption Agenda. Challenges, Possibilities and Opportunities*, 2010, available at [http://www.ichrp.org/files/reports/58/131b\\_report.pdf](http://www.ichrp.org/files/reports/58/131b_report.pdf), 43; J. G. LAMBSDORFF, *Causes and consequences of corruption: What do we know from a cross-section of countries?*, in S. Rose-Ackerman (ed. by) *International Handbook of the Economics of Corruption*, Cheltenham, 2006, 4 et seq., where are identified nine possible causes of corruption in public sector: the size of the public sector, the quality of regulation, the degree of economic competition, the structure of Government, the amount of decentralization, the impact of culture, values and gender, and the role of invariant features such as geography and history. A. MILLS, *Causes of corruption in public sector institutions and its impact on development*, 2012, available at <http://unpan1.un.org/intradoc/groups/public/documents/un-dpadm/unpan049589.pdf>, 7 et seq.

(21) Transparency International, *The Anti-Corruption Plan Language Guide*, 2009, 44 et seq.; International Council on Human Rights Policy – Transparency International, *Integrating Human Rights in the Anti-corruption Agenda. Challenges, Possibilities and Opportunities*, cit., 14 and 26.

(22) E.g. Council Decision 2007/252/EC of 19 April 2007, establishing for the period 2007-2013 the specific programme “Fundamental rights and citizenship” as part of the general programme “Fundamental Rights and Justice”.

(23) R. HODESS, *Civil Society and Nongovernmental Organisations as International Actors in Anti-Corruption Advocacy*, in S. Rose-Ackerman – P. Carrington (eds.) *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, Carolina Academic Press, 2013, 75 et seq., where it is posited that to build a “virtuous circle” three elements are needed: accountability, trust and coalitions.

Indeed, as has already been established, a community of values should grow in the wider context of transnational and international bodies such as the UN, the Council of Europe and EU Member States, all to buttress a joint system of fundamental rights protection.(24)

Unfortunately, at the EU level, corruption remains one of the biggest challenges for all societies, harming the EU as a whole by lowering investment levels, hampering the fair operation of the Internal Market and wasting public resources. It is estimated that the economic costs incurred as a result of corruption in the EU amount to around EUR 120 billion per year.(25) This constitutes one percent of the EU GDP, representing only a little less than the EU's annual budget.(26) Four out of five EU citizens regard corruption as a major problem in their State.(27) Transparency International estimates that "systematic corruption can add at least 20-25% to the cost of government procurement."(28)

A firm political commitment is required to restore trust in the effectiveness of anti-corruption policies.(29) The European Union (EU) has a general right to act in the field of anti-corruption policies,(30) within the limits established

(24) As was presented in detail in the Focus of EU Agency for Fundamental Rights (FRA)'s 2011 Annual report available at: [http://fra.europa.eu/sites/default/files/fra\\_uploads/2211-FRA-2012\\_Annual-Report-2011\\_EN.pdf](http://fra.europa.eu/sites/default/files/fra_uploads/2211-FRA-2012_Annual-Report-2011_EN.pdf); see: UN, *Guidebook on anti-corruption in public procurement and the management of public finances*, 2013, available at [www.unodc.org](http://www.unodc.org). See also: T. SØREIDE – R. TRUOX, *Collaboration against corruption?: Multistakeholder groups in natural resource management*, in *www.u4.no*, 2011; C. MCCRUDDEN, *Buying Social Justice. Equality, government Procurement, & Legal Change*, Oxford, 2007, 90 et seq. S. ROSE-ACKERMAN, *Introduction: The Role of International Actors in Fighting Corruption*, in S. ROSE-ACKERMAN – P. Carrington (ed. by) *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, cit., 3.

(25) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 2013, 78. OECD, *CleanGovBiz, Integrity in Practice*, 2013 available at <http://www.oecd.org/cleangovbiz/49693613.pdf>, according to the World Bank, the document reported that corruption represents 5 % of global GDP (USD 2.6 trillion), with over USD 1 trillion paid in bribes each year; corruption adds up to 10 % of the total cost of doing business on a global basis and 25 % of the cost of procurement contracts in developing countries.

(26) EU Home Affairs Department, data available at the home page of DG Home affairs: [http://ec.europa.eu/dgs/home-affairs/what-we-do/agencies/index\\_en.htm](http://ec.europa.eu/dgs/home-affairs/what-we-do/agencies/index_en.htm).

(27) EU Commission, *Fighting corruption in the EU*, 6 June 2011, COM (2011) 308 final, in <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52011DC0308:EN:NOT>, 3.

(28) International Council on Human Rights Policy – Transparency International, *Integrating Human Rights in the Anti-corruption Agenda. Challenges, Possibilities and Opportunities*, cit., 43.

(29) S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform*, Cambridge, 1999, 143 et seq., concerning the form of control of the political power. EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, cit., 40.

(30) EU Commission, *Consultation on a future reporting and monitoring mechanism on EU Member states progress on fighting corruption*, in [http://ec.europa.eu/home-affairs/news/consulting\\_public\\_consulting\\_0007\\_en.htm](http://ec.europa.eu/home-affairs/news/consulting_public_consulting_0007_en.htm). In the EU, corruption has been on the agenda since the mid-1990s. Although the focus on it has been sharpened by the two latest waves of enlargement, its effects have been identified across the Union to the extent that the European Commission concludes that "within the EU there is no corruption free-zone."

by the Treaty on the Functioning of the European Union.<sup>(31)</sup> In particular, the EU should ensure a high level of security, including through the prevention and combating of crime.<sup>(32)</sup> Indeed, corruption is one of the most serious crimes with a cross-border dimension. Moreover, it is often linked to other forms of serious crime, such as the trafficking of drugs and human beings, and cannot be adequately addressed by EU Member States alone.<sup>(33)</sup> The recent EU Anti-Corruption Report<sup>(34)</sup> confirms that this objective “cannot be sufficiently achieved by the Member States”<sup>(35)</sup> and will require an intervention at the Union level.<sup>(36)</sup>

(31) Treaty on the Functioning of the European Union, Art. 83, § 1. “The European Parliament and the Council may, by means of directives adopted in accordance with the ordinary legislative procedure, establish minimum rules concerning the definition of criminal offences and sanctions in the areas of particularly serious crime with a cross-border dimension resulting from the nature or impact of such offences or from a special need to combat them on a common basis. These areas of crime are the following: terrorism, trafficking in human beings and sexual exploitation of women and children, illicit drug trafficking, illicit arms trafficking, money laundering, corruption, counterfeiting of means of payment, computer crime and organised crime”. Council of the EU – General Secretariat, *The Lisbon Treaty’s impact on the Justice and Home Affairs (JHA) Council: More co-decision and new working structures*, December 2009, available at [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/111615.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/111615.pdf); C. DI DAMIAN – D. GARETH -G. MONTI, *European Union Law: Cases and Materials*, Cambridge, 2010, 581 et seq.

(32) The EU established its own instruments to tackle corruption as the two conventions on the protection of the European Communities’ financial interests and the fight against corruption involving officials of the European Communities or officials of the EU Member States and the European Anti-Fraud Office (OLAF), set up in 1999, which has interinstitutional investigative powers. The first call for action was in 1997 (see: EU Commission, *Action programme on organised crime calls for a comprehensive anti-corruption policy based on preventive measures*, 1997, see: [http://europa.eu/legislation\\_summaries/fight\\_against\\_fraud/fight\\_against\\_corruption/l33301\\_en.htm](http://europa.eu/legislation_summaries/fight_against_fraud/fight_against_corruption/l33301_en.htm)) followed by a 2003 Commission Communication on “a comprehensive anti-corruption policy” (see: EU Commission, *Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee on a Comprehensive EU Policy Against Corruption*, COM(2003) 317 final, May 28, 2003) and by the 2003 Framework Decision on combating corruption in the private sector since it introduced criminal liabilities for legal persons (EU Council, *Council Framework Decision on combating corruption in the private sector*, 2003/568/JHA, 22 July 2003).

(33) EU Commission, *Fighting corruption in the EU*, cit. See also EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, cit., 36-38. See also: J. DUGARD, *Corruption: Is there a Need for a New Convention?*, in S. Rose-Ackerman – P. Carrington (ed. by) *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, cit., 159 et seq. In the same book see also: K. E. DAVIS, *Does the Globalization of Anti-Corruption Law Help Developing countries?*, 169 et seq.

(34) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 3 February 2014, 24, where is reported that “the proposal also included the setting up of oversight monitoring of the implementation of public procurement rules, red flagging and alert systems to detect fraud and corruption. However, Member States raised fundamental objections to such measures which were considered too cumbersome for their administrations.”

(35) Treaty of the European Union, Art. 5, § 3: “Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level. The institutions of the Union shall apply the principle of subsidiarity as laid down in the Protocol on the application of the principles of subsidiarity and proportionality.”

(36) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 2. Concerning the relationship between the corruption prevention and public procurement infringements see 23 et seq.

A lack of integrity, either in public institutions or in private markets, undermines fundamental rights. First, it causes a waste of scarce resources and undermines the trust and effectiveness of public powers.<sup>(37)</sup> Moreover, tolerance of corruption distorts all the rules of civil society and the quality of services provided to citizens.<sup>(38)</sup>

The current widespread socio-economic crisis requires us to identify shared values in order to cope with the new challenges.<sup>(39)</sup> The urgent need for resources provides an extraordinary incentive to ensure accountability in public authorities, and to improve social controls over the quality of public spending.

As a result of citizens' growing consciousness of their social rights, there is a greater demand for inclusiveness and opportunities for social mobility. Such citizens may mobilize pressures to establish more open and transparent governments, or for an increase in service provision standards.<sup>(40)</sup> The urge to gain clear data on the quality of public spending, for better assessments and consequently better policies, is evident. Demands for quality services can be expected to grow faster and faster, and to require improvements despite the economic crisis.

Public spending in procurement could significantly improve citizens' quality of life, affecting all the sectors of services.<sup>(41)</sup> In the procurement sector, information tools make it possible to gather data on prices, and disparate higher prices covering bribes should not be tolerated.<sup>(42)</sup> Two factors converge: the need for quality in spending; and the potential of information technologies to overcome the obscurity of paper documents in historically impenetrable archives.

Civil society has a key role to play in fighting corruption, from monitoring public procurement and services to denouncing bribery and raising

(37) Concerning social sectors see: S. GUPTA – H. DAVOODI – E. TIONGSON, *Corruption and the provision of health care and education services*, in A. K. Jain (ed. by) *The Political Economy of Corruption*, London, 2001, 111 et seq. See also: International Council on Human Rights Policy – Transparency International, *Integrating Human Rights in the Anti-corruption Agenda. Challenges, Possibilities and Opportunities*, cit., 43-45.

(38) Concerning the policy for “zero tolerance” on corruption see: PricewaterhouseCoopers study prepared for the European Anti-Fraud office (OLAF), *Identifying and Reducing Corruption in Public Procurement in the EU*, 2013, cit., 318.

(39) EU Agency for Fundamental Rights (FRA), *Fundamental rights: challenges and achievements in 2012*, 2013, available at <http://fra.europa.eu/en/press-release/2013/eu-agency-fundamental-rights-fra-presents-its-annual-report>, 12 et seq.

(40) OECD, *Perspectives on Global Development 2012 Social Cohesion in a Shifting World*, 14 December 2011, in <http://www.oecd.org/site/devpgd2012/>.

(41) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 53 et seq. and 101 et seq.

(42) G. M. RACCA, *The Electronic Award and Execution of Public Procurement*, in *Ius Publicum Network Review*, 2012, available at <http://www.ius-publicum.com/pagina.php?lang=it&pag=articoli>, 6. See also: ID., *The role of IT solutions in the award and execution of public procurement below threshold and list B services: overcoming e-barriers*, in D. Dragos – R. Caranta (eds. by) *Outside the EU Procurement Directives – Inside the Treaty?*, Djøf, Copenhagen, 2012, 373-395.

awareness of the risks of wasting public money. As representatives of the general public, civil society organizations should investigate and bring to light cases of corruption. In this context, new technologies and social media can be used to gather information and publicly hold governments and public entities to account.(43)

## 2.2. Securing Fundamental Rights in the EU

According to the Preamble of the EU Charter of Fundamental Rights, “the Union is founded on the indivisible, universal values of human dignity, freedom, equality and solidarity; it is based on the principles of democracy and the rule of law. It places the individual at the heart of its activities, by establishing the citizenship of the Union and by creating an area of freedom, security and justice”.

Within the EU, it is possible to make a distinction between a wider set of values that address areas falling outside the EU scope,(44) an inner set of fundamental rights obligations imposed on and by the EU,(45) and socio-economic rights (especially Title IV ‘Solidarity’ of the Charter of Fundamental Rights of the European Union). These values all overlap with national social rights, and fundamental rights form part of the founding values in Article 2 TEU. However, the level of compliance with these rights appears to differ.

Amsterdam Treaty and Lisbon Treaty primary law explicitly provides for an EU “founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the

(43) Clean gov biz, *Boosting Integrity fighting corruption*, 2013, available at: <http://www.oecd.org/daf/anti-bribery/50350066.pdf>.

(44) Treaty on European Union (TEU), Art. 2. The ECJ has interpreted this more widely as referring to situations that are “covered by European Union law”. See: European Court of Justice, 15 November 2011, *Murat Dereci and Others v. Bundesministerium für Inneres*, in C-256/11, par. 72 and European Court of Justice, 26 February 2013, *Åklagaren v. Hans Åkerberg Fransson*, in C-617/10, par. 18. EU Commission, *2012 Report on the application of the EU Charter of Fundamental Rights*, COM(2013) 271 final, 8 May 2013, available at: [http://ec.europa.eu/justice/fundamental-rights/files/charter\\_report\\_2012\\_en.pdf](http://ec.europa.eu/justice/fundamental-rights/files/charter_report_2012_en.pdf).

(45) Treaty on European Union (TEU), Art. 6, where it is stated that “the Union recognises the rights, freedoms and principles set out in the Charter of Fundamental Rights of the European Union of 7 December 2000, as adapted at Strasbourg, on 12 December 2007, which shall have the same legal value as the Treaties. The provisions of the Charter shall not extend in any way the competences of the Union as defined in the Treaties. The rights, freedoms and principles in the Charter shall be interpreted in accordance with the general provisions in Title VII of the Charter governing its interpretation and application and with due regard to the explanations referred to in the Charter, that set out the sources of those provisions. 2. The Union shall accede to the European Convention for the Protection of Human Rights and Fundamental Freedoms. Such accession shall not affect the Union’s competences as defined in the Treaties. 3. Fundamental rights, as guaranteed by the European Convention for the Protection of Human Rights and Fundamental Freedoms and as they result from the constitutional traditions common to the Member States, shall constitute general principles of the Union’s law”. See: European Union Agency For Fundamental Rights, *The European Union as a Community of values: safeguarding fundamental rights in times of crisis*, 2012, available at [http://fra.europa.eu/sites/default/files/fra-2013-safeguarding-fundamental-rights-in-crisis\\_en.pdf](http://fra.europa.eu/sites/default/files/fra-2013-safeguarding-fundamental-rights-in-crisis_en.pdf), 8.

rights of persons belonging to minorities.”(46) These foundational values have normative implications for both candidate countries and EU Member States. Nonetheless the sanctioning procedure against a Member State has never been used and might only have a deterrent effect.(47)

The obligation to comply with fundamental rights also arises “from the constitutional traditions common to the Member States” which constitute the general principles of EU law. The recalled multi-level governance of the community of values provides for the sharing, in a coordinated system, of the protection of fundamental rights.(48)

Regrettably, the actions of the Member States must comply with the requirements deriving from the fundamental rights guaranteed in the legal order of the EU “only when they are implementing Union law”, according to European Court of Justice case-law.(49) The exact scope of application of fundamental rights obligations under EU law remains open to interpretation and discussion. It is up to the Court, also in part to guarantee legal clarity, to fine-tune the limits of the fundamental rights review offered by EU law.(50)

This situation seems to be the consequence of a limited awareness of EU law obligations and limited access to the CJEU for individuals. Moreover, it has been reported that “even where cases reach the CJEU, there remain differences with the ECHR, with the latter hearing a large number of third-party interventions providing on-the-ground information and evidence”.(51)

It is important to remember that the “principles” are “judicially recognizable” only in the interpretation of implementing acts. Half of the rights listed in the Charter’s title on solidarity refer back to “national laws and practices”.(52)

(46) Treaty on European Union (TEU), Art. 2 “*The Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the rights of persons belonging to minorities. These values are common to the Member States in a society in which pluralism, non – discrimination, tolerance, justice, solidarity and equality between women and men prevail*”.

(47) Treaty on the Functioning of the European Union (TFEU), Artt. 258 - 259.

(48) Presented in detail in the Focus of EU Agency for Fundamental Rights (FRA)’s 2011 Annual report, *cit.* See: R. CAVALLA PERIN, *Crisis del Estado de Bienestar. El papel del Derecho Administrativo*, in J. L. Piñar Mañas (ed. by) *Crisis económica y crisis del Estado de Bienestar El papel del derecho administrativo*, Madrid, 2014.

(49) ECJ, 26 February 2013, *Åklagaren v. Hans Åkerberg Fransson*, in C-617/10, par. 18.

(50) EU Agency for Fundamental Rights (FRA), *Fundamental rights: challenges and achievements in 2012, 2013, cit.*

(51) EU Agency for Fundamental Rights (FRA), *Fundamental rights: challenges and achievements in 2012, 2013, cit.* To gain political consensus on the inclusion of all these rights in the Charter, the drafters included a cross-cutting provision in paragraph 4 of Article 52.

(52) Charter of Fundamental Rights of The European Union, Art. 52, differentiates between rights and “principles”. The article “*Scope and interpretation of rights and principles*” state that “*Any limitation on the exercise of the rights and freedoms recognised by this Charter must be provided for by law and respect the essence of those rights and freedoms. Subject to the principle of proportionality, limitations may be made only if they are necessary and genuinely meet objectives of general interest recognised by the Union or the need to protect the rights and freedoms of others. 2. Rights recognised by this Charter for which provision is made in the Treaties shall be exercised under the conditions and within the limits defined by those Treaties. 3. In so*

This implies that the European Community of values requires that the EU and its Member States respond by working “closely together to support growth and employment, ensure financial stability, and put in place a better governance system for the future”.

EU Member States should not be seen as decoupled from their neighboring states and the EU as a whole. Member States and the EU are increasingly linked by an interdependent, but in some ways “semi-constitutional”, construction.<sup>(53)</sup>

The EU principle of solidarity,<sup>(54)</sup> together with the corresponding national principles, stipulates that the citizens, as members of a Community of values, should assure loyalty to the deeper meaning of solidarity implied by social cohesion.

It has always been considered that Government representatives and administrators should not only conform to Constitutions and laws, but also adhere to the scope and spirit of such rules (principles).

By way of example, the Italian Constitution provides for any citizen to be loyal to the Constitution and laws, and elected politicians and public officials have a specific duty of “discipline and honor” in their functions (art. 54 Italian Constitution).<sup>(55)</sup> The further obligation of civil servants (including elected politicians) implies that their work must aim at reaching the final goal of public interest (“the spirit of the law”) with a commitment that in fact goes beyond the legal *minima*.

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*far as this Charter contains rights which correspond to rights guaranteed by the Convention for the Protection of Human Rights and Fundamental Freedoms, the meaning and scope of those rights shall be the same as those laid down by the said Convention. This provision shall not prevent Union law providing more extensive protection. In so far as this Charter recognises fundamental rights as they result from the constitutional traditions common to the Member States, those rights shall be interpreted in harmony with those traditions”.*

(53) EU Agency for Fundamental Rights (FRA), *Fundamental rights: challenges and achievements in 2012*, 2013, cit. S. GRILLER – J. ZILLER (eds. by), *The Lisbon Treaty. EU Constitutionalism without a Constitutional Treaty?*, Springer, Wien, 2008, 235-256; J. ZILLER, *Il nuovo Trattato europeo*, Il Mulino, Bologna, 2007, 27 et seq. J.-B. AUBY – J. DUTHEIL DE LA ROCHÈRE, *Introduction*, in J.-B. Auby – J. Dutheil de la Rochère (eds. by) *Traité de droit administratif européen*, Bruxelles, 2014, 30-32. In the same book see: S. DE LA SIERRA, *Les sources constitutionnelles du droit administratif européen*, 487-489.

(54) The principle of solidarity is applied in the context of social protection. Cfr. ECJ, *Poucet v. Assurances générales de France* in cases C-159/91 and C-160/91, [1993] ECR 637. The French government cited Article L 111-1 of the Social Security Code, which defines the principles of social protection in France: solidarity and compulsory affiliation. See also: Charter of Fundamental Rights of the European Union, Artt. 27-38. Chapter IV is entitled ‘Solidarity.’ Artt. 27-34 bear directly on employment and industrial relations: Workers’ right to information and consultation, right to collective bargaining and action, right of access to placement services, protection in the event of unjustified dismissal, fair and just working conditions, prohibition of child labour and protection of young people at work, family and professional life, and social security and social assistance. The other articles in the Solidarity Chapter concern: health care, access to services of general economic interest, environmental protection and consumer protection.

(55) Italian Constitution, Art. 54, “All citizens have the duty to be loyal to the Republic and to uphold its Constitution and laws. Those citizens to whom public functions are entrusted have the duty to fulfil such functions with discipline and honor, taking an oath in those cases established by law”.

A lack of loyalty to these aims risks undermining the credibility and effectiveness of public institutions, and may warrant sanctions that should differ from criminal or civil sanctions, but should be either disciplinary or reputational for public servants and undertakings, in the sense of a lack of respect for the community of the citizens. Violation of the integrity principle undermines the link of solidarity typical of citizenship.

Such a commitment might be considered as soft law, and sanctions for its violation might be issued to unfair citizens.

**3. The problem of legal rules, effectiveness  
and rapid obsolescence. The instruments of transparency  
and accountability. The need for fine-tuned strategies  
for fighting collusion and corruption**

The two pillars of transparency and accountability should be correctly addressed to encourage correct incentives toward integrity and avoid establishing a further cumbersome procedure either for public authorities or economic operators in the market.<sup>(56)</sup> Recording and reporting mechanisms together with benchmarking might become useful tools for integrity.<sup>(57)</sup>

The right incentives and disincentives at the right time for public and private part compliance,<sup>(58)</sup> as well as the correct quantity/quality of transparency and accountability, should be provided.

(56) OECD, *Recommendation of the Council on Enhancing Integrity in Public Procurement*, C(2008)105, 2008, *cit.* The principles set out in the Recommendation are anchored in four pillars: transparency, good management, prevention of misconduct, accountability and control. See also: United Nations Office on Drug and Crime (UNODC) and the World Bank, *Stolen Asset Recovery (StAR), Initiative: Challenges, Opportunities, and Action Plan*, June 2007 and Interaction, *Anti-corruption and Transparency*, 2013, available at <http://www.interaction.org/document/2013-q20-anti-corruption-and-transparency-background-policy-brief>, 3. “Anonymous companies are increasingly being misused by criminals and kleptocrats to conceal their identities while they benefit from the assets derived from their illegal activities. Once these anonymous companies are formed they easily enter the global financial system to begin the process of laundering the criminal proceeds. The lack of transparency of beneficial ownership of these companies makes it too easy to hide the proceeds of corrupt acts. It is estimated that \$20 billion to \$40 billion are illegally removed from developing countries annually – roughly equivalent to the combined annual GDP of the world’s 12 poorest countries, where more than 240 million people live. Furthermore, these stolen assets are often hidden in the financial centres of developed countries. The true cost of corruption far exceeds the value of these stolen assets – siphoning away funds that could have been used to further critical development goals”.

(57) G. M. RACCA, *The Electronic Award and Execution of Public Procurement*, in *Ius Publicum Network Review*, 2012, available at <http://www.ius-publicum.com/pagina.php?lang=it&pag=articoli&n=2>, 17 et seq.; OECD, *Checklist for record keeping*, 2013, available at <http://www.oecd.org/>; World Bank, *Country Procurement Assessment Report*, 2013, available at <http://web.worldbank.org/>. Concerning the tools to be implemented see also: EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, *cit.*, 57 et seq.

(58) P. TREPTE, *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Public Procurement*, paper to OECD Expert Group meeting on Integrity in Public Procurement, 2005, 3.

It seems important to distinguish between different kinds, forms and means of transparency and accountability in order to assure the right incentives for compliance.

At the international level, for example, the United Nations Convention against Corruption (UNCAC) requires the disclosure and declaration of any existing interest, in particular in public procurement.<sup>(59)</sup> It recommends that each party make all information relating to procurement public and that all the requirements for awarding a contract be clearly established in advance and published. The selection criteria must be objective and predetermined, and a system of domestic review and appeal must be available in the event that a conflict arises. Other principles to promote transparency and accountability include a system of accounting and auditing standards and related oversight, as well as effective and efficient systems of risk management and internal control.<sup>(60)</sup>

A set of instruments has already been foreseen for public officials, at various levels. However, they are often not effective and merely constitute redundant bureaucracy and red tape for economic operators.<sup>(61)</sup>

Incentives and sanctions on compliance by politicians could be made to turn on the values that they should pursue in the public interest.

Especially with regard to procurement, strategies could be designed by skilled teams of procurement officials to mitigate corruption, for example by tampering with the size of lots to be purchased, or with the kind of products, work or services required on a case by case basis.<sup>(62)</sup>

These types of strategies could efficiently prevent collusion and nurture competition in the relevant markets; moreover, discouraging repetitive procedures may improve the quality of public spending.<sup>(63)</sup> The procurement strategies are

(59) United Nations Convention Against Corruption, Art. 9.

(60) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 8-9.

(61) Transparency generally involves: (a) publicity of procurement opportunities and the disclosure of the rules to be followed; (b) undertaking procurement processes publicly and visibly, according to prescribed rules and procedures that limit the discretion of officials; and (c) the provision of a system for monitoring and enforcing applicable rules. Given that procuring entities frequently have a high degree of discretion in the procurement process, it is also transparency which allows this exercise of discretion to be monitored. Concerning the principle of transparency in EU in public contracts see also: M. TRYBUS, *Public Contracts in European Union Internal Market Law*, in R. Noguellou – U. Stelkens (eds. by), *Comparative Law on Public Contracts*, Bruxelles, 2010, 103 et seq. and in the same book R. CARANTA, *Transparence et concurrence*, 145 et seq.; J. GONZALEZ GARCÍA, *Classic Procurement Procedures*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public Contract Law. Public Procurement and Beyond*, Bruxelles, 2014, 61-64.

(62) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 14; concerning the problem of a qualified workforce in the field of the US Public Contracts see: S. L. SCHOONER, *Contractor Atrocities at Abu Ghraib: Compromised Accountability in a Streamlined, Outsourced Government*, in *Stanford Law & Policy Review*, 2005, 10-11.

(63) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 2013, 32, between the 2008 and the 2013 “the majority of countries reformed their procurement legislation while only 7% reported investing in human, financial and technological resources” to ensure an adequate degree of transparency. See also: OECD, *Survey on Reporting Back on Procurement Recommendation*, 2011.

characterized by rapid obsolescence, due to their need to be frequently changed in order to get the most favorable tenders from the market, improving participation and fostering competition. Working in skilled teams could also prevent the loneliness of the procurement officials, who might otherwise find it difficult to resist the pressure applied by unfair participants. Networking between procuring entities and Central Purchasing Bodies also might strengthen these positive effects.(64)

### 3.1. The incentives for compliance in the public sector

Preventing and combating favoritism, conflicts of interest, corruption and collusion cannot be left to the mechanical application of legal rules and procedures.(65)

The legal rules ought to be designed in such a way as to provide “correct” incentives towards integrity. A joint approach and multidisciplinary strategy for effective enforcement are required. Public resources are too scarce (and precious) for any waste to be tolerated, be it for incompetence or corruption.(66) Monitoring the performance of any procurement system requires peer reviews, benchmarks and indicators.(67)

A new emphasis on individual responsibility, organizational design and economic incentives is needed. In addressing these issues, it is necessary to investigate civil servants’ ethical obligations as a set of norms which guide public administration towards the public interest,(68) taking into account that “procurement officials are not recognised as a specific profession in more than a third or OECD countries” and the procurement function is not yet considered to be strategic.(69) In assessing “ethics requirement for public officials,

(64) G. M. RACCA – G. L. ALBANO, *Collaborative Public Procurement and Supply Chain: The European Union Experience*, in C. Harland – G. Nassimbeni – E. Schneller (eds. by) *The SAGE Handbook of Strategic Supply Management*, London, 2013, 185-188 and G. M. RACCA, *Collaborative procurement and contract performance in the Italian healthcare sector: illustration of a common problem in European procurement*, in *PPLR*, 2010, 1130-132. Collaborative procurement in the EU through a network of CPBs is the object of the *Healthy Ageing and Public Procurement of Innovation (HAPPI)* project funded by the EU Commission (DG Enterprises) – rif. call ENT/CIP/11/C/N02C011 – within the framework of the *Competitiveness and Innovation Programme (CIP)*. The project concern the EU joint procurement system in Healthcare. see: <http://www.happi-project.eu/>.

(65) S. ROSE-ACKERMAN, *Corruption and conflicts of interest*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 5-10

(66) OECD, *Bribery in Public Procurement. Methods, Actors and Counter-Measures*, 2007, available at <http://www.oecd.org/investment/anti-bribery/anti-briberyconvention/44956834.pdf>, 64.

(67) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 2013, 97. G. L. ALBANO, *Discussion Paper on Public Procurement Performance Measures. OECD Meeting of Leading Practitioners on Public Procurement*, 11-12 February 2012, available at <http://search.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=GOV/PGC/ETH%282013%291&docLanguage=En>, 7-8.

(68) G. M. RACCA, *Disciplina e onore nell’attuazione costituzionale dei codici di comportamento*, in F. Merloni – R. Cavallo Perin, *Al servizio della Nazione. Etica e statuto dei funzionari pubblici*, FrancoAngeli Editore, Milano, 2009, 254 et seq.

(69) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 2013, 78. The report identified: Austria, Belgium, Czech Republic, Finland, France, Germany, Italy, Japan, Luxembourg, Norway, Turkey.

including procurement officials, policymakers may wish to consider that ethics rules and screening procedures are almost always part of part of a broader fabric of social norms, laws and mechanisms for ensuring social harmony”.(70) In that light, the ethics rules designed to protect the procurement system “should complement the broader set of norms and rules, and may well draw upon other formal and informal mechanisms for maintaining social order”.(71) Preventive policies cover a wide variety of aspects including clear-cut ethical rules, awareness-raising measures, building a culture of integrity within various organizations, setting a firm tone from the top in relation to integrity issues, to effective internal control mechanisms, transparency, easy access to public interest information, effective systems for evaluating the performance of public institutions.(72) Forms of effective external and internal audits and asset disclosure might make it possible to consolidate the accountability of public officials.(73) A clear code of conduct may provide concrete examples of situations officials could face in the course of their work. It should also give the contact details of persons that can provide advice and guidance to procurement practitioners. Many countries have codes of conduct that set general rules by which all public officials are to govern themselves. These general rules are sometimes supplemented by more specific codes related to a high ranking and specific high-risk positions, of which public procurement is one.(74)

Particular difficulties arise from the scarce and weak sanctions applicable to elected officials. Where they cover conflicts of interest, the codes of conduct of various elected assemblies are usually not accompanied by dissuasive sanctions. Party discipline and self-control may not be sufficiently effective in this regard. Cancellation of contracts and procedures concluded or carried out in conflict of interest situations or the recovery of estimated damages are often left to general civil regulations and are not effectively implemented in practice.(75) Integrity in politics is a serious issue in many countries and codes of conduct within political parties or elected assemblies at the central or local level are the exception more than the rule and often lack an effective monitoring

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(70) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 11-12. See: OECD, *CleanGovBiz Integrity in practice. Toolkit for Integrity*, available at <http://www.oecd.org/cleangovbiz/49891354.pdf>, 2012, 96.

(71) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 11-12.

(72) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 10.

(73) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 11 and 13.

(74) OECD, *Code of conduct for procurement practitioners*, in <http://www.oecd.org/>.

(75) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 12.

mechanism or clear sanctioning regulations, rarely leading to the application of dissuasive penalties. Insufficient accountability has generated a perception of quasi-impunity of political elites.(76)

At the same time, a corresponding obligation for private operators to act with integrity when dealing with a public administration is also required.

Both sides (public and private) must face sanctions for improper behavior, whether by impaired reputation, or through sanctions on individuals acting on the organizations' behalf (criminal, administrative, or disciplinary sanctions, for example).

It is well-known that legal systems punish corruption as a crime,(77) but it is less known that corrupt behavior can also be sanctioned because it undermines a plurality of further public interests and goods protected by the law.(78)

Social cohesion for the benefit of the protection of fundamental rights requires not only that economic operators abide by the rules, but also that they be sufficiently loyal to them to share the goals and accept the loss of a contract if a better tender is submitted.

Most corrupt behavior involves not only the violation of criminal law but also the citizen's lack of loyalty to the State (Republic). The citizen does not hesitate to undermine the proper functioning of the institutions, such as the course of justice (by buying a judgment), or of the administration (by paying an official to win a tender) for individual interest.(79)

Non-acceptance of the rules of the game and the will to win unfairly betrays the principle of solidarity between the members of a community, and should trigger exclusion from that community.

Such unfaithfulness does not concern only the corruptor and the person corrupted. Corruptive behavior gives rise to a general distrust of institutions, which weakens other citizens' confidence in the impartiality and effectiveness of public institutions. Similarly, corruption alters the proper functioning of private institutions when these are exposed to corruptive power. Here too, corruption breeds a lack of confidence in the proper functioning

(76) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, 8.

(77) H. CAROLI CASAVOLA, *Global rules for public procurement*, in (R. Noguellou – U. Stelkens) *Comparative Law on Public Contracts*, Bruxelles, 2010, 48 et seq., deals with the Italian implementation of the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. Recently, see: Law 6 November 2012, No. 190, and G. M. RACCA, *La prevenzione e il contrasto della corruzione nei contratti pubblici (Art. 1, commi 14-25, 32 e 52-58)*, in B. G. Mattarella – M. Pelissero (ed. by) *La legge anticorruzione. Prevenzione e repressione della corruzione*, Torino, 2013, 125-151.

(78) R. CAVALLO PERIN – B. GAGLIARDI, *Status dell'impiegato pubblico, responsabilità disciplinare e interesse degli amministrati*, in *Dir. Amm.*, 2009, 53.

(79) G. M. RACCA, *Disciplina e onore nell'attuazione costituzionale dei codici di comportamento*, cit., 250 et seq.

of market forces, and undermines public faith in the ability of the market to correct itself.

Loyalty is considered to be a constitutive element of every organization as it represents an element of cohesion.<sup>(80)</sup> Its deficiency is usually sanctioned by the organization through temporary discontinuation of membership and, in serious cases, through expulsion from the corporate team, i.e., through temporary or permanent deprivation of the benefits enjoyed by belonging to the corporate group.

The relationship between the benefits of citizenship and a violation of the duty of loyalty to the State should be seriously re-assessed. Violation of the latter could lead to the administrative sanction of a temporary suspension of the benefits of citizenship scaled in proportion to the severities of the unloyal behavior.

The sanction would not be a fine, but it could mean being denied the right to receive public services, with any privileges of citizenship, for some time (e.g. one month). The essential element of the sanction is not so much the inconvenience that this might cause; it is the impairment and compromising of the person's reputation within the social group, which presents a very evident deterrent effect.

### 3.2. The incentives for compliance in the private sector

Integrity in the business sector is important because clean companies are more efficient and more competitive, which in turn leads to healthier markets and greater investor confidence. Governments can promote greater private sector integrity by encouraging companies to adopt stronger anticorruption practices and robust corporate governance systems (compliance and ethics systems) and to compete fairly and openly.<sup>(81)</sup> Corporations are called upon to

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(80) R. CAVALLO PERIN, *L'etica pubblica come contenuto di un diritto degli amministrati alla correttezza dei funzionari pubblici*, in F. Merloni – R. Cavallo Perin, *Al servizio della Nazione. Etica e statuto dei funzionari pubblici*, cit., 152-155. See also: OECD, *Bribery in Public Procurement. Methods, Actors and Counter-Measures*, 2007, available at <http://www.oecd.org/investment/anti-bribery/anti-briberyconvention/44956834.pdf>, 57 et seq. The report moves into the detail of how to prevent and punish bribery. It evaluates transparency issues, as well as preventive measures and controls. One challenge pointed out in the report is to train up staff not only to spot the signs, but also to come forward and report them. This raises important issues about teamwork and loyalty of civil servant involved in public procurement.

(81) Many resources to help keep business clean are available: this includes OECD instruments such as the Anti-Bribery Convention; the Good Practice Guidance on Internal Controls, Ethics and Compliance; the Principles of Corporate Governance; and the Guidelines for Multinational Enterprises. It also includes instruments from other organizations such as the APEC Anti-Corruption Code of Conduct for Business; the Ten Principles of the UN Global Compact; the EITI Principles and Criteria; the World Economic Forum PACI Principles for Countering Bribery. See: <http://www.oecd.org/corruption/ethics/>. United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 26, "compliance systems include business

adopt principles related to human rights protection, social and environmental standards, and anti-corruption in the management of their businesses, on a voluntary basis, according to key UN targets.(82)

Guidelines,(83) recommendations for responsible corporate behaviour, integrity pacts,(84) and standards of conduct (e.g. codes of ethics in business)(85) may favor the prevention of and fighting against illicit conducts by promoting the best practices and integrating legal provisions. However, these tools require a voluntary commitment on the part of the economic operators.(86)

Compliance systems have proven to be an effective instrument for combating corruption inside private organizations.(87) The more advanced experiences

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principles that reject corruption and put standards and procedures in place to ensure that the entity acts according to the legal requirements”.

(82) Transparency International, *Handbook for Curbing Corruption in Public Procurement*, available at [http://www.transparency.org/whatwedo/pub/handbook\\_for\\_curbing\\_corruption\\_in\\_public\\_procurement](http://www.transparency.org/whatwedo/pub/handbook_for_curbing_corruption_in_public_procurement), 2006, 70. “They derive from the Universal Declaration of Human Rights, the International Labour Organization’s Declaration on Fundamental Principles and Rights at Work, the World Summit for Social Development in Copenhagen 1995, the Rio Declaration on Environment and Development of 1992 and the United Nations Convention Against Corruption. The 10th Principle “Anti-Corruption” was integrated after long debates in 2004”.

(83) See the *OECD guidelines for Multinational enterprises*, available at: <http://mneguidelines.oecd.org/text/>.

(84) Transparency International, *The integrity pact. The Concept, the Model and the Present Applications: a Status Report*, 31 December 2002, 3 e 4; Transparency International, *Handbook for Curbing Corruption in Public Procurement*, 80-81.

(85) See: International Chamber of Commerce, *Combating Extortion and Bribery: ICC Rules of Conduct and Recommendations*, available at <http://www.iccwbo.org/Advocacy-Codes-and-Rules/Document-centre/2004/ICC-Rules-of-Conduct-and-Recommendations-to-Combat-Extortion-and-Bribery-%282005-Edition%29/>. Transparency International, in co-operation with Social Accountability International, spearheaded the development of the Business Principles for Countering Bribery (BPCB), introduced in December 2002. The Business Principles as well as the Guidance Document and a document outlining the Six Step Implementation Process can be downloaded for free at: [http://www.transparency.org/global\\_priorities/private\\_sector/business\\_principles](http://www.transparency.org/global_priorities/private_sector/business_principles). OECD, *code of conduct for procurement practitioners*, in <http://www.oecd.org/>.

(86) Transparency International, *Handbook for Curbing Corruption in Public Procurement*, cit, 68 et seq.

(87) The US legal Framework provide a committee for drafting federal guide-lines on corporate sentences (see: *Sentencing Reform Act*, Pub. L. No. 98-473, 98. Stat. 1873,1987, 18 U.S.C.A. §§ 3351-3742; 28 U.S.C.A. §§ 991-998) and a guidelines system for establishing and maintaining within the corporates specific internal controls to detect and prevent improper conduct (*United States Federal Sentencing Guidelines*, 1<sup>st</sup> November 1991, 18 U.S.C. §§ 1365 (f), 1801; 42 U.S.C. §§ 1129(a), 14133; 49 U.S.C. § 31310). About the case-law *United States v. Johnson & Johnson*, 37, Cr-99 (DDC 2011); *United States v. Caputo*, 456 F. Supp. 2d 970 (N.D. Ill 2006); *United States v. Booker*, 375 F.3d 508 (7<sup>th</sup> Cir. 2004); *Fanfan v. United States*, 2004 WL 1723114 (D. Me. 2004); *Hollis v. City of Buffalo*, 28 F. Supp. 2d 812, 821 (W.D. N.Y. 1998); *United States v. Exxon Corp.*, No. A90-015 CR (U.S. Superme Court 1990); *Hoffman – LaRoche Ltd. et Rhone Paulenc*, Plead Agreement, 1999; *Caremark Intern. Inc.* Derivate Litigation, 698 A.2d 959 (Del. Ch. 1996); *United States v. Daiwa Bank* (SDNY 1995 Cr 947); *United States v. C.R. Bard, Inc.*, 848 F. Supp. 287 (D. Mass. 1994); *United States v. NME Psychiatric Hospital*, 94 Cr. 0268 (D.D.C. 1994). See J. E. MURPHY, *The EU Takes a Tentative First Step Toward Compliance Programs*, in *Ethikos* Jan./Feb. 2012, Vol. 25, No. 4; J. E. MURPHY, *How the CEO can make the difference in Compliance and Ethics Program*, in *Ethikos*, May/June 2007, Vol. 20, No. 9; ID., *Ethic for Ethicists? A code for Ethics and Compliance and ethics professionals*, in *Ethikos*, March/April 2004, Vol. 17, No. 8; J. E. MURPHY – C. VIGALE, *The Role Of Incentives In Compliance Programs*, in *Ethikos* May/June 2005, Vol. 18, No. 6; A. SINGER,

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in the United States permit enterprises to discover and disclose the corrupt practices of their own employees.<sup>(88)</sup> In the US experience, public officials require the undertaking to provide a substantial compliance system in order to guarantee that future procurement will be fairly conducted.<sup>(89)</sup> Suspension or debarment from public contracts has proven to be an effective tool in the fight against corruption. Depriving private companies of the opportunity to do business with the government is likely to be one of the strongest deterrents for future wrongdoers, and ensures that the government does not enter into contracts with contractors that lack effective internal controls.<sup>(90)</sup>

Whenever an economic operator tries to avoid competition by persuading a government to give it a protected position, colluding with competitors to fix prices, or artificially dividing requirements among a group of contractors,

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*Anti-Corruption Enforcement Gains Traction On a Global Scale*, in *Ethikos* Jan./Feb. 2012, Vol. 25, No. 4; ID., *Even At Smaller Companies Ethics Programs Gain Traction*, in *Ethikos* Jan./Feb. 2010, Vol. 23 No.4; J. KAPLAN, *Key to success when mitigating identified compliance and ethics and ethic risks*, Corporate Compliance and Ethics Insights, June 2011; C. E. CARRASCO – M. K. DUPEE, *Corporate Criminal Liability*, in *Am. Crim. L. Rev.*, 1999, 445 ss.

(88) On compliance and ethics programs in the public procurement sector see: *United States v. Metcalf & Eddy, Inc.*, CA No. 99CV-12566-NG (D. Mass. 1999); *United States v. Depuy, Inc.*, 34 (DDC 1999); *United States v. Lucas Aerospace Communications & Electronics, Inc., Wholly Owned Subsidiary of Lucas Industries, Inc.* (1994 Cr 493 E.D. N.Y.); *United States v. Hernandez*, 952 F.2d 1110 (9<sup>th</sup> Cir. 1991). See: J. E. MURPHY, *A Compliance and ethics & Ethics Program on a Dollar a Day: How Small Companies Can Have Effective Programs*, Society of Corporate and Compliance Ethics, August 2010; J. M. KAPLAN, *Compliance Programs for Smaller Companies*, in *Ethikos* Jan./Feb. 2008, Vol. 21 No. 5; K. W. BUFFINGTON – M. FLYNN, *The Legal Aspects of Public Purchasing*, in *Journal Of Public Procurement*, Vol. 6, 3, 2006, p. 321ss.; C. R. CARTER – M. M. JENNINGS, *The Role Of Purchasing In Corporate Social Responsibility: A Structural Equation Analysis*, in *Journal of Business Logistics*, Vol. 25, No.1, 2004, 145 ss.

(89) On the relevance of compliance and ethics programs for the contracting authorities see *United States Federal Acquisition Regulation*, Vol. 73, §§ 67064 - 67091-92, Rev. 12 November 2008 about the requirements for a federal contractor code of business ethics and conduct, an internal control system, and disclosure to the Government of certain violations of criminal law, violations of the civil False Claims Act, or significant overpayments. See OECD, *Good practice Guidance on Internal Control, Ethics and Compliance*, 18<sup>th</sup> February 2010; J. LEET, *A New Compliance and Ethics Certification Program*, in *Ethikos*, Jan./Feb 2007, Vol. 20, No. 4; B. SHARPE, *Checking your Compliance and ethics Program's performance – By the Numbers*, in *Ethikos*, May/June 2003, Vol. 16, No. 10. See also: U.S. Department of Justice, *Largest health care fraud case in U.S. history settled HCA investigation nets record total of \$ 1.7 billion*, available at [http://www.justice.gov/opa/pr/2003/June/03\\_civ\\_386.htm](http://www.justice.gov/opa/pr/2003/June/03_civ_386.htm).

(90) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 25. As debarment systems have matured in different countries, two broad models for debarment have emerged. The first is a highly discretionary approach, such as that used by the United States federal procurement system, under which a senior contracting official, acting on behalf of one or more government agencies, may exclude contractors because of almost any serious issue regarding contractor qualification. The alternative model, used by the World Bank (WB) in its sanctions system, is much more focused: under this approach, the reviewing officials act in an adjudicative manner, and a formal determination must be made as to whether the contractor in question has committed acts that qualify as grounds for debarment, under a specific list of prohibited acts. The EU Directives, for example, do not provide for a debarment regime, but for an ad-hoc approach of exclusion in which each procuring entity has to determine, on a case-by-case basis, whether or not a particular company is suitable and reliable or should be excluded from a public tender procedure. See: S. WILLIAMS-ELEGBE, *Fighting Corruption in Public Procurement. A Comparative analysis of Disqualification or Debarment Measures*, Oxford, 2012, 38-81. C. R. YUKINS, *Cross-Debarment: A Stakeholder Analysis*, *GW Law Faculty Publications*, 2013, 220 et seq.

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the result for the public consumer is almost always a higher price for inferior goods.<sup>(91)</sup> The risk of the loss of not only reputation but also the opportunity to win procurements should act as an effective deterrent for improper conduct.

An effective anti-corruption clause might be included in order to guarantee a more effective follow-up in the event of corrupt practices being proven within the lifetime of the contract, “e.g. clear-cut procedures for declaring a contract null and void or for applying other contractual penalties”.<sup>(92)</sup> This would avoid the lengthy procedures involved in the annulment of the “corrupt” public contract with a separate civil action that often risks producing effects too late, when it is difficult or even impossible to fully recover the losses.<sup>(93)</sup>

#### **4. Public oversight, “social witness” experience for the evidence of the quality of public spending**

It has been recognized that civil society has an important role to play in the fight against corruption.<sup>(94)</sup> Governments are realizing the growing importance of civil society participation, and are starting to involve citizens in scrutinizing government activities.<sup>(95)</sup>

The monitoring of procurement processes by an independent voice might provide a source of expertise and make it possible “to raise issues and difficult questions, to manage conflict and balance powers and bring together groups of people”.<sup>(96)</sup> In a far-reaching transparency policy, civil society can become

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<sup>(91)</sup> G. M. RACCA – R. CAVALLO PERIN, *Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption*, in *European Procurement & Public Private Partnership Law Review*, 2013, 287-290; G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011, 99 et seq.; OECD instruments such as the Recommendation concerning Effective Action against Hard Core Cartels and the Guidelines for Fighting Bid Rigging in Public Procurement help to ensure free and fair competition. On OECD Legal Instruments on Corruption Prevention see: <http://www.oecd.org/gov/ethics/oecdlegalinstrumentsoncorruptionprevention.htm>.

<sup>(92)</sup> EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 34.

<sup>(93)</sup> R. CAVALLO PERIN – G. M. RACCA, *Caratteri ed elementi essenziali nelle sponsorizzazioni con le pubbliche amministrazioni*, in *Dir. Amm.*, 2014, forthcoming.

<sup>(94)</sup> United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 26. R. CAVALLO PERIN, *L'etica pubblica come contenuto di un diritto degli amministrati alla correttezza dei funzionari pubblici*, cit., 159-161, on the right of citizens to require compliance of civil servant to their duties. P. SZAREK-MASON, *OLAF: The anti-corruption policy within the European Union*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 288.

<sup>(95)</sup> See also a Mexican case where the participation of “social witnesses” to scrutinise the integrity of the procurement procedure is mandatory for large contracts. A study of the OECD and the World Bank Institute (2006) found that such practice had resulted in savings of approximately USD 26 million in 2006 and increased the number of bidders by over 50%.

<sup>(96)</sup> Transparency International, *Handbook for Curbing Corruption in Public Procurement*, cit., 80 et seq.

very active in the “complex monitoring of procurement processes and public contracts”.(97) “Integrity pacts”(98) could present an effective instrument for defining further instruments to provide transparency, monitoring activities by civil society organizations.

Integrity pacts, as agreements between the contracting authority for a particular project and the bidders, who are all committed to abstaining from any corrupt practices,(99) could help enhance public trust in government contracting and therefore contribute to improving the credibility of government procedures and administration in general.(100) Integrity pacts can establish the contractual rights and obligations of all the parties to a governing contract and thus eliminate uncertainties as to the quality, applicability and enforcement of criminal and contractual legal provisions in a given country.(101) Moreover, such obligations could attribute a role to third parties in order to assure further monitoring during the selection and execution of the contract. Codes of conduct and integrity pacts may introduce additional constraints on transparency and monitoring during the period of execution of the contract by also allowing for the collaboration of other participants in the competition as well as social witness(102) and citizens’ associations.(103)

Voluntary compliance with the terms defined in integrity pacts might allow economic operators to engage in the monitoring activity. The reciprocal obligations between private parties and public entities makes each party liable

(97) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report, cit.*, 31.

(98) EU Commission, *op. ult. cit.*, 31. Transparency International, *The integrity pact. The Concept, the Model and the Present Applications: a Status Report*, 31 December 2002, 12.

(99) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report, cit.*, 31.

(100) Using the integrity pacts economic operators wishing to participate in a procedure for the award of a public contract, contracting and public officials acknowledge that they understand and accept the obligations arising as a result of their turning. OECD, *Integrity in Public Procurement: good practice from A to Z*, 2007, *cit.*, 158.

(101) Transparency International, *The integrity pact. The Concept, the Model and the Present Applications: a Status Report, cit.*, 3 - 4. “The IP is intended to accomplish two primary objectives: (a) to enable companies to abstain from bribing by providing assurance to them that (i) their competitors will also refrain from bribing, and (ii) government procurement, privatisation or licensing agencies will undertake to prevent corruption, including extortion, by their officials and to follow transparent procedures; and (b) to enable governments to reduce the high cost and the distortionary impact of corruption on public procurement, privatisation or licensing”. Transparency International, *Handbook for curbing corruption in public procurement*, 2006, 125 et seq.

(102) OECD, *CleanGovBiz Integrity in practice. Fighting corruption in public procurement*, February 2012, 25 e ss.; OECD, *Integrity in Public Procurement. Good Practice From A To Z, cit.*, 117 et seq.

(103) Transparency International, *The integrity pact. The Concept, the Model and the Present Applications: a Status Report, cit.*, 5. The report highlights the two arguments that “often raised against such a monitoring role for civil society can easily be disarmed: availability of the necessary expertise among the Civil society monitors (...) and the legitimate confidentiality of property information, to which civil society representatives would gain access”.

in respect of the others(104) for any violations that occur during the whole procurement cycle.(105)

With a view to ensuring that they are effectively implemented, integrity pacts(106) could be effectively monitored by civil society groups at the initiative of NGOs, especially with regard to certain large public contracts (e.g. large-scale infrastructure projects).(107)

Public oversight requires the transparent management of public finances in order to improve the likelihood of limited resources being used as intended. All countries should establish transparent and accountable public finance management systems, including for budgeting and procurement.(108) Information regarding awarded contracts, including the name of the contractor and the contract price, should be publicly available, either through transparency measures or through access to information regimes.(109) Not only is the economic efficiency in procurement important, but so is the perceived legitimacy of public decisions. This legitimacy is fostered by due procedures in awarding public contracts even if due processes might represent more economic costs (i.e. less economic efficiency).(110)

Civil society initiatives have already had a “beneficial effect on the accountability of local administrations with regard to transparency of public spending”.(111) Civil society, “be it a single citizen, media, a company, an NGO, academia, etc.” may identify possible improper public official actions which may be the result of collusion between a public official and a bidder.(112)

(104) Transparency International, *The integrity pact. The concept, the Model and the Present application. A status report*, cit., 5. OECD, *Principles for Integrity in Public Procurement*, 2009, 36-37.

(105) Transparency International, *Handbook for curbing corruption in public procurement*, 2007, 82.

(106) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 31. Integrity pacts are agreements between the contracting authority for a particular project and the bidders, all committing themselves to abstain from any corrupt practices.

(107) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 31. Integrity pacts are agreements between the contracting authority for a particular project and the bidders, all committing themselves to abstain from any corrupt practices.

(108) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 30-31.

(109) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 27.

(110) EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, 2013, 30.

(111) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 28.

(112) G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, cit., 99-100; OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 119. One of the ten OECD principles for enhancing integrity in public procurement provides that “Member countries should empower civil society organisations, media and the wider public to scrutinise

Directing media attention onto procurement spending might help in discovering “that the number of computers contracted and purchased for a public school was not delivered or that a procurement official is providing incomplete information to selected bidders in order to favor a certain company”, which repeatedly wins contracts from the same procuring entity.(113) The reputation of the subjects involved would be compromised and might be an incentive for appropriate behavior. Civil society can generate pressure against corruption in public procurement, leading to various kinds of sanctions of the corrupt actors

This practice of “direct social control” could complement more traditional accountability mechanisms under specific circumstances. Strict criteria should be defined so as to determine when direct social control mechanisms may be used, on the basis of the high value, complexity and sensitivity of the procurement, and for the purpose of selecting the external observers.(114) Obviously, a systematic verification should be carried out to ensure that the external observer is exempt from any conflict of interest to participate in the process and that they are also aware of any restrictions and prohibitions with regard to potential conflict-of-interest situations, such as the handling of confidential information. The oversight of third parties could prove extremely useful for ensuring the competitive selection principle is respected and the procurement correctly executed.(115)

Governments should support an effective monitoring by civil society “by ensuring timely access to information, for instance through the use of new technologies, and providing clear channels to allow the external observer to inform control authorities in the case of potential irregularities or corruption”.(116)

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public procurement. Governments should disclose public information on the key terms of major contracts to civil society organisations, media and the wider public. The reports of oversight institutions should also be made widely available to enhance public scrutiny. To complement these traditional accountability mechanisms, governments should consider involving representatives from civil society organisations and the wider public in monitoring high-value or complex procurements that entail significant risks of mismanagement and corruption”.

(113) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, cit., 119. One of the ten OECD principles for enhancing integrity in public Procurement provide that “Member countries should empower civil society organisations, media and the wider public to scrutinise public procurement. Governments should disclose public information on the key terms of major contracts to civil society organisations, media and the wider public. The reports of oversight institutions should also be made widely available to enhance public scrutiny. To complement these traditional accountability mechanisms, governments should consider involving representatives from civil society organisations and the wider public in monitoring high-value or complex procurements that entail significant risks of mismanagement and corruption”.

(114) OECD, *OECD Principles for Integrity in Public Procurement*, cit., 47.

(115) G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, cit., 99-100; United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 26-27

(116) OECD, *OECD Principles for Integrity in Public Procurement*, cit., 47.

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**5. New social sanctions for the infringement of public  
loyalty to fundamental rights: a violation of social solidarity.  
Temporary exclusion from full social membership**

Reliable judicial systems are crucial for ensuring that laws and regulations are properly enforced.

If verdicts or favors can be bought, any set of laws to curb corruption will be crippled. Clear rules on ethical conduct for judges and court officials, built around the fundamental principles of independence, impartiality, integrity, propriety, equality, competence and diligence, are essential, along with a system to make sure that they are being implemented.(117)

Different forms of sanctions need to be applied, that could also be informal in nature.(118) Informal sanctions mean penalties that do not impose tangible costs on the offender, though they may decrease their utility. It has been proven that “informal sanctions such as social disapproval, ostracism, gossip, peer pressure, or public embarrassment of offenders are often applied to try to alter behavior, and in many cases appear to be effective”.(119) In corporations and academic institutions, the failure to perform a level of service activity viewed as appropriate may be penalized through various sorts of sanctions. These may include financial sanctions, such as lower salary increases, or the denial of promotion, as well as the engendering of expressions of disapproval and a degree of social ostracism. In organizations such as the military and at some academic institutions, “honor codes exist that overlap with formal policies. One reason that these institutions label cheating and theft as honor code violations may be to create a social prohibition against them in addition to the explicit penalties in force”.(120)

According to some recent economic models, social pressure and shame can have highly effective consequences. Social penalties (condemnation, ostracism, loss of esteem)(121) or some form of public “blacklisting” of citizens that

(117) Clean gov biz, *Boosting Integrity fighting corruption, cit.*, 6. International instruments such as the UN’s Bangalore Principles of Judicial Conduct and the UN’s work on boosting judicial integrity contribute to putting these systems in place.

(118) P. BLAU, *Exchange and Power in Social Life*, New York: Wiley, 1964.

(119) C. NOUSSAIR – S. TUCKER, *Combining Monetary and Social Sanctions to Promote Cooperation*, in *Economic Inquiry*, Vol. 43:3, 2005, 649.

(120) C. NOUSSAIR – S. TUCKER, *Combining Monetary and Social Sanctions to Promote Cooperation, cit.*, 650.

(121) See for example: G. A. AKERLOF, *A Theory of Social Custom, of Which Unemployment May Be One Consequence*, in *Quarterly Journal of Economics*, 1980, 749; A. LINDBECK – S. NYBERG – J. W. WEIBULL, *Social Norms and Economic Incentives in the Welfare State*, in *Quarterly Journal of Economics*, 1999, 1; J. ELSTER, *Emotions and Economic Theory*, in *Journal of Economic Literature*, 1998, 47, distinguishes between guilt, an internal type of pressure and shame, an external type of social pressure, as forces promoting pro-social behaviour. Labour economists have modelled the effect of peer pressure on team output. For this aspect see: E. KANDEL – E. P. LAZEAR, *Peer Pressure and Partnership*, in *Journal*

betrayed the common bonds of solidarity might have a significant effect in terms of reputation, and could therefore be feared.

Informal sanctions may have less of a deterrent effect because they are less certain, but they may have the advantage of avoiding fixed administrative costs.<sup>(122)</sup> Moreover, in the context of an information society, web reputation can become a great value.

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*of Political Economy*, 1992, 801; J. M. BARRON – M. JOHN – G. K. PAULSON, *Peer Pressure in an Agency Relationship*, in *Journal of Labor Economics*, 1997, 235. K. KAMEI – L. PUTTERMAN – J.-R. TYRAN, *State or Nature? Formal vs. Informal Sanctioning in the Voluntary Provision of Public Goods*, in *Brown Economics Working Paper*, 2011 available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1752266](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1752266), 5, where they remember that James Madison wrote: “If there be no virtue among us, no form of government can render us secure. To suppose that any form of government will secure liberty or happiness without any virtue in the people is an illusion.” (Speech to Virginia Ratifying Convention, June 20, 1788). The same theme appears almost two millennia earlier in the observation of Horace that “*Leges sine moribus vanae*” (Laws without morality are useless).

(122) K. KAMEI – L. PUTTERMAN – J.-R. TYRAN, *State or Nature? Formal vs. Informal Sanctioning in the Voluntary Provision of Public Goods*, *cit.*



## CHAPTER 2

### An emblematic case: corruption as an illicit secondary consideration in public procurement in Italy

BY

Antonio ROMANO-TASSONE

Professor of Administrative Law, University of Messina

#### *1. Introduction*

The evolution of Italian legislation on Public Procurement shows a great difference between past and actual rules of award. In 1924, in the Regulations in force (“*Regolamento di contabilità pubblica*”), automatic and discretionary systems of award had the same value: Public Administration could choose the former or the latter according to the object and the purpose of the contract to be awarded. In 2006, the Italian Public Contract Code (IPPC) “*Codice dei contratti pubblici*” (2006), widely inspired by European rules, opted without uncertainty for automatic systems of award, while discretionary systems are regarded as almost exceptional.

The change was brought about by many factors, but the aim to prevent a subjective use of the award was and is nowadays the most important.

Indeed, the diffusion of corruption in the field of Public Procurement, together with the aim of the European Union to open this important market to competition, brought to a discipline in which not only the choice of the partners, but even the choice of the pattern of the relationship, is generally automatic.

Nevertheless, this situation cannot be considered suitable to meet public interests, because the physiology of contract is therefore distorted, and subjected to the only goal of preventing corruption.

#### *2. The illicit “secondary” considerations pursued through public procurement*

Public procurement has always been concerned with corruption, or rather with the abuse of power to award contracts in order to advantage some competitors. This, most of all, is due to the usual high economic value of the contracts awarded, which is an obvious incentive to criminal behaviours. Experience

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shows, however, that civil servants can be induced to abuse of award procedures not only to satisfy economic and selfish interests, but also, sometimes, for “ideal” and collective reasons. This happens, over all, when the incorrect choice is due to the aim of providing an advantage not just to a single competitor, but rather a competitor belonging to a certain group of firms. The most important aspect of this trend, is surely the purpose to advantage national over foreign companies, in order to avoid the danger of foreign dominion in national economics, that is to say, the risk of loss of national sovereignty.

Another face of this phenomenon is the aim to advantage local firms, because they usually employ local workers. Local Administrations then prefer as partners local companies, which redistribute in their own territory the proceeds of the contract.

In the end, it is worth mentioning that in Italy, in the time of “Prima Repubblica” (1945-1992), civil servants sometimes advantaged a firm that had previously paid a certain sum (usually: the 15% of the amount of the contract) to a political party. Public Procurement was so concerned with political competition, especially to rebalance the chances of the Communist Party, which was supposed to be unofficially sponsored by Soviet Union, and democratic liberal parties, because they had not such a rich and powerful sponsor.

### ***3. The evolution towards the preference of apparently automatic award systems***

Corruption in public procurement, thus, has multiple and different roots. Therefore it is not possible to look at it just as a criminal phenomenon. This is arguably the reason of the choice to contrast corruption in Public Procurement not only through usual repressive and criminal means, but also by shaping administrative procedures in order to prevent any kind of abuses.

Rules of award have then deeply changed in the last 30 years: if they were once designed to achieve at their best public interests concerned with the contract, now they have the purpose to prevent a subjective use of the award procedures. The evolution of Italian Law of public procurement, for example, shows a great difference between past and actual rules concerning the award phase.

In 1924, the Regulation in force (“*Regolamento di contabilità pubblica*”) provided the possibility of both automatic and discretionary systems for the award of public contracts. Procuring entities could choose the former or the latter according to the objects and the purposes of the contracts to be awarded.

In 2006, the *Italian Public Contract Code* (IPPC), while implementing the European Directives, clearly opted for a (supposed) objective and detailed award procedure. Discretionary systems of award (such as negotiated

procedures) are considered exceptional. The change was brought about by many factors, but the aim to prevent a subjective use of the award was and still remains the most important and unachieved goal.

Indeed, the widespread corruption in the Public Procurement sector together with the European aim to open this important market to competition, induced policymakers to adopt a legal framework in which not only the choice of the partners, but even the choice of the pattern of the relationship, is generally ruled as automatic.

#### ***4. The risks of automatic (objective) awards***

Yet, this situation cannot be considered suitable to meet public interests, since the physiology of contract is therefore distorted, and subjected to the main goal of preventing corruption.

But corruption, like any other illegal behaviour, must be most of all repressed, and in any case it must be prevented without distorting the physiology of economical relationships, otherwise public aims in contracting cannot be efficiently reached. Apart from anything else, automatic systems of award are suitable to meet public interests only if the public administration can identify in advance, perfectly and exhaustively, the performance required: otherwise, the danger of obtaining an inconvenient performance is very high. This is possible only in case of very simple (i.e.: not complex) performances, which means: not in the most important and in the wider part of public contracts. Automatic systems of award, in addition, are usually based on the lowest price offered by competitors. It is well known that often the lowest price is not the best price in the interest of the procuring entity, because competitors, in order to win, are naturally brought to offer less than what should be needed for a good performance. Therefore, the contract so awarded frequently does not have the expected success.

#### ***5. The overcoming of illicit secondary considerations***

Of course, corruption has such a deep impact over institutional life, that to stop – or at least to limit it – can be considered as an absolute priority in modern democracies: yet, one can argue that the sacrifice of public interests concerned in Public Procurement is not really needed. Currently, the subjective use of the power of awarding must once again be regarded as a criminal behaviour: the “ideal” and the “local” reasons that could induce such abuse having lost importance, if not actuality. The trend to abuse of public procurement in order to struggle against the “red danger”, for example, is no longer actual, and, over all, foreign firms are no more regarded as alien (or enemy)

firms, at least in the European Union: misuse of power of awarding is therefore generally connected to selfish economic interests of the civil servants. It means that one has not to fear too much the weakening of the checks, generally brought by reason of a wide sharing of the motivations of the abuse. It seems, therefore, that criminal repression of corruption can once again be considered as reasonably efficient, and that there's hence no real need to distort the physiology of public contracts to prevent abuses.

# CHAPTER 3

## Perspectives on fighting corruption in public contracts in Italy

BY

Francesco MANGANARO

Professor of Administrative Law,  
Mediterranean University of Reggio Calabria

### *1. Corruption and administration*

This chapter aims to analyze the size of the phenomenon of corruption in Italy and its effect on the social and administrative system of the country. Secondly, we want to analyze the main administrative remedies against corruption, especially in the field of public procurement.(1)

Corruption has been defined as the “crime of the infidels”, that is the betrayal by those who should care for the public good, and who instead allow access to public benefits not due or deny public benefits owed in exchange for money or other personal utility. It is clear that corruption is often identified with clientelism or with maladministration. Although these phenomena often intersect or overlap, it should be noted that corruption has a very precise definition, outlined as a crime in the Criminal Code(2) and it is currently the subject of more specific (and contrasting) measures in the field of administrative law.

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(1) See also: D. DELLA PORTA – A. VANNUCCI, *Corruzione politica e amministrazione pubblica: risorse, meccanismi, attori*, Bologna, 1994; G. COLOMBO (ed. by), *Il sistema degli appalti*, Milano, 1995; S. SCAMUZZI (ed. by), *Italia illegale*, Torino, 1996; B. G. MATTARELLA, *Le regole dell'onestà*, Bologna, 2007; F. MERLONI – G. ARENA (ed. by), *La trasparenza amministrativa*, Milano, 2008; F. MERLONI – L. VANDELLI, *La corruzione amministrativa. Cause, prevenzioni e rimedi*, Firenze, 2010; F. MANGANARO, *L'evoluzione del principio di trasparenza*, in [www.astrid-online.it](http://www.astrid-online.it); M. SPASIANO, *I principi di pubblicità, trasparenza e imparzialità*, in M. A. SANDULLI (a cura di) *Codice dell'azione amministrativa*, Milano, 2011, 83 et seq.; M. OCCHIENA, *I principi di pubblicità e trasparenza*, in M. RENNA – F. SAIITTA (ed. by), *Studi sui principi del diritto amministrativo*, Milano, 2012, 141 ss.; F. PALAZZO (ed. by), *Corruzione pubblica*, Firenze 2011; AA.VV., *Corruzione contro Costituzione*, in *Percorsi costituzionali*, 1-2, 2012.

(2) The corruption of official duties, pursuant to Art. 318 Italian criminal code (c.p.) is when a public official or a public service operator, to commit an act of his office, receives, for himself or for a third party, money or other benefits, a payment which is not due, or accepts a promise. Rather, corruption of acts against official duties, pursuant to Art. 319 c.p. punishes a public official or a public service operator, which, for omitting or delaying or for having omitted or delayed an act of his office, or for performing or having performed an act contrary to the duties of office, receives for himself or a third party, money or other benefit, or accepts a promise.

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Therefore, we highlight some possible remedies on the side of the legality of administrative action. The fight against corruption requires both criminal sanctions and administrative measures. With regard to the latter, given the substantial ineffectiveness of system of penal repression of the phenomenon, it is necessary to formulate a homogeneous *corpus* of rules of a special anticorruption administrative law, whose purpose is the prevention and combating of corruption in an antecedent and different respect than the relative penal cases.

It would be naïve to imagine that there is a simple and final solution to fight corruption: every measure of the fight against illegality has advantages whose effects must always evaluated compared to the chameleontic nature of the corruption, which tends to adapt to the anti-corruption measures and to paralyze their positive effects. At the same time, means that would otherwise apparently favor corrupt practices can be used for opposite purposes.<sup>(3)</sup>

## 2. *Corruption in Italy*

The statistics on corruption are often inaccurate and unverifiable, considering that the phenomenon by its nature is based on the secrecy of the offense agreement between corrupt and corrupting, which derive from corruption an (apparent) advantage.

The European Union, aware of the damage that corruption causes on the economic and social development, has intervened through the Communication from the Commission COM 2011/308. According to the European estimates, the total annual cost of corruption may be € 120 billion, equivalent to 1% of GDP.

The Communication also notes that 19% of EU GDP consists of expenditure for procurement of works, goods and services, so not only is it important to the specific discipline, but should be submitted to stricter regulation all national threshold contracts that constitute 3.6% of European GDP.

In Italy, the controversial interpretation of the phenomenon is influenced by the political need to amplify or underestimate the phenomenon, and therefore there is a divergence between criminal justice data on the incidence of corruption and reports on the perception of corruption, which better show the pervasiveness of the phenomenon.

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(3) For example, in Europe the award of public loans using the lowest price mechanism has long been considered a way of facilitating collusion between enterprises; this element in Italian law has, however, proved to be a useful anti-corruptive instrument, because it in practice means that any briber receives a lower profit. On the contrary, public-private partnerships that are considered a form of consensual agreement that impedes corruption in the European system, have had the opposite effect in our legal order.

In relation to the first, the Report to Parliament 2010 produced by the Servizio Anticorruzione e Trasparenza of the Ministero della Funzione Pubblica analyzes the phenomenon from the point of view of procedural data.

From the analysis of judicial statistics it appears that in the period between 2004 and 2010, 939 complaints were submitted for the crime of corruption and 881 complaints for the crime of bribery for a total of 1,820 complaints, compared to the total of 25,537 complaints for all crimes committed against the public administration. This data suggest that there is a “hyperbolic difference” between the real figure and the data imagined, so that the crimes of corruption and bribery would be a fraction of the crimes against the public administration.

However, the judicial data are not significant, just taking into account the fact that the typical characteristic of the crime of corruption is secrecy, which allows both parties to the crime to obtain an improper advantage.

For this reason, the judicial data must be associated with the figure for the “perception” of the phenomenon of corruption, which indicates how citizens perceive the phenomenon beyond the judicial data. The most well-known statistical datum in this field is produced by Transparency International, an international organization that annually draws up a list on the perception of corruption in the world, using data from different agencies and specialized organizations. In 2011, Italy obtained a bad evaluation, ranking 69th out of 183 countries, the fourth lowest in Europe, ahead of only Greece, Romania and Bulgaria.

The OECD, in its 2011 report, recommended that Italy introduce criminal liability of legal persons and, in the awareness of the difficult emergence of the phenomenon, take protective measures for whistleblowers or those that denounce cases of corruption.

The most worrying data emerge from the annual reports of the Court of Auditors, which show a constant increase in corruption.

The report of the General Prosecutor for the year 2011 shows sadly that “quella contro la corruzione, latamente intesa, rappresenta davvero un’impari battaglia: basti pensare che, a fronte del costo plurimiliardario del fenomeno come stimato dagli organismi sopra citati, la Corte dei conti nel 2011 è riuscita ad infliggere condanne in primo grado, per soli 75.254.141,70 euro (danno patrimoniale pari ad euro 73.619.459,63 + 1.634.682,07 euro per danno all’immagine), mentre in sede d’appello sono state definitivamente confermate condanne per l’importo di euro 15.050.803,58 (danno patrimoniale pari ad euro 13.189.771,21 + 1.862.032,37 euro per danno all’immagine) relative a giudizi trattati negli anni precedenti”.

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### 3. *The report on Italy of the Group of States against Corruption (GRECO)*

The most significant analysis was carried out by a committee constituted by the Council of Europe, the Group of States against Corruption (GRECO), which analyzed the situation of individual State Parties in cooperation with the representatives of the States themselves, to identify critical aspects of national systems and suggest possible remedies. For Italy, the evaluation process began with an initial GRECO report of 16 October 2009, which contained 22 recommendations to combat the corruptive phenomenon.

On 31 January 2011, the Italian State submitted a report on measures taken to implement the recommendations of the first report. Later GRECO, with its report of 27 May 2011, assessed whether and how the 22 recommendations have been implemented or not, taking into account the report of the Italian State.

Of the twenty-two recommendations proposed, less than half have been actually implemented.<sup>(4)</sup> The recommendations *ix*, *xiv* and *xxii*<sup>(5)</sup> have been reflected in a legislative amendment, the recommendations *ii*, *iv*, *vi*, *vii*, *xii* and *xiii*<sup>(6)</sup> were treated in a satisfactory manner. The recommendations *i*, *iii*, *v*, *viii* and *xvi* have been partially implemented.<sup>(7)</sup> Instead, the recommendations *xi*, *xv*, *xvii*, *xviii*, *xix*, *xx* and *xxi* were not implemented.

(4) The data refer to a period before the approval of Italian Law 6 November 2012, No. 190.

(5) There was satisfactory implementation of *ix*, the recommendation on the control of suspicious financial transactions, because it is improved traceability of economic flows. Favorable assessment has been expressed also with respect to the recommendation *xiv*, which called for more rigidity in the rules relating to disciplinary liability of public employees, and which is being realized by the Brunetta reform and specific training programs on integrity of public administration, organized at the national level. Satisfactory measures were taken in consequence of the *xxii* recommendation on complaints of suspected cases of corruption and money laundering, including through the involvement of professional bodies.

(6) The *ii* recommendation suggested to revise Italian legislation with regard to Criminal Law Convention on Corruption. The *iv* recommendation on the need for coordination of police forces was implemented through inter-groups at national and local levels. The *vi* recommendation required a change of Italian Law No. 124 of 2008 (so-called Lodo Alfano), which was used to suspend the criminal proceedings against the Presidente del Consiglio dei Ministri, Ministri and Presidenti delle due Camere: the declaration of unconstitutionality of that law has fully satisfied this recommendation. The *vii* recommendation suggested seizure or confiscation of goods obtained through corruption and, on this point, the GRECO shows satisfaction with the measures taken by our country in the confiscation of assets of organized crime, calling for an extension of the remedy also in other cases of corruption. There was a satisfactory response to the *xii* recommendation, since the recent issue of the Code of Administrative Procedure allows a more rapid and effective protection against government. Equal satisfaction has been expressed with regard to the *xiii* recommendation, which called for the strengthening of the internal control systems in the public administration: the establishment of the Commission for the evaluation, transparency and integrity of public administrations (CIVIT), as well as the disclosure of other types of internal controls are considered positive events.

(7) With the *i* recommendation, the GRECO asked for the adoption of a plan of anti-corruption policy, now realized. The *iii* recommendation, on the implementation of a comprehensive program of specialized training for police forces, was only partially realized. The *v* recommendation asked for a statistical analysis on disputes concerning corruption extinguished by prescription, which was done only partially. There was also only a partial implementation of the *viii* Recommendation, on effective

Let us reflect only on the latter recommendations, which remained unimplemented. There is a limitation on the right of access (recommendation xi) and this would seem paradoxical in a legal system such as the Italian one, which has sought to regulate this right since 1990 with the Law on Administrative Procedure and Access.

Instead, according to the GRECO, the need to justify the request for access constitutes a restriction on the exercise of the right and also there is lack of publicity and access to the meetings of the collegial administrative bodies.<sup>(8)</sup>

There has been a critical assessment of the GRECO about the failure to implement recommendation xv, on the integrity of government members, because no measure, while promising, has been adopted in a context in which the example of absolute integrity is more necessary than ever.

The GRECO has also criticized the failure to regulate conflicts of interest (recommendation xvii) among public officials, who were left by the administration to take on private commissions that could be the subject of corrupt exchanges. Measures indicated by the government are unsatisfactory not only because they have not yet been adopted in the anti-corruption law, but also for their inherent limitations, given that they should extend much more broadly, to additional cases.

Also not satisfactory are the proposed measures regarding the protection of informants or complainants of corruption (recommendation xviii), because those measures are not sufficient to deter possible retaliation against employees and complainants in corruption cases.

Finally, the GRECO noted that no measures have been adopted to address corruption in the private sector (recommendation xix); in order to prevent those convicted of corruption of holding public office (recommendation xx); or on the strengthening and effectiveness of sanctions for firms (recommendation xxi).

The final judgment of the GRECO must make us reflect on the legislative and administrative measures to put in place. It is not enough to ratify the UN Convention against Corruption of 2009, but we must undertake the measures called for by the Council of Europe to give effect to the Criminal and Civil Law Conventions on Corruption. In addition, the GRECO noted that some questions have not yet received sufficient attention in our country: the Code of Conduct for members of the government, the prevention of conflicts of interest,

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precautionary measures by the police against the proceeds of corruption. There was unsatisfactory implementation of the xvi recommendation, which suggested clear rules of incompatibility (conflicts of interest) for all government employees, and total publicity of revenues earned by Ministers.

(8) It should be noted that the recent Italian d.lgs. 14 March 2013, No. 33, extended the right to access, now identified as civic access.

and the protection of those who denounce corruption, all of which reinforce the fight against corruption in the private sector.

The GRECO recommended not only the implementation of any unfulfilled measures, but also to give wide publicity to the measures against corruption in public opinion, in order to demonstrate the intention of the institutions to fight the corruption phenomenon.

#### ***4. Corruption in public procurement***

The first factor affecting the quantity and quality of corruption in procurement relates to the large number of contracting authorities in our country, about 30,000 with 60,000 cost centers, that according to the 2011 report of the *Autorità per la Vigilanza sui Contratti Pubblici* would be 74,000. This high number affects the system of public procurement, both with regard to overall costs and with regard to the professional incapacity that characterizes the operators of smaller contracting authorities, which are the most part. In addition, the territorial level of cost centers – usually a municipal dimension – is very near to the citizens and therefore highly susceptible to corrupt practices.

According to data provided by the *Autorità per la Vigilanza sui Contratti Pubblici*, the largest buyers, in respect to works and services, are the municipalities,<sup>(9)</sup> while in the supplies sector the first position is held by the companies of the National Health Service:<sup>(10)</sup> the amount of the value of supply contracts awarded by the latter is equal to one billion € per annum.

With regard to procurement procedures, it should be noted that the use of private negotiation has increased, i.e., the procedures in which the risk of collusive agreements is higher, and the restrictions on competition are more manifest, in works contracts<sup>(11)</sup> as in the service procurements,<sup>(12)</sup> and in supply contracts.<sup>(13)</sup>

(9) According to data provided by the Italian Authority for the Supervision of Public Contracts for works, services and supplies (AVCP) for 2011, out of a total of 22,143 notices for work in ordinary and special sectors, 11,238 were issued by Municipalities for a total amount of € 930,826,436.00, which constitutes 49.71% of the total. Consider that, in this ranking, the second-ranked buyer are the Provinces, with only 9.47% of the total amounts. With regard to procurement of services, on 50,276 notices, 13,810 were by of Municipalities for a total of EUR 850 051 290 (27.27% of the total amounts), in second place come the health service companies, with amounts at 11.32% of the total.

(10) In the supply side, the companies in the national health service, on 55,703 notices, have issued 26,077 for an amount of euro 1,558,343,944.95 (46.54% of total); in second place, municipalities held a mealy 7.36% of the overall.

(11) In particular, works contracts in the ordinary sectors amounted to less than euro 150,000, 46.3% of the total made with the negotiated procedure without prior publication of the notice, for a total amount of euro 789,957,217.12.

(12) In the procurement of services, there are direct assignments for 29% (euro 615.016,384,02) and by negotiated procedure without prior publication of the notice by 25.2% (euro 675,649,692.25), which means that more than 50% of the loans of services occurs without an open procedure.

(13) A similar situation for supply contracts, assigned directly to the 23.2% (euro 567.773.040,60) and negotiated without prior publication of the notice for an additional 23.2% (euro 696.678.951,23).

Comparing the data on contracting authorities and those on the awarding of contracts, it is very difficult to detect planning, especially on the part of those small contracting authorities that incorporate design defects which often cause disputes in the works contracts.

An appropriate solution may be the creation of a unique central purchasing body, as happened, for works contracts, in the case of the “stazione unica appaltante” created in Calabria with the regional law n. 26 of 2007, or as the similar experience of the “stazione unica appaltante” of the Provincia of Reggio Calabria, in which participating more than 97% of municipalities of the Provincia. However, if it is not possible to arrive to a similar solution, it would be very necessary to set up common planning centers, because it is in this phase that we highlight the weaknesses of the contracting authorities.

Corruption also differs by type of contract and procedure used. So, while in the case of adjudication at the lowest price, the risk is concentrated in an agreement between the enterprise and the commissioning body, in the negotiated procedure and in the supply of the economically most advantageous tender, the risk focuses on the low transparency of the award committee.

The question is obviously more complex, because sometimes the same type of contract award can produce different effects. For example, the tendering system with the criterion of the lowest price – according to some observers – limits corruption. But according to the European orientation, it is preferable the offer be the economically most advantageous (not necessarily the lowest price), although this, for the wide margins of discretion, may encourage corruption.

Another obstacle to competition, and a breeding ground for corruption, is the use of emergency administrative authority.

In practice works contracts are almost exclusively considered urgent. As mentioned, in the work in derogation one can easily find corruption, because in these areas there is an obligation to respect Community law. Areas subject to emergency administrative law are traditionally those related to natural disasters, major events and commissarial administrations.

The further problem related to the weakness of the monitoring of the actual realization of the work can be remedied by increasing checks on controllers, establishing systems of rotation of those who make the verifications. And also pressure from the civil society – as suggested by the OECD – can be a useful innovative tool.

Transparency is the general instrument, also in public procurement, for the administrative prevention and repression of corruption. Finally, the legislator provided (Article 18 of the Law, Aug. 7, 2012, No. 134) that the measures of subsidies are not effective unless they are published on the websites of

administrations. The same rule, in paragraph 5, provides that the publication is a condition of effectiveness of the legal title legitimizing the grant.<sup>(14)</sup>

A further element of difficulty is created by the link between corruption and organized crime. In the report for the inauguration of the judicial year 2012, the Procuratore Generale of the Corte dei conti pointed to an Economic Index forum report, as well as the OECD reports and GRECO, to define corruption and organized crime as the principal obstacles to economic development in Italy, especially in the South. These data are confirmed by the CENSIS in the 2010 survey, according to which 42.2% of the complaints for corruption crimes occurs with the highest density in four regions (Campania, Puglia, Calabria and Sicily).

All analyses confirm, albeit in different ways, that the fight against corruption constitutes a significant segment of policies to combat organized crime, by combating – including public opinion – that milieu of diffused illegality, which is fertile soil (albeit difficult to measure) for the growth of organized crime.

### ***5. For an administrative law on anticorruption***

The subject of administrative law on anticorruption is currently absolutely central to the Italian political debate. We must take advantage of this temporary centrality to vigorously promote the evolution of this emerging special law, whose adoption will profoundly affect the normal activities of public administrations. In this sense we must act without any further adieu, making such a law effective to all levels of government (national, regional, local), to open new modes of audit and rules against conflicts of interest, and establishing rewards to fight the widespread phenomenon of corruption.

In fact, corruption, more so when it is connected with the phenomenon of organized crime, not only represents a weak point of legality but undermines trust in the State of law, and weakens the moral conscience and collective responsibility for the common good. Therefore, any work to combat corruptive phenomenon must necessarily be multi-disciplinary, combining rules on the control of administrative law, disciplinary sanctions, amendments to Criminal Code, educational measures, paths of legality and good practices.

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(14) This rule was abrogated and represented, with the same content, by Italian d.lgs. 14 March 2013, No. 33.

## CHAPTER 4

### The Italian efforts on anti-corruption

BY

Bernardo Giorgio MATTARELLA

Professor of Administrative Law, University of Siena

#### *1. The problem of corruption in the Italian administrative law*

As is common knowledge, the notion of corruption in administrative law is different from the criminal law one. It is certainly broader than the latter, as it refers not only to criminally relevant behaviours, but also to behaviours which are sources of other types of liability or which do not expose the subject to any sanction, being nevertheless unwanted in the legal system: conflicts of interests, nepotism, clientelism, partiality, occupation of public offices, absenteeism, waste of resources.(1)

Because of the greater breadth of the administrative law notion of corruption, the administrative law strategy for fighting against corruption is also broader and more articulated. While the criminally relevant corruption is mainly fought through repression, i.e. through the imposition of more or less heavy penalties, the malfeasance relevant to administrative law is fought through organizational and procedural mechanisms, acting in the fields of administrative controls and transparency, and relying on deontology and staff training.

A good description of the administrative law strategy for preventing corruption is provided by the broadest and most original study among the works and reports published in the last 20 years, that is the work of the Study Committee on the prevention of Corruption, appointed in 1996 by the Chairman of the Italian Chamber of Deputies and chaired by Sabino Cassese.(2) In this study, five areas of intervention have been identified.

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(1) M. CLARICH – B. G. MATTARELLA, *La prevenzione della corruzione*, in B. G. Mattarella – M. Pellissero (eds. by), *La legge anticorruzione. Prevenzione e repressione della corruzione*, Torino, 2013, 60. See also: F. MERLONI – L. VANDELLI, *La corruzione amministrativa. Cause, prevenzione e rimedi*, Firenze, Passigli, 2010; F. PALAZZO, *Corruzione pubblica. Repressione penale e prevenzione amministrativa*, Firenze, Firenze University Press, 2011.

(2) With reference to the Study Committee chaired by Sabino Cassese in 1996, the related report is published in *La lotta alla corruzione*, Laterza, Roma-Bari, 1998. See also the Committee appointed by the Minister of Public Administration and presided over by Gustavo Minervini in the same year, and the

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The first area applies to the normative arrangement, as a breakdown in norms opens the door to rules which favor corruption. Remedies include the lowering of the regulatory burden, liberalization, analysis of the impact of the regulation, deregulation and codification of the rules in force.

The second area is relative to the relationships between politics and administration,<sup>(3)</sup> which have to accommodate a separation of responsibilities and reciprocal control. Rules on the financing of political activities, a more precise definition of the restrictions on access to elective positions, rules on the conflict of interests of politicians, as well as reform of political appointments have been suggested as remedies.

The third area concerns public administration, which has to be strengthened in order to react to illegalities and to resist improper pressures. Among the remedies: codes of conduct, rules on public servants' conflicts of interest, public servants' declarations of assets, definition of the relationships between the disciplinary process and criminal one, rules on the activities following the employment relationship, incompatibilities of public jobs and restrictions on career progressions, improvement of public servants' condition and recovery of public service's prestige, avoiding the interference between politics and public servants' selection and career, and strengthening of Government's technical offices.

The fourth area corresponds to administrative activities and controls, whose good functioning is essential to the guarantee of legality and integrity. Among the remedies: transparency and control of the contractual activity, transition from process controls to product controls, transparency of privatization processes and of administrative activities carried out through private law schemes.

Finally, the last area of intervention coincides with controls carried out in the private law area. In this context, the danger of illicit commerce or of a distorted use of the monitoring power looms. Among the remedies: liberalization of private activities and simplification of the monitoring procedures; contingent regulation of the lobbying activity; internal audits of the corporations.

As can be seen, the relationship between corruption and administrative law is complex and manifold in turn. Hence, the fight against corruption can sometimes be the primary interest, propelled by administrative offices and acts; sometimes that fight can be the secondary interest, which must be taken into account by the administrations. The awareness of the importance of the administrative strategy for the prevention of corruption goes together with the awareness of the insufficiency of criminal repression. Moreover, the comparison

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one appointed by the Minister of Public Administration and chaired by Roberto Garofoli in 2011 (whose report is published in *La prevenzione della corruzione. Per una politica di prevenzione*, available at [http://www.governo.it/GovernoInforma/documenti/20121022/rapporto\\_corruzioneDEF.pdf](http://www.governo.it/GovernoInforma/documenti/20121022/rapporto_corruzioneDEF.pdf)), which contributed to the elaboration of amendments to the bill that later became the law commented in this chapter.

(3) S. CASSESE, *Idee per limitare la corruzione politica*, in *Il Corriere giuridico*, 1992, n. 7, 701 et seq.

between administrative prevention and criminal repression allows one to identify a further reason why the first kind of action is important. Criminal law is suitable for individual interventions, relative to single events; it is not appropriate for fighting macro-phenomena of widespread criminality. Criminal law is the “heavy coin” of the legal system, and it must be used with parsimony. The administrative law tools must be used in a more widespread fashion.

In addition to the legislative efforts and to the activities of political institutions, the prevention-of-corruption goal gave birth to other initiatives, also in the field of public servants’ training. Among these initiatives, the activities of the National School of Administration (*Scuola nazionale dell’amministrazione*) deserve to be mentioned. In 2010, this institution launched an interdisciplinary project on integrity, with various training, research and seminary activities; furthermore, it included this subject into all the basic training courses for public officials.<sup>(4)</sup>

## ***2. The prevention of corruption in the Italian public administration through the recent law***

In Italy, the prevention of corruption<sup>(5)</sup> at the administrative level should take place in several respects, as there are many weak points allowing malpractices to enter. Remedies are largely known. Just a few examples of what would be needed: full transparency of expenditures in administrative procedures, as well as the funding of political parties; centralization of public award procedures and of open competitive exams; elimination of the spoils system; rules for direct collaboration offices; liberalizations and limitation of certain administrative discretion, above all in the processes for monitoring private activities and for dispensing benefits to individuals; strengthening of the technical and inspective offices of the administrations; codes of conduct for politicians and

(4) See also the text of the Law No. 190 of November 6th of 2012, Art. 1, par. XI, which provides that the National School of Administration has the task to prepare “paths, that may be also specific and sectorial, for the training of public administration employees on the subjects of ethics and legality. Periodically and in agreement with administrations, it provides for the training of public servants acting in the sectors where the risk of corruption is higher according to the plans adopted by the single administrations”. See also par. V, which confers to central administrations the task of defining (and transmitting to the Department of Public Service) the appropriate procedures to select and instruct, “in collaboration with the National School of Administration, the employees acting in sectors particularly exposed to corruption, providing the rotation of officials and functionaries”. B. G. MATTARELLA, *Recenti tendenze legislative in materia di prevenzione della corruzione*, available at <http://www.masterprocurement.it/ckfinder/userfiles/files/Mattarella.pdf>, 2012, 10.

(5) To see an analysis of corruption in Italy, see also A. VANNUCCI, *La corruzione in Italia: cause, dimensioni, effetti*, in B. G. Mattarella – M. Pellissero (eds. by), *La legge anticorruzione. Prevenzione e repressione della corruzione*, cit., 25. On the subject of transparency, see also in the same volume: G. M. RACCA, *La prevenzione ed il contrasto alla corruzione nei contratti pubblici*, 125 et seq. See also M. GNES, *Italy*, in *Anticorruption Strategies within the Competences of the Supreme Audit Institutions in the European Union*, London, Esperia, 2006, 283 et seq.

for each category of public servants; definition of requirements and controls for political appointments; restrictions to be applied after the expiration of the office or of the public employment relationship; protection of the individuals that denounce a bad behaviour.

The prevention of corruption has been recently regulated through a Law of the Italian Parliament.<sup>(6)</sup> Yet, a relevant deficiency can be seen in its configuration: the bill deals a lot with administrative corruption, overlooking political corruption.<sup>(7)</sup> For example, administrative transparency is mentioned,<sup>(8)</sup> but few references are made to transparency of politics and its funding system; there are rules on the offices of public servants, but not on the incompatibilities and on the conflicts of interests of parliamentarians; the regulation of the codes of conduct of public servants is reorganized, but nothing is provided about the rules of conduct of politicians. It seems that the political class, attacked and discredited, is attacking in turn: its victim is public administration.

The bill contains provisions in several fields, which can be summarized as follows.

1. First, it acts at the organizational level, (nearly) solving the problem of the competent national authority in the field of corruption. Anti-corruption authorities exist in many countries, institutionally positioned and with extremely heterogeneous tasks: sometimes they are governmental structures, sometimes they are independent; sometimes they have study or proposing functions, sometimes they have investigative ones; sometimes they have inquiry and sanctioning powers, while in other cases they have only request or advising powers. There are international agreements requesting the existence of such authority. Actually, these provisions seem to be provided above all for those countries that do not have independent and efficient public prosecutors and magistrates.

In Italy,<sup>(9)</sup> this issue was vaguely introduced in the debate in the Nineties. In 2003, the High Commissioner for prevention of and fight against

(6) M. CLARICH – B. G. MATTARELLA, *La prevenzione della corruzione*, cit., 61 e 62, which describes the legislative system introduced through Italian Law No. 190 of 2012.

(7) See also, for example, the provisions on incompatibility and on bans to confer offices (“inconfiribilità”) in public administrations and in private entities under public control, provided on the application of article 1, par. 49 and 50, of the Law of November 6th of 2012, No. 190, by the Legislative Decree of April 8<sup>th</sup> of 2013, No. 39. On this point, see: B. PONTI, *Le modifiche all’Art. 53 del testo unico sul lavoro alle dipendenze della p.a. (Art. 1, commi 39-40 e 42-43)*, in B. G. Mattarella – M. Pellissero (eds. by), *La legge anticorruzione. Prevenzione e repressione della corruzione*, cit., 167 et seq. On this subject and in the same volume, see also the contribution of F. MERLONI, *Nuovi strumenti di garanzia dell’imparzialità delle amministrazioni pubbliche: l’inconfiribilità e incompatibilità degli incarichi (Art. 1, commi 49 e 50)*, in B. G. Mattarella – M. Pellissero (eds. by), *La legge anticorruzione. Prevenzione e repressione della corruzione*, cit., 192 et seq.

(8) See also the Italian legislative decree No. 33 of 2013 and the circular of the Department of Public Service of July 19<sup>th</sup> of 2013, No. 2, on the subject of implementation of provisions on transparency.

(9) S. CASSESE, «*Maladministration*» e rimedi, in *Il Foro Italiano*, 1992, n. 9, V, 243 et seq.

corruption and the other forms of illicit practices in public administration was established.(10) This body operated since the beginning of 2005; its functions were not defined by the law and its independence was limited (the office was normally fulfilled by a prefect at the end of his/her career, appointed by the Government). In 2008 it was abolished, raising many polemics, and its functions were ascribed to an office of the Department of Public Service (namely, to the Anticorruption and Transparency Service – Saet).(11)

In 2009, the establishment of the already-mentioned CiVIT raised the question of the subdivision of competences with that office. The bill tries to solve this problem, identifying the same CiVIT as a national anticorruption authority, and ascribing new tasks and powers to it.(12) Competences remain on the Department of Public Service, above all to the end of elaboration of the strategies for prevention and elaboration of the national anticorruption plan which is introduced. The bill seems to ascribe to the CiVIT tasks of reaction (study, advice and surveillance), while tasks of initiative (coordination, scheduling, elaboration of rules) are attributed to the Department.

The law in question introduces also the plans for prevention of corruption,(13) that the national administrations shall elaborate, as well as the role of the person responsible for prevention of corruption that they have to appoint among their public officials.(14) As can be observed, these

(10) Law of January 16th, 2003, No. 3. In this law the idea materialized of establishing a national authority for fight against corruption, which had remained absent in the proposals elaborated by the study committees in the field of corruption, established in the second half of the Nineties. On this point, see also the activity of the Study Committee on the prevention of Corruption, appointed on September 30<sup>th</sup> of 1996 by the Chairman of the Italian Chamber of Deputies, and coordinated by Sabino Cassese (whose works resulted into the report published as AC, XII Legislatura Doc. CXI, No. 1 and of the Study Committee appointed through Decree of the President of the Council of Ministers of October 18<sup>th</sup> of 1996 and chaired by Gustavo Minervini. See also B. G. MATTARELLA, *Le regole dell'onestà*, Il Mulino, Bologna, 2007, 23 et seq.

(11) Italian Decree Law of June 25th of 2008, No. 112, converted by the Law of August 6<sup>th</sup> 2008, No. 1, Art. 68, par. VI, a). With reference to the establishment of the new body and to the duplication of competencies, see also M. CLARICH – B. G. MATTARELLA, *La Commissione per la valutazione, la trasparenza e l'integrità delle amministrazioni pubbliche nel panorama della autorità indipendenti*, in G. Scognamiglio (ed.) *Il nuovo ordinamento del lavoro pubblico e il ciclo della performance*, Promo P.A. Fondazione, Roma, 2010, 139 et seq. See also G. SCIULLO, *L'organizzazione amministrativa della prevenzione della corruzione (art. 1, commi 1-4)*, in B. G. Mattarella – M. Pellissero (eds. by), *La legge anticorruzione. Prevenzione e repressione della corruzione*, cit., 71 et seq.

(12) Italian Legislative decree of October 27th of 2009, No. 150, Art. 13.

(13) Italian Law of November 6th of 2012, No. 190, Art. 1, par. V, VI e VIII. On the plans for prevention of corruption, see F. DI CRISTINA, *I piani per la prevenzione della corruzione (art. 1, commi 5-14)*, in B. G. Mattarella – M. Pellissero (eds. by), *La legge anticorruzione. Prevenzione e repressione della corruzione*, cit., 91 et seq.

(14) Italian Law of November 6th of 2012, No. 190, Art. 1, par. VII. In relation to powers and duties of the person responsible for the prevention of corruption, see Dipartimento della Funzione Pubblica, January 25<sup>th</sup> 2013, No. 1, on the provisions for prevention and repression of corruption and illegality in public administration.

documents do not replace the plans for transparency and integrity and the other instruments provided by the in-force legislative decree No. 150 of the 2009. On the contrary, they are added to these existent instruments, therefore imposing further organizational and procedural obligations to the administrations. Some provisions are specifically referred to the local entities, to which the regulation is extended. The mechanism arranged by the law is similar to the mechanism of liability of legal entities, as provided by the legislative decree No. 231 of 2001: whenever certain crimes are committed, the person responsible for the prevention of corruption is liable at the revenue and disciplinary level, unless he or she provides evidence of having put in place the obligations provided by the law, as well as of having monitored compliance with the plan.<sup>(15)</sup>

2. The bill intervenes on a second subject: administrative transparency, which is definitely an excellent instrument to fight against corruption, although recently it has been overemphasized, misinterpreted or overestimated. In this regard our legal system, although in a confused and not-so-aware fashion, carried out a transition which was accomplished also by other legal systems: the transition from the right of access, defined as the right of the individuals to access documents or information inhering to them, to the publicity of information that the administrations shall disclose to all the citizens, without any need of request. The most general rules in this respect are provided by the Law No. 15 and by the Decree No. 150 of 2009. These acts establish the rule of full publicity of all the information concerning the organization and the activity of the public administration.<sup>(16)</sup> This formulation is very broad, resulting in vague and difficult application in the short term. Inevitably, this provision has not been implemented until now. Hence, it is not surprising that many other legislative provisions introduced, in the last years, more specific obligations of publicity for the administrations, providing for publication of information which is already included in the mentioned general provision. The law adds some further precise provisions, but these are too many, so it is difficult for the administrations to understand which provisions they should apply. For this reason, the bill conveniently contains a legislative mandate to reorganize the regulation of the obligations of publicity, transparency and diffusion of the information by the

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(15) Italian Law of November 6th of 2012, Art. 1, par. XIV.

(16) Italian Legislative decree of March 14th of 2013, Art. 1, par. I. The recent regulation provides for obligations of publicity, transparency and diffusion of information by the side of public administrations and identifies obligations of transparency concerning the organization and the activity of public administrations and the modalities for its fulfilment, defining transparency “as complete accessibility of the information concerning the organization and the activity of public administrations”. See also Art. 9 relative to information published by public administrations on websites.

side of public administrations (implemented through legislative decree No. 33 of the 2013). In cases like these, rationalization is needed to make provisions cognisable and effectively executing.

3. The bill intervenes also in the field of public management, with the declared aim of guaranteeing impartiality in the exercise of the administrative functions and of strengthening separation between and reciprocal autonomy of the political bodies and the administrative ones. These necessities have been stated in the first half of the Nineties and heavily harmed by several national and regional legislative interventions in the following 15 years. In order to re-state them, several further regulatory interventions are needed, especially in the field of the appointment of public officials. Recourse to external subjects should be avoided or at least limited drastically. This recourse should have allowed the introduction in the public sector of very professional managers from the private sector, but it was used improperly. Several articles of the bill contain provisions in that regard, introducing restrictions on the possibility to confer offices to certain subjects, as well as transparency instruments in relation to those offices.

Further provisions concern the codes of conduct in the public sector.<sup>(17)</sup> A Code of conduct for the employees of public administrations has existed since 1994; at present, it is included in the single act on public employment, issued through the legislative decree No. 165 of 2001. This decree establishes that a violation of the Code of conduct may be relevant for disciplinary liability, according to the provisions of collective agreements; furthermore, it provides for the possibility for single administrations to adopt specific codes, for all their employees or for certain categories. The law intervenes on two aspects. On the one hand, it makes the liability regime heavier, establishing that its violation always causes disciplinary liability and – under certain conditions – also civil, administrative and accounting liability. On the other hand, it states that each administration shall – not may – adopt its own code of conduct.

A short but important article of the bill aims at introducing in the legal system a specific protection for the so-called whistleblowers, i.e. those who

(17) See the recent Decree of the President of the Council of Ministers, of March 8<sup>th</sup> 2013, containing the Code of conduct of public servants under Art. 54 of the legislative decree of March 30<sup>th</sup> of 2001, No. 165, Art. 3. With reference to the duties of public servants, see in doctrine: S. CASSESE, *L'etica pubblica*, in *Giornale di diritto amministrativo*, 2003, 1097 et seq.; G. M. RACCA, *Disciplina e onore nell'attuazione costituzionale dei codici di comportamento*, in F. Merloni – R. Cavallo Perin (eds. by), *Al servizio della Nazione. Etica e statuto dei funzionari pubblici*, Milano, 2009, 250; R. CAVALLO PERIN – B. GAGLIARDI, *Status dell'impiegato pubblico, responsabilità disciplinare e interesse degli amministrati*, in *Dir. amm.*, 2009, 1 et seq.; B. G. MATTARELLA, *Le regole dell'onestà*, Bologna, 2007, 131; V. CERULLI IRELLI, *Etica pubblica e disciplina delle funzioni amministrative*, in F. Merloni – L. Vandelli (eds. by), *La corruzione amministrativa. Cause, prevenzione e rimedi*, cit., and in the same volume: G. SIRIANNI, *I profili costituzionali. Una nuova lettura degli articoli 54, 97 e 98 della Costituzione*, 130. In relation to the outline of the evaluation of public officials, see also S. PONZIO, *La valutazione della qualità delle pubbliche amministrazioni*, Roma, 2012, 108 and 109.

denounce crimes committed in the public administration. In other experiences, the whistleblowers receive even a prize. The law provides only for the prohibition of penalties as well as of discriminatory behaviours, with specific provisions protecting the privacy of the denouncing person's identity.

One last issue deserving to be pointed out is the "incandidabilità", i.e. inability to access certain elective offices for individuals that have been condemned for certain crimes.(18) This notion of ineligibility, as known, works like general ineligibility; the difference is that it depends on the unworthiness of the individual and not on the possibility that he (or she) influences voters. At present, the ineligibility in the first meaning is provided only for local administrators, but not for national parliamentarians. This is the reason why individuals with even rather heavy criminal records often sit in the Parliament, while they could not be elected in a city council. The bill contains a legislative mandate for the reorganization of the subject, including the opportune introduction of that notion of ineligibility also for national and European parliamentarians.

Further provisions are relative to the following subjects: arbitration in litigations where public administration is involved; conflicts of interests and external offices of public servants; offices that cannot be conferred to individuals convicted for certain crimes; activities particularly subject to risks of criminal infiltration; fiscal damage resulting from corruption crimes; periods of leave of the magistrates and lawyers of the Government; liability for lack of compliance with the terms of the procedure.

Further in-depth analysis should be conducted on the regulation and experience of specific sectors or subjects that, for various reasons, are more harmed by corruption, or that are strategic for its prevention. These sectors are, in particular: public procurement, administrative controls, public health and local government. Specific attention should be paid to prevention of and fight against corruption in these sectors, because of the economic relevance exposing them to corruptive pressures. For this reason, the Study Committee appointed in 2011 by the Minister of Public Service decided to focus on some sectors and to write on these sectors part of its final report.(19)

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(18) Legislative decree of April 8<sup>th</sup> 2013, No. 39.

(19) The Committee appointed by the Minister of Public Service has been chaired by Roberto Garofoli. The report made by the Committee has been published in *La prevenzione della corruzione. Per una politica di prevenzione*, available at [http://www.governo.it/GovernoInforma/documenti/20121022/rapporto\\_corruzioneDEF.pdf](http://www.governo.it/GovernoInforma/documenti/20121022/rapporto_corruzioneDEF.pdf).

**CHAPTER 5**  
**Fighting corruption in public procurement:**  
**the case of Romania**

BY

Bogdana NEAMTU

Associate Professor, Babes Bolyai University

Dacian C. DRAGOS

Professor, Babes Bolyai University

***1. Introduction***

The chapter discusses corruption in public procurement in Romania, one of the newer member states of the EU, which faces significant challenges in this area. While corruption in public procurement is not a problem faced only by transition countries, the scope of the phenomenon and the implications for the absorption of the EU Structural Funds is tremendous. The chapter has the following structure: Section one focuses first on corruption as a systemic societal problem in the countries of Central and Eastern Europe and highlights the characteristics of this endemic phenomenon in order to better assess the context against which certain anti-corruption strategies are implemented. It then focuses on describing corruption in the field of public procurement in Romania, indicating specific risks for our country. Section two focuses on a specific instance of corruption in public procurement in Romania, namely conflicts of interest. We decided to focus on it because it is among the most common and widespread problem identified in different studies. The section offers a detailed analysis of the legal and institutional framework in place regarding conflicts of interest and focuses on a newly created policy that it is hoped will limit conflicts of interest, especially in public procurement that is financed from the EU Structural Funds. Section three analyzes transparency as a strategy for reducing corruption in public procurement and focuses on the role played by SEAP, the Romanian Electronic System for Public Procurement. It then explains how a recent policy of the government concerning open data could enhance transparency in public procurement by providing more systematic and user-friendly data. The chapter ends with conclusions which emphasize that governments have

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a variety of tools at their disposal to promote integrity in public procurement. In the case of Romania most problems are due not to the legislative and institutional framework but rather to implementation; thus, policy solutions regarding the fight against corruption need to be designed with this concern in mind.

## ***2. An overview of corruption in public procurement in Romania***

### **2.1. Corruption as a systemic problem in the CEE countries and Romania**

A number of studies on corruption<sup>(1)</sup> carried out in Central and Eastern European (CEE) countries during the past decade suggest medium to high levels of corruption, which casts an unfavorable light on the countries of this region, linking them to the position of the developing countries in Africa, Asia or South America.<sup>(2)</sup> By the same token, corruption in the CEE countries is perceived as greater than what exists among the OECD countries.<sup>(3)</sup> While some countries in the region have been successful in implementing effective anti-corruption reforms (some of the EU members which entered the Union in 2004, including the Baltic States), others, such as Romania and Bulgaria, still struggle to comply with EU requirements regarding anti-corruption measures and rule of law standards.<sup>(4)</sup>

Various corruption indexes compiled by international organizations confirm this situation. According to the Corruption Perception Index (CPI) by Transparency International, the best-ranked countries in the region (Estonia and Slovenia) are placed in the 60-69 score interval. However, the same countries have experienced in recent years a worsening of the corruption level as measured by CPI.<sup>(5)</sup> An even gloomier picture is depicted if one analyzes another instrument used by Transparency International, namely

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(1) A. GRØDELAND, *Informality, Corruption and Public Procurement in The Czech Republic, Slovenia, Bulgaria and Romania*, 2005, Norwegian Institute of Urban and Regional Research, available at <http://www.unpcdc.org/media/4428/european%20union%20anti-corruption.pdf>, accessed November 1st, 2013.

(2) A. KOTCHEGURA, *Reducing Corruption in Post-Communist Countries*, in *International Public Management Review*, 2004, 5(1), 152.

(3) R. SPROUT, *An Overview of Corruption in Central and Eastern Europe & Eurasia*, 2002, 1, available at <http://resources.transparency.bg/download.html?id=201>, last accessed October 14, 2013.

(4) OECD, *Anti-corruption Reforms in Eastern Europe and Central Asia: Progress and Challenges, 2009-2013, Fighting Corruption in Eastern Europe and Central Asia*, OECD Publishing, 2013, 14-15.

(5) Transparency International, *Corruption Perception Index reports for years 20110-2013*, available at <http://www.transparency.org/research/cpi/>, last accessed November 13, 2013.

the 2013 Corruption Barometer. In many countries from the CEE region, more than 50% of their populations estimated that the level of corruption increased over the last two years. This holds true even for countries that were traditionally considered at the forefront of the anti-corruption movement (Estonia 47%, Slovenia 62%, Hungary 61%, etc.). Not only do citizens perceive corruption as increasing, they also regard the anti-corruption strategies of their governments as highly ineffective (Czech Republic 72%, Slovenia, 77%, Lithuania 79%, etc.).<sup>(6)</sup> The conclusion of the 2013 'Nations in Transit' report by Freedom House, entitled *Authoritarian Aggression and the Pressures of Austerity*, is also a gloomy one with regard to corruption in the region. The report claims that corruption in the Balkan states is increasing, and that the CEE countries have failed to strengthen the judiciary and to limit the influence that political interests and personal connections between government and business have in the area of public procurement and privatization of state owned assets/companies.<sup>(7)</sup> The first EU anti-corruption report issued in February 2014 states that for most countries, the ranking of the CPI index tends to correspond to answers given by the Eurobarometer respondents. While various countries from the CEE region experience different challenges with regard to corruption, the countries lagging behind in the scores concerning both perceptions and actual experience of corruption include Croatia, the Czech Republic, Lithuania, Bulgaria, Romania and Greece. In these countries between 6% and 29% of respondents indicated that they were asked or expected to pay a bribe in the past 12 months, while between 84% and 99% think that corruption is widespread in their countries. In the same vein, corruption is most likely to be considered a problem when doing business by companies in the Czech Republic (71%), Portugal (68%), Greece and Slovakia (both 66%).<sup>(8)</sup>

In order to understand corruption in the CEE countries, a distinction needs to be made between state capture and administrative corruption.<sup>(9)</sup> State capture refers to the actions of both private sector and public sector actors which strive to shape the formation of laws and regulations – the very 'rules' of the game, through illicit payments and/or other benefits

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(6) Transparency International, *Global Corruption Barometer 2013*, available at <http://www.transparency.org/gcb2013/report>, last accessed November 13, 2013.

(7) Freedom House, 2013 report, *Authoritarian Aggression and the Pressures of Austerity*, available at <http://www.freedomhouse.org/sites/default/files/NIT%202013%20Booklet%20-%20Report%20Findings.pdf>, last accessed November 13, 2013.

(8) European Commission, COM(2014) 38 final, Report from the Commission to the Council and the European Parliament, *EU Anti-Corruption report*, 6-7, available at [http://ec.europa.eu/dgs/home-affairs/e-library/documents/policies/organized-crime-and-human-trafficking/corruption/docs/acr\\_2014\\_en.pdf](http://ec.europa.eu/dgs/home-affairs/e-library/documents/policies/organized-crime-and-human-trafficking/corruption/docs/acr_2014_en.pdf), last accessed February 10, 2014.

(9) World Bank, *Anticorruption in Transition: A Contribution to the Policy Debate*, The World Bank, Washington, D.C., 2000, xv-xvii.

to public officials. Specific examples include the ‘sale’ of Parliamentary votes and presidential and executive decrees to private interests; the sale of civil and criminal court decisions to private interests; corrupt mishandling of central bank funds through illegal contributions by private actors to political parties.(10) Administrative corruption occurs when public official exact unofficial payments and/or other benefits from firms and individuals in exchange for favoritism in the allocation of licenses, permits, public service or tax relief. Familiar examples of administrative corruption include ‘grease payments’ as bribes to gain licenses, to smooth customs procedures, to win public procurement contracts; misdirection of public funds under administrators’ control for their own or their family’s direct financial benefit.(11) In public procurement we are most likely to encounter administrative corruption, though state capture is also possible – interest groups may lobby/bribe MPs in order to adopt weaker conflict of interest regulations, for example.

What distinguishes corruption in Central and Easter Europe, irrespective of its forms, is its systemic/endemic character. There are numerous studies which try to explain the causes of corruption in terms of the communist legacy – informal networks and personal contacts were important in the context of product scarcity; or in terms of cultural values that exist within these societies – they developed as neo-traditionalist societies, through the imposition of communism on traditional rural societies, governed by unwritten rules rather than formal laws.(12) Failures to address systemic corruption in the region are due to a lack of genuine political will, lack of leadership and consistent, targeted action against corruption, as well as ongoing political changes. Declarative support of political leaders for anti-corruption reforms needs to be matched with concrete reforms and enforcement/sanctions mechanisms.(13)

Among the countries from the CEE region, Romania, oftentimes together with Bulgaria, is considered to be lagging most behind in the anti-corruption fight. The problem is not so much the lack of a proper legal and institutional framework but rather the implementation process, which becomes the missing link.(14) Very often, state of the art legislation, policies and institutions do not translate into reduced levels of corruption.

(10) World Bank, 2000, *op. cit.*, xvi.

(11) *Ibid.*, xvii.

(12) A. MUNGIU-PIPPIDI, *Hijacked Modernization: Romanian Political Culture in the 20th Century*, *SUDOSEUROPA*, 2007, 55(1), 33.

(13) OECD, *op. cit.*, 25-26.

(14) W. N. DUNN – K. STARONOVA – S. PUSHKAREV, *Implementation: The Missing Link*, in W. N. Dunn – K. Staronova S. Pushkarev (eds. by), *Implementation: The Missing Link in Public Administration Reform in Central and Eastern Europe*, Bratislava, NISPAcee, 2006.

## 2.2. Corruption in public procurement in Romania: Areas of concern

Public procurement is commonly seen as the government activity most vulnerable to waste, fraud and corruption due to its complexity, the size of the financial flows it generates and the close interaction between the public and the private sectors.<sup>(15)</sup> In this section data from various international and national studies and reports documenting the extent of corruption in public procurement are presented, with a main focus on the case of Romania.

According to the 2013 flash Eurobarometer survey on corruption relevant to businesses,<sup>(16)</sup> more than three out of ten (32%) companies in the Member States that participated in public procurement say corruption prevented them from winning a contract. Within the CEE countries, more than half of company representatives say this has been the case (Bulgaria -58%, Slovakia - 57%, Cyprus - 55%, and the Czech Republic - 51%; for Romania - 43%). Studies done on population samples as opposed to businesses portray, however, a different and gloomier picture in the case of Romania. A 2005 survey done by World Economic Forum on a sample of 125 countries placed Romania among the last 25 countries (together with Cameroon and Madagascar) concerning the frequency of bribery and additional payments in public procurement. At that time Romania was the only EU or candidate country to be placed on such a poor ranking while most of the EU member states, with consolidated democracies, were among the best 25 performers.<sup>(17)</sup> A recent survey done at the national level shows that 88% of the Romanian population believes that contracts are not awarded in a fair and transparent manner.<sup>(18)</sup>

Table 1 below presents some of the corrupt practices in public procurement that are most widespread in Romania. As one can see from the data, more of the described practices are thought to be more widespread in our country than in the EU (average of the EU 27 Member States).

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(15) OECD, *Fighting Corruption in the Public Sector/OECD Principles for Enhancing Integrity in Public Procurement*, available at <http://www.oecd.org/>, last accessed November 1st, 2013.

(16) 2013 Flash Eurobarometer, 374.

(17) OECD, *Integrity in Public Procurement – Good Practice from A to Z*, OECD Publishing, 2007.

(18) IPP, National Survey on Public Procurement, September 2013, available at (in Romanian) <http://ipp.ro/library/IPP%20ACHIZITII%20PUBLICI%201.pdf>, last accessed December 1st, 2013.

Table 1: Most widespread corruption practices in public procurement in EU member states and Romania

|   |         | Widely wide-spread % | Fairly wide-spread % | Fairly rare % | Very rare % | Non-existent % | Don't know % |
|---|---------|----------------------|----------------------|---------------|-------------|----------------|--------------|
| Specifications tailor-made for certain companies                                      | EU 27   | 23                   | 34                   | 18            | 4           | 1              | 20           |
|   | Romania | 15                   | 44                   | 11            | 3           | 8              | 21           |
| Conflicts of interest in the evaluation of bids                                       | EU 27   | 17                   | 37                   | 19            | 6           | 1              | 20           |
|   | Romania | 21                   | 36                   | 12            | 4           | 6              | 21           |
| Collusive bidding   | EU 27   | 16                   | 36                   | 18            | 6           | 1              | 23           |
|   | Romania | 17                   | 36                   | 12            | 5           | 5              | 25           |
| Unclear selection or evaluation criteria  | EU 27   | 17                   | 34                   | 21            | 6           | 1              | 21           |
|   | Romania | 16                   | 40                   | 13            | 6           | 5              | 20           |
| Involvement of bidders in the design of specifications                                | EU 27   | 13                   | 35                   | 19            | 5           | 1              | 27           |
|   | Romania | 10                   | 39                   | 11            | 5           | 5              | 30           |
| Abuse of negotiated procedures  | EU 27   | 13                   | 34                   | 21            | 7           | 1              | 24           |
|   | Romania | 10                   | 35                   | 20            | 5           | 7              | 23           |
| Abuse of emergency grounds to justify use of non-competitive or fast-track procedures | EU 27   | 14                   | 32                   | 21            | 7           | 1              | 25           |
|   | Romania | 11                   | 40                   | 18            | 6           | 5              | 20           |
| Amendments of the contract terms after conclusion of the contract                     | EU 27   | 15                   | 29                   | 23            | 9           | 1              | 23           |
|   | Romania | 19                   | 24                   | 21            | 7           | 7              | 22           |

Source: 2013 Flash Eurobarometer 374, data set for Romania, available at [http://ec.europa.eu/public\\_opinion/flash/fl\\_374\\_fact\\_ro\\_en.pdf](http://ec.europa.eu/public_opinion/flash/fl_374_fact_ro_en.pdf)

In the same vein, a 2013 study<sup>(19)</sup> assessing the costs of corruption in public procurement in eight EU member states (Romania included), shows that the most encountered form of corruption in public procurement in Romania is kickbacks. They are defined in the mentioned study as referring to situations when the public official demands, or is open to, a bribe which will be accounted for in the tendering process, including administrative processes. Another country similar to Romania in this respect is Spain. Conflicts of interest and bid rigging are also present in our country.

For Romania (and Bulgaria) the reports of the European Commission under the Cooperation and Verification Mechanism are perhaps the best source offering a longitudinal perspective on the evolution of corruption in public procurement. The accession to the EU of Bulgaria and Romania in 2007 led to the creation of this novel monitoring instrument, called the Cooperation and Verification Mechanism (CVM), in an attempt to trigger reform by extending EU leverage into the post-accession period.<sup>(20)</sup> While by 2005, the eight post-communist states that joined the EU in 2004 were, on average, indistinguishable from the EU's old member states on measures of political rights and civil liberties,<sup>(21)</sup> the situation was rather different for the two countries which joined the EU in 2007 – Bulgaria and Romania. In addition to a less favorable start than the other neighboring countries, Bulgaria and Romania, after almost two decades since the collapse of the communism, were still facing challenges in the area of the independence of the judiciary, corruption, and state capacity.

CVM works in a rather straightforward way. Before accession, two sets of benchmarks were established by the European Commission for the two countries. Romania's progress will be judged against four benchmarks while Bulgaria's progress will be judged against six benchmarks. Three out of the four benchmarks established for Romania directly concern the fight against corruption, integrity in public office and prevention of conflicts of interests. Every six months the Commission issues a monitoring report evaluating progress on the established benchmarks and highlighting the most pressing issues/red flags that should be addressed before the next report. These reports are rather detailed, addressing with specific country examples corruption problems or problems

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(19) PwC EU Services, Ecorys and University of Utrecht, *Public Procurement: Costs We Pay for Corruption. Identifying and Reducing Corruption in Public Procurement in the EU*, 2013, available at [http://ec.europa.eu/anti\\_fraud/documents/anti-fraud-policy/research-and-studies/pwc\\_olaf\\_study\\_en.pdf](http://ec.europa.eu/anti_fraud/documents/anti-fraud-policy/research-and-studies/pwc_olaf_study_en.pdf), last accessed November 1st, 2013.

(20) M. A. VACHUDOVA – A. SPENDZHAROV, *The EU's Cooperation and Verification Mechanism: Fighting Corruption in Bulgaria and Romania after EU Accession*, Swedish Institute for European Policy Studies, 1, available at <http://www.sieps.se/en/publikationer/the-eu%E2%80%99s-cooperation-and-verification-mechanism-fighting-corruption-in-bulgaria-and-romania-after-eu->, accessed November 1st, 2013.

(21) *Ibid.*, 2.

regarding the reform of the judiciary. The main reports are usually published in July while the interim technical reports are published in February.

If one scrutinizes the CVM reports starting with 2010(22) (before this year references to public procurement are very limited or missing) there are several common ideas present. First, all reports state that progress seems very limited in the prevention and sanctioning of corruption related to public procurement. The Commission has noted several times that the progress made against high-level corruption in general has not been matched in public procurement. Second, almost all reports address similar shortcomings, including: frequent changes of the legal framework and an institutional set-up that lacks sufficient capacity, as well as the absence of key instruments for effective controls such as a comprehensive register of public tenders; weak protection of public procurement against conflict of interest – few cases of conflict of interest are pursued in public procurement, and even when pursued in court, sanctions in this area are not dissuasive; limited instances when the cancellation on the grounds of conflict of interest of projects/procurement contracts that have already been executed is possible; court cases in this area take a long time (partly due to the need for specific financial expertise) however this leads to the particular problem of contracts concluded before court judgment on the offence. Third, in the recent reports, emphasis is placed on creating ex-ante verifications in order to detect conflicts of interest in the early stages of the award procedure. This can be done by providing the National Agency for Integrity (ANI) with responsibility in this area.

CVM reports draw also on studies and policy papers drafted by national NGOs and think tanks working in the area of transparency in the public sector, democracy and openness in government, etc. Such reports include for example a study from 2009 by the Romanian Academic Society (SAR),(23) and a 2012 report by the Institute for Public Policies (IPP).(24) These studies include empirical research carried out in this field, as well as various ‘famous’ cases of corruption, which have drawn media publicity.

Public procurement procedures in Romania are highly dysfunctional and sometimes corrupt especially in the absorption of Structural Funds. Recent studies(25) point out how extensively corruption affects the spending of Euro-

(22) These reports are available on the European Commission’s website at [http://ec.europa.eu/cvm/progress\\_reports\\_en.htm](http://ec.europa.eu/cvm/progress_reports_en.htm).

(23) SAR Policy Brief no. 43, O evaluare a eficienței, integrității și transparenței sistemului de achiziții publice în România [An evaluation of the efficiency, integrity, and transparency of public procurement in Romania], available at <http://www.sar.org.ro/files/paper-final.pdf>, last accessed on January 30, 2014.

(24) IPP, *Transparency, Fairness and Competitiveness of Public Procurement in Romania. Case Study: Central Contracting Authorities*, 2012, available at [www.ipp.ro/profiles.php?IDfile=151](http://www.ipp.ro/profiles.php?IDfile=151), last accessed on January 30, 2014.

(25) M. FAZEKAS – J. CHVALKOVSKA – J. SKUHROVEC – I. J. TÓTH – L.P. KING, *Are EU funds a corruption risk? The impact of EU funds on grand corruption in Central and Eastern Europe*, in European Research Centre for Anti-Corruption and State-Building, Working Paper no. 39, 2013, available at

pean Union (EU) funds across many new and old member states. The authors argue that in the context in which EU funds amount to 1.9%-4.4% of annual member state GDPs and well above 50% of public investment, even if only a fraction of these amounts is impacted by corruption, the negative effects are likely to be considerable. ERAWATCH, the European Commission's information platform on European, national and regional research and innovation systems and policies, under the heading public procurement for innovation, listed three causes that lead to corruption in the spending of EU Structural Funds.<sup>(26)</sup> While the first cause mentioned is generally applicable to corruption in public procurement in Romania, the next two directly concern the spending of EU money: corruption and complex, unstable and unclear regulations of the public procurement legislation; large numbers of institutions overseeing the management of Structural Funds, with dense bureaucracy and extensive paperwork; delayed payment by the state of outstanding invoices raised by contractor firms leading to blockages of the contractor's cash liquidities.

In June 2013 the Romanian government responded to the requests and critiques coming from the European Commission and adopted a joint ministerial order<sup>(27)</sup> regarding the approval of the guide comprising the main risks identified in the field of public procurement, and citing the recommendations of the European Commission which need to be followed by the management authorities and intermediary organisms in the process of verifying public procurement procedures. The order addresses ten major risks as well the strategies used to mitigate them. These risks are briefly presented below.

- Unjustified shortening of deadlines as a result of the publication of notice of an intention to purchase. The shortening of deadlines in this case is possible only if the intention notice comprises, similarly to a participation notice, all the information regarding qualification and selection criteria, as well as the award criterion.
- Use of an accelerated award procedure. This can be done only if the emergency situation is clearly justified by the contracting authority and it is not connected to its own fault (e.g., because of delays in nominating the members of the evaluation commission). The shortening of deadlines for a specific stage needs to be correlated with the length of all the other stages of the procedure.

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*[http://www.againstcorruption.eu/wp-content/uploads/2013/11/wp39\\_eufunds\\_corruptionrisk\\_cee2.pdf](http://www.againstcorruption.eu/wp-content/uploads/2013/11/wp39_eufunds_corruptionrisk_cee2.pdf)*, last accessed on January 30, 2014.

(26) ERAWATCH, Romania/Policy Mix/Other Policies, available at *[http://erawatch.jrc.ec.europa.eu/erawatch/openems/information/country\\_pages/ro/country?section=PolicyMix&subsection=OtherPolicies](http://erawatch.jrc.ec.europa.eu/erawatch/openems/information/country_pages/ro/country?section=PolicyMix&subsection=OtherPolicies)*, last accessed on January 30, 2014.

(27) *Order 543/2.366/1.446/1.489/1.441/879/2013*, published in the Official Journal of Romania, Part I, no. 481 from 01.08.2013.

- Publication of discriminatory, insufficiently detailed, or incomplete qualification/selection criteria. Most often contracting authorities are breaching the law by requesting similar experience in a very specific type of activity (e.g., construction of schools as opposed to construction of all types of buildings), certificates that are not relevant for carrying out the contract (ISO 9001 from producers) or unreasonable means of proof for complying with a certain qualification criterion (invoices attesting the turnover for a specific time interval).
- Use of the award criterion ‘the most economically advantageous tender’ with the inclusion of irrelevant or unquantifiable evaluation factors. Often contracting authorities use factors that are not linked to the subject matter of the contract and do not bring an obvious advantage for the authority. Also, the evaluation factors and methodologies often offer room for subjective interpretations due to the way in which they are drafted (level of understanding of the information from the award documentation).
- Automatic exclusion of the lowest tender. This is often done based on the justification that such a low price will most likely generate problems during the execution of the contract. The contracting authority has the obligation to thoroughly investigate the basis of the financial offer before deciding the exclusion of a tenderer.
- Modification of the participation notice through clarifications and not through the publication of an *erratum*. The publication of an *erratum* means that the changes are published in the national electronic system for public procurement (SEAP) and, depending on the value of the contract, in JOUE. Thus, all economic operators have access to the modified information.
- Rejection of the request of economic operators to prolong the deadline for submitting the tender. Often contracting authorities set the minimum deadline from the law without correlating its length with the complexity of the contract and the time economic operators need in order to draft their tenders. Contracting authorities should also avoid setting short deadlines which in addition overlap with holidays.
- Requests for clarifications during the evaluation of the tenders which are made in a discriminatory manner and with the intention to favor certain tenderers.
- Mandatory information missing from the communications regarding the result of the award procedure.
- Unreasonable time intervals established for the evaluation of tenders/ negotiation of changes to the contract. For rejected candidates and rejected tenders (unacceptable or non-compliant) as well as for the

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tenderers who submitted acceptable and compliant tenders but did not win the tender, the contracting authorities need to clearly explain their decisions and to indicate the deadline for lodging a complaint.

### ***3. Conflicts of interest as a specific instance of corruption in public procurement in Romania***

#### **3.1. Assessment of the problem**

As already discussed in the previous section, conflicts of interest represent one of the most widespread forms of corruption in public procurement in Romania. In March 2013, while attending the conference ‘Combating criminality in the field of public procurement, an operational approach’ (organized by Freedom House Romania with the final support of EU – DG Home Affairs), Horia Georgescu, president of the National Agency for Integrity, declared that, according to an internal study conducted by the Agency at the level of local and county authorities, conflicts of interest are no longer controlled by the state authorities due to a legal framework which is outdated and does not match the challenges from practice. According to the study, 78 elected officials at the local level were found to have received/gained public money via public procurement corrupt practices, and the estimated prejudice accounts for more than 8 million Euros.(28)

A somewhat similar signal came in 2011 from the National Agency for Regulating and Monitoring Public Procurement (ANRMAP), which, in a press release, warned contracting authorities that issues concerning conflicts of interest will in the future be the object of all verifications initiated during monitoring/supervising procedures, as well as at the level of the award documentation sent to SEAP. This warning was triggered by a shocking discovery made at a hospital from Targu Mures. The hospital concluded in 2011 two contracts for the provision of goods with the same economic operator. The sole shareholder and legal representative of the said economic operator was the mother of one of the members of the evaluation commission. In order to disguise this conflict of interest, the economic operator used a fake document during the qualification stage which attested that the shareholder/legal representative was a different person than the mother of the employee of the contracting authority.(29)

(28) Evenimentul Zilei, Head of ANI: The Phenomenon of the Conflict of Interests in Public Procurement is out of Control. Intention: To Detect Conflict of Interests in Real Time, by A. Etes and V. Fotache, March 20, 2013, available at <http://www.evz.ro/detalii/stiri/seful-ani-fenomenul-conflictului-de-interese-in-achizitiile-publice-este-scapat-de-sub-co-10289.html>, last accessed on January 30, 2014.

(29) ANRMAP, Press release, 21 November 2011, available at <http://www.anrmap.ro/comunicat/conflictul-de-interese-procedurile-de-achizi%C8%9Bie-publica>, last accessed January 5, 2014.

Significant problems regarding conflicts of interest are especially found in the area of public procurement financed from the EU Structural Funds. They represent in the case of Romania the main deficiency identified by the audit missions of the European Commission in 2012. At that time the problems generated by conflicts of interests in public procurement led to the pre-suspension of payments under three operational programs (OPs), and a warning for a fourth one. Some of the main problems identified included: (30) a) With regard to the OP for Enhancing Economic Competitiveness, the conflict of interest regarded the relationship between the companies/entities which evaluated the projects and the consultants who took part in the drafting of these projects. b) With regard to the OP for Transportation, all public procurement contracts were verified, but especially those concluded by the Railroad Company and the Highways and Roads Company. Problems identified concerned a poor control of the award procedures, fraud suspicions, as well as red flags regarding possible conflicts of interest. c) With regard to the Regional PO, conflicts of interest were discovered within public procurement procedures concerning contracts for regional and local infrastructure. More specifically, the conflicts of interest regarded the relationship between local authorities and the entrepreneurs. d) With regard to the OP Environment a warning and a request were launched regarding the establishment of a special procedure for avoiding conflicts of interests.

Since conflicts of interest represent a key fraud strategy of public procurement contracts financed under EU Structural Funds projects, specific indicators were identified and described by the European Commission. Among these were: inexplicable favoring of a certain tenderer or provider; continuous acceptance of works at a high price and low quality; the responsible person with the award procedure does not fill out the declaration regarding conflicts of interest; the responsible person with the award procedure refuses to quit his/her responsibilities regarding a certain contract and to take over similar ones; there are clues that the responsible person with the award procedure undertakes parallel activities. (31)

### 3.2. Legal framework and its effectiveness

In the field of conflicts of interest, the legal and institutional framework has been constantly updated and changed in the last years, in order to make the anti-corruption fight more effective. The section below examines these changes with an emphasis on the challenges that are still present.

(30) Available at [http://www.euractiv.ro/uniunea-europeana/articles|display Article|articleID\\_25687/LINKS-DOSSIER-Modificarile-legislative-in-problema-conflictelor-de-interese-pericol-iminent-pentru-fondurile-europene.html](http://www.euractiv.ro/uniunea-europeana/articles|display Article|articleID_25687/LINKS-DOSSIER-Modificarile-legislative-in-problema-conflictelor-de-interese-pericol-iminent-pentru-fondurile-europene.html), last accessed on January 30, 2014.

(31) ANRMAP, *Best Practices Guide in the Field of Public Procurement regarding Project Financed from Structural Instruments*, Draft, 2014, 125, available at <http://www.anrmap.ro/sites/default/files/poat/2460.pdf>, last accessed on February 4, 2014.

### 3.2.1. Applicable national legal acts

At the national level, conflicts of interest in public procurement are regulated by a broad set of legal provisions, all of which can be grouped into three major categories:

- a) Legislation applicable to all public procurement (Emergency Government Ordinance (EGO) No. 34/2006, the framework act regarding the award of public procurement contracts, of works and services concessions; Government decision (GD) No. 925/2006 for the approval of application norms of the provisions concerning the award of public procurement contracts as regulated by EGO 34/2006; Order No. 170/2012 regarding the interpretation of Art. 69<sup>1</sup> from EGO 34/2006)
- b) Legislation applicable to public procurement within the framework of projects financed from EU Structural Funds (Order 543/2.366/1.446/1.489/1.441/879/2013 regarding the approval of the guide comprising the main risks identified in the field of public procurement and of the recommendations of the European Commission which need to be followed by the management authorities and intermediary organisms in the process of verifying public procurement procedures; EGO No. 66/2011 regarding the prevention, identification and sanctioning of wrongdoings in obtaining and using European funds and/or public national funds that are complementary to the European ones; GD no. 875/2011 regarding the approval of the methodological norms for the application of the provisions from EGO No. 66/2011). With regard to the provisions that apply only for EU financed public procurement contracts, it has to be said that they can be extended in certain cases to all public procurement contracts. For example, the provisions detailing the risks that may occur in the award of public procurement contracts and strategies to avoid them are basically generally applicable to all public procurement contracts – they are merely explaining and interpreting for contracting authorities the provisions of the framework legislation in public procurement. The provisions regarding specific obligations, at least for now, apply only to EU-financed public procurement contracts, the trend, though, at least at a declaratory level, is to extend them in the future to all public procurement contracts.
- c) Legislation regarding conflicts of interest applicable to public servants and elected officials (Law No. 161/2003 concerning certain measures for ensuring transparency in the exercise of elected positions, of public office, and in the business sector, prevention and sanctioning of corruption; Law No. 176/2010 concerning integrity in the exercise of elected functions and positions, for the modification of Law No. 144/2007 regarding the establishment, organization and functioning of ANI, as well as for the modification of other legal acts; Law No. 7/2004 regarding the Code of behavior for public servants).

It is very clear from the long list of acts applicable to the area of conflicts of interest in public procurement that a more integrated legal framework would prove to be of great help for all the actors involved in public procurement in Romania. This is in line with the recommendation of the European Commission from the January 2014 CVM report which states that ANI's efforts in the near future should be directed toward steering a codification of the integrity framework, which should also ensure that any perceived ambiguities in the current framework are removed.

### 3.2.2. Definition of conflicts of interest

National public procurement legislation does not include a precise definition of conflicts of interest; instead, the law states very clearly several situations which have the potential to indicate the occurrence of a conflicts of interest and/or unfair competition. With regard to the persons involved in verifying/evaluating the candidates/tenders, the conflict may be generated by an interest which can influence the impartiality/objectivity of those persons throughout the evaluation process (for more details on the situations leading to a conflicts of interest see the next section).

The national legislation regarding elected officials and/or public servants defines conflicts of interest, but sometimes does it in a narrow manner. Law No. 161/2003 (Art. 70) defines conflicts of interest as the situation in which an elected official or a public servant has a personal interest of a patrimonial nature which may influence the accomplishment with objectivity of his/her duties as defined by Constitution and other legal acts. It is interesting to note that this law makes reference only to the financial/material dimension of the private interest, while newer regulations in the public procurement field are broader, to include non-financial gains/benefits. Law No. 7/2004 (Art. 4/e), on the other hand, though adopted only one year after Law No. 161/2003, has a more modern interpretation of conflicts of interest. According to this law, it refers to a situation when the personal interest, direct or indirect, of the public servant goes against the public interest, affecting or having the potential to influence his/her independence and impartiality in making decisions or completing his/her duties on time and with objectivity. We need to keep in mind that some of these laws/acts are from early 2000 and the anti-corruption legislation/strategies used have made tremendous progress since then, often by responding to challenges from practice and by adapting/adopting best practices from other jurisdictions.

EGO No. 66/2011, similar to EGO No. 34/2006, does not include a definition of conflicts of interest; Art. 2/4 states that the term conflicts of interest has the meaning from the regulations/implementation guidelines in this field adopted by the EU or other international public donors. Defining conflicts of

interest by reference to EU rules is motivated by the subject matter of EGO No. 66/2011 – prevention and sanctioning of misuse of EU funds (as well as of the complementary national ones), which require greater flexibility with regard to the concepts used, in order to respond to the specific requirement of each type of fund. In light of EGO No. 66/2011, the broad definition from EU legal acts regarding conflicts of interest also apply to the Romania natural/legal persons who normally are not contracting authorities but implement EU-financed projects and have the obligation to follow the provisions from EGO No. 34/2006 when procuring goods, services, and works.

The most recent piece of legislation addressing the issue of conflicts of interest is Order 543/2.366/1.446/1.489/1.441/879/2013. According to this act, conflicts of interest should be understood broadly – conflict between the professional duties and the private interest of a public servant (or of a person acting on the behalf of a contracting authority) which may be perceived as having the potential to impede upon the impartial and objective execution of duties. In the context of this broad definition, even non-patrimonial interests have the potential to influence the behavior of a person. It is advisable for the contracting authorities to try to identify the occurrence of possible conflicts of interest early on in the public procurement process, if possible during the award procedure. Thus, *ex-ante* verification and the limitation/elimination of the risk should represent a priority. Very importantly, this piece of legislation recommends that during the verification procedures information/signals from the press should be taken into account, if known. Very often the press and the NGOs active in this field have identified situations presenting conflicts of interest.

### 3.2.3. Specific situations leading to conflicts of interest under the national legislation

Generally speaking, though it is advisable to have a broad definition of conflicts of interest, in practice contracting authorities may face challenges if they have to apply the broad definition to the specific elements of each tender. In order to mitigate this difficulty, the Romanian legislators have opted for a mixed solution: on the one hand, there are specific situations defined which automatically trigger the presumption of the existence of a conflict of interest; on the other hand, the law also describes more general situations which need to be applied to the specific elements of each tender.<sup>(32)</sup>

According to the national legislation, conflicts of interest arise at both the level of the contracting authorities and of the economic operators. In the first case certain persons cannot verify the candidates and evaluate their tenders. In the latter case, certain economic operators cannot take part in a tender.

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(32) ANRMAP, 2014, *op. cit.*, 115.

> *Situations leading to conflicts of interest for persons working for the contracting authority*

According to EGO No. 34/2006 (Art. 69) the following categories of individuals cannot be involved in the process of verifying the candidates and/or the evaluation of tenders:

- a) Persons having any type of participation or holding shares from the subscribed capital of one of the tenderers/candidates or subcontractors, or persons who are on the board of directors / management or supervisory body of one of the tenderers/candidates or subcontractors;
- b) Spouse, relative or affinity up to the fourth degree, to persons on the board of directors /management or supervisory body of one of the tenderers/candidates;
- c) Persons found to have an interest which may affect their impartiality during the verification/evaluation process of the candidates/tenders.
- d) Persons who during the exercise of their function/position within the contracting authority found themselves in the situation of a conflict of interest as regulated by Law No. 161/2003.(33)

If one examines the text of Art. 69, two important conclusions can be drawn: first, in the category of persons involved in the evaluation of tenders, the law includes the experts hired by the contracting authority and not just the evaluation commission; second, the first two situations described by Art. 69 automatically lead to a conflict of interest, while the latter two are more nuanced, requiring an assessment based on the specific elements of each tender.

The courts usually apply a rather harsh scrutiny when it comes to situations under c) and acknowledge a quite broad spectrum of situations that may lead to a conflict of interest. Thus, Bucharest Appellate Court(34) ruled that there was a conflict of interest when the expert hired to participate in the evaluation of tenders was hierarchically subordinated to the spouse of the winning tenderer. Also, Pitesti Appellate Court(35) ruled that the situation in which the son of the president of the evaluation commission was permanently/full time hired by the winning tenderer represents a conflict of interest.

(33) The following types of interest conflicts are covered under this Law: conflicts of interest in the exercise of the function of a member of the Government and of other executive functions at the level of central and local public administration; conflicts of interest regarding elected local officials; conflicts of interest concerning public servants. We are chiefly interested in the conflicts of interest concerning public servants since they are likely to be part of the evaluation commission. It includes the following instances: the public servant is asked to solve requests, to make decisions or to take part in the decision-making process regarding natural or legal persons with whom he/she has patrimonial relationships; the public servant participates in the same commission, established according to the legal requirements, with public servants who are his/her spouse or first degree relative; his/her patrimonial interests can influence the decisions he/she must make in the exercise of the public office.

(34) Civil Decision No. 652/CA from 10 July 2008.

(35) Decision no. 1615 from 19 July 2011.

> *Situations leading to conflicts of interest for economic operators*

According to the national legislation the following categories of persons cannot be candidates, tenderers, associated tenderers, or sub-contractors:

- Natural or legal persons who took part in the drafting of the award documentation, with the exception of the case when their involvement does not lead to the distortion of the competition (Art. 67 EGO 34/2006).
- Natural or legal persons who take part directly in the verification/evaluation of the candidates/tenders (members of the evaluation commission as well as the hired experts) (Art. 68 EGO 34/2006).
- Economic operators which have as members of the board of directors/management or supervisory body, or as shareholders or associates, persons who are a spouse, relative or affinity up to the fourth degree; similarly it applies to economic operators which are engaged in commercial relations with persons holding an executive position within the contracting authority. This interdiction also applies to supporting third parties (Art. 69<sup>1</sup> EGO 34/2006).

This legal provision has created over time quite a bit of confusion because of its wording. Order No. 170/2012 offers a more detailed and clear specification of all the situations possible to be encountered under Art. 69<sup>1</sup>. A first clarification was necessary regarding the meaning of persons holding an executive position within the contracting authority. Often, economic operators have argued in court proceedings that the meaning of an executive position should be interpreted in a restricted way (persons holding an executive position who are involved directly in the award procedure). Before Order No. 170/2012 was issued, courts usually ruled that such a narrow interpretation should not be made.<sup>(36)</sup> Currently Order No. 170/2012 includes among the persons holding an executive position within the contracting authority all persons who approve/sign documents issued in connection with or for the award procedure, including the persons who approve the budget of the contracting authority, needed for the financing of public procurement contracts.

Until Order No. 170/2012 was adopted, various studies<sup>(37)</sup> argued that the Romanian legislation placed an unnecessary burden regarding the prevention of conflicts of interest on the economic operators. The cited study refers to the situation in which an economic operator can be excluded from the procedure even if a minority shareholder (holding only several shares) is related to

(36) Bucharest Appellate Court, Civil decision No. 2692 from 10 November 2011.

(37) Deloitte, final report on the behalf of the European Commission/General Directorate for Regional Policy, Evaluation of the Public Procurement System from Romania, available at <http://www.sn-seap.ro/wp-content/uploads/2012/07/DG-Regio-Third-Interim-Report-Part-C-FINAL-RO-version.pdf>, last accessed January 10, 2014.

a person holding an executive position within the contracting authority. Also, the study argued that economic operators sign eligibility declarations without knowing in advance who the members of the evaluation commission are. These situations were addressed in 2012 through the provisions of Order No. 170/2012 (see next section on the obligation of the contracting authorities to publish the names of the persons holding an executive position).

A special interdiction operates for the winning tenderers after the conclusion/signing of the contract – the tenderer is forbidden to hire (the concept of hire should be understood in a broad sense), for at least 12 months following the conclusion of the public procurement contract, natural or legal persons who took part in the verification of candidates/evaluation of tenders. These persons are most commonly the members of the evaluation commission as well as the experts. Even if this interdiction is not of a conflict of interest *per se*, it is meant to discourage unethical behaviors which cannot be detected until the conclusion of the contract.

### 3.2.4. Strategies for identification and avoidance of conflicts of interest

#### > *Obligations of the contracting authorities*

The members of the evaluation commission as well as the hired experts have the obligation to sign a confidentiality and impartiality declaration based on which they agree to follow the rules meant to prevent conflicts of interest; they will also confirm in the declaration that they are not in a situation involving the existence of a conflict of interest. Also, the contracting authority uploads in SEAP, together with the award documentation, a declaration of the legal representative of the institution comprising the identification data for all persons holding an executive position within the contracting authority. The identification data required are extensive, including name, surname, date and place of birth, current address, national identification number, and the position occupied within the contracting authority by reference to his/her implication in the public procurement process. This information is not publicly available; it can be accessed only by the entities responsible to check conflicts of interest and by the unit from the Ministry of Finance having the verification task.

In response to the difficulty discussed above, of the economic operators to properly identify the persons holding executive positions within the contracting authority, the contracting authority needs to publish in the participation notice the names of all persons who approve/sign documents issued in connection with or for the award procedure, including the persons who approve the budget of the contracting authority, needed for the financing of public procurement contracts.

The contracting authority also needs to publish in SEAP the name and identification data of the tenderer(s) which submitted tenders no later than 5 days after the deadline for submitting a tender has expired.

> *Obligations of the economic operators*

The economic operators have one main obligation, namely to sign a declaration that they are under none of the situations described by Article 69 from EGO No. 34/2006. The economic operators have also the obligation to respond to a request coming from the contracting authority regarding clarifications that a conflict of interest as regulated by Art. 69 (1) is not present.

It is worth mentioning that the contracting authorities are the ones which need to have an active role in the prevention of conflicts of interest and need to act diligently. The National Agency for Regulating and Monitoring Public Procurement (ANRMAP) recommends a set of pro-active practices that can be initiated at the level of all contracting authorities. Contracting authorities can and should go as far as they feel necessary with scrutiny, even if the legal provisions in place do not establish a mandatory obligation in this sense. Some of the pro-active strategies recommended by ANRMAP include: (38)

- Contracting authority should request, as a qualification criterion, a certificate issued for the economic operators by the National Office of the Commerce Registry which offers relevant information for identifying situations regulated under Art. 67-69 (1) from EGO No. 34/2006.
- Contracting authorities should set up an internal procedure for identifying conflicts of interests, with an emphasis on those clear situations which do not require an evaluation by reference to the specific elements of an award procedure. For a limited number of persons such as the legal representative of the institution, the delegated representative, the project manager, other persons holding an executive position within the contracting authority, and the persons directly involved in the award procedure, the contracting authority should check if they have shares or are hired by the tendering entities. The verification can also include obvious connections (such as name similarities) between the persons mentioned above and the legal representative of the tendering entity. Finally, the contracting authority should check if the authority itself has some sort of participation in the tendering company.

### 3.2.5. Sanctions/remedies in case of the existence of conflicts of interest

In this section we refer to administrative sanctions from the public procurement legislation, and not to criminal penalties. There are mainly three sanctions which can occur:

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(38) ANRMAP, 2014, *op. cit.*, 123-124.

> *Replacement of the members of the evaluation commission and of the hired experts*

If, after the signing of the impartiality declaration by the members/experts of the evaluation commission, one of these members finds himself/herself in a situation described as a conflict of interest, the contracting authority has the following obligations:

- To verify/assess if a conflict of interest really exists, provided that the member/expert of the evaluation commission himself/herself notifies the contracting authority about this situation. If the contracting authority finds that the elements of a conflict of interest are present, it can proceed to replace the member/expert.
- To immediately replace the member/expert of the evaluation commission if the conflict of interest is identified and brought to the attention of the contracting authority by the Ministry of Public Finances, through a specialized control unit called the Unit for Coordination and Verification of Public Procurement (UCVAP – the Romanian acronym). Though the measure that needs to be taken by the contracting authority is similar under both circumstances, the legislature has recently intended to give more relevance to the verifications carried out by UCVAP.(39) Contracting authorities can and have in practice decided to approve the report of the evaluation commission without taking into consideration the observations of the UCVAP experts concerning the existence of a conflict of interest. In this case, the contracting authority needs to notify ANI and to send the entire dossier regarding the award of the contract. Courts have generally ruled on this matter that the contracting authority cannot ignore the UCVAP's report and proceed with the evaluation of the tenders and the award of the contract without replacing the member/expert affected by a conflict of interest.(40) An interesting question is if the exclusion of the member/expert affected by a conflict of interest is enough in order to safeguard the principles governing the field of public procurement, or the contracting authority should annul all the acts adopted during the award procedure. The answer depends upon the moment when the conflict occurs – if the member/expert did not undertake any of his/her duties then it is enough to simply replace him/her. If, however, the person affected by the conflict of interest has been involved in the drafting/adoption of certain acts, then those acts need to be annulled. It is important for the contracting authority to undertake a thorough scrutiny of all the procedures/acts affected by the conflict of interest.

(39) ANRMAP, 2014, *op. cit.*, 127.

(40) Ploiesti Appellate Court, Decision No. 1615 from 19 July 2011.

> *Exclusion of economic operators from the tender*

The national public procurement legislation establishes three main situations which should lead to the exclusion of a tenderer from the tendering procedure:

- The tenderer/associated tenderer/subcontractor who took part in the drafting of the award documentation if he/she cannot prove that his/her involvement did not limit competition.
- The candidate/tenderer/associated tenderer/subcontractor who directly participates in the process of verification of the candidates/evaluation of tenders.
- The candidate/tenderer/associated tenderer/subcontractor who has as members of its board of directors/management or supervisory body, or as shareholders or associates, persons who are spouse, relative or affinity up to the fourth degree to or are engaged in commercial relations with persons holding an executive position within the contracting authority. The exclusion of a tenderer can only be decided by the contracting authority. It cannot take place as the result of a decision during an action before the Council or the court.

> *Ineffectiveness/Annulment of the public procurement contract*

Currently, in our public procurement legislation, there is only one situation which can lead to the ineffectiveness of the contract due to the existence of a conflict of interest. It refers to a breach of the interdiction stated in Art. 70 from EGO 34/2006: the winning tenderer/economic operator (once the public procurement contract is signed and its execution starts) hires, with the aim of carrying out the public procurement contract, a natural or legal person who has been involved in the verification of candidates/evaluation of tenders, before the 12-month deadline after the signing of the contract expires. The ineffectiveness of the contract following the breach of the interdiction from article 70 is due to an immoral cause. The same sanction, for the same reason, is also established under the civil law (Art. 1238/2 from the Civil Code). Any person can request the court of law to rule the ineffectiveness of the contract due to an immoral cause. Until the legislative changes introduced by Law No. 193/2013 (starting with July 1<sup>st</sup>, 2013), in addition to the economic operators who took part in the award procedure, the National Agency for Regulating and Monitoring Public Procurement (ANRMAP), also may request a court of law to rule a contract as ineffective, based, among other things, on a breach of provisions concerning conflicts of interest. The CVM report on Romania from January 30, 2013(41)

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(41) European Commission, COM(2013) 47 final Report from the Commission to the European Parliament and the Council On Progress in Romania under the Co-operation and Verification Mechanism, 11, available at [http://ec.europa.eu/cvm/docs/com\\_2013\\_47\\_en.pdf](http://ec.europa.eu/cvm/docs/com_2013_47_en.pdf), last accessed on 22 January, 2014.

mentions the problem of the public procurement legislation in Romania which does not contemplate a possibility of a cancellation on the grounds of conflict of interest of projects that have already been executed. This problem should be seen in a broader context, as described in the CVM report: cases seem to take a long time, partly due to the need for specific financial expertise, leading to the particular problem of contracts concluded before court judgment on the offence (therefore a remedy/sanction such as ineffectiveness after the execution of the contract is relevant); the penalties for officials involved in fraudulent public procurement cases continue to be very low; there are also major doubts on the effectiveness of prosecutors' handling of these cases.

### 3.3. Recent developments: Enhancing the role of ANI in identifying and preventing conflicts of interest in public procurement

As demonstrated by the previous section, changes to the legal framework governing conflicts of interest in public procurement have been made in the last years (and with more rapidity in 2012 and 2013). The current framework however needs at this point a complete makeover, as suggested by the ANI president (see previous section). The legal and institutional framework in place can no longer be improved to provide additional gains in the fight against corruption.

What is needed for this significant make-over? Recently, the newly issued CVM report on Romania from January 22, 2014<sup>(42)</sup> focused, in the context of continuous vulnerability of public procurement procedures to corruption, on the need to pay more attention to the prevention side, including early detection of conflicts of interest through an ex-ante verification procedure of conflicts of interest. This implies an integrated framework and the cooperation between ANI, the national entity involved in monitoring and sanctioning conflicts of interest in Romania and ANRMAP, the body responsible for monitoring procurement procedures. According to the ANI's president, public procurement will become, in the near future, an important component of the institution's activity. The CVM report mentioned earlier offers a preview of what this framework should look like. First, potential conflicts of interest should be identified and avoided in advance, before contracts are signed. Thus, a legal obligation on contracting authorities to respond to problems identified by ANI will be important to make the system work. Also important would be a provision that, if the contract went ahead and the ANI ruling was confirmed, the official in conflict of interest would be liable for a minimum portion of the cost of the contract. Of course, a new law is needed, including provisions such as the

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(42) European Commission, COM(2014) 37 final, Report from the Commission to the European Parliament and the Council On Progress in Romania under the Co-operation and Verification Mechanism, available at [http://ec.europa.eu/cvm/docs/com\\_2014\\_37\\_en.pdf](http://ec.europa.eu/cvm/docs/com_2014_37_en.pdf), last accessed on January 30, 2014.

immediate cancellation of a contract when a decision on a conflict of interest becomes final, more controls at the stage of appointment, and easier access to declarations of interest.

How it will be done? Horia Georgescu, the president of ANI, briefly explained at a recent conference how the system will become operational and what legal changes are needed for this.<sup>(43)</sup> Within the framework of the Electronic System for Public Procurement (SEAP), a new integrity declaration will be introduced. This form will target all individuals holding executive positions in the contracting authorities and will be processed by the inspectors from ANI. If during the award procedures and up until the conclusion of the public procurement contract, a conflict of interest is identified, ANI will issue an integrity warning for the head of the contracting authority and the person suspected of being under a conflict of interest. ANI will get the integrity forms via SEAP – when an award procedure is initiated, the uploading of the integrity forms represents a precondition for moving ahead with the procedure. In the near future, ANI with other interested actors in the area of public procurement will define the affected executive positions in the public institutions. It is not clear yet if contracting authorities will have to comply with ANI's decision or the warning will have only a consultative/informative role. The contracting authorities will however need to inform ANI if they followed it or not. In case of non-compliance with the warning, ANI will have the option of taking its warning and possible conflicts of interest to the other entities that are part of the integrity and anti-corruption institutional framework.

ANI currently receives money under an EU-financed project (PREVENT) in order to develop this ex-ante verification procedure and the needed institutional framework. While initially the system will apply to EU-financed contracts, the policy-makers envision its extension to all national public procurement contracts. Further on, while this system targets only contracting authorities, it could be extended to include the economic operators as well. For this more cooperation with ANRMAP is needed.

#### ***4. Transparency as a precondition for integrity in public procurement: some evidence from Romania***

In the fight against corruption, transparency-related measures/legal provisions are considered crucial because corruption thrives on secrecy. Transparency, especially in the form of e-procurement, is often described as a strategy for curbing corruption in the area of public procurement. In this section we will

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(43) Expert Forum, Challenges and Solutions for Improving the Institutional and Legal Framework for Public Procurement in Romania, available at <http://expertforum.ro/provocari-si-solutii-pentru-imbunatatirea-cadrului-legal-si-institutional-privind-achizitiile-publice-din-romania/>, last accessed February 4, 2014.

focus on the Romanian Electronic System for Public Procurement (SEAP) and on the way in which it is believed to contribute to better transparency in public procurement. We also examine some empirical evidence concerning the proactive role of contracting authorities in making their public procurement more open and transparent for the general public through electronic means.

#### 4.1. Legal framework in place

In the previous section we described the numerous changes made to the legislation on conflicts of interest in the area of public procurement. As opposed to conflicts of interest, transparency has benefited over the years from a rather stable legal framework. EGO No. 34/2006 includes broad publicity requirements for all public procurement contracts, irrespective of their value – as opposed to other countries,(44) even for small value contracts publicity requirements need to be complied with through SEAP (for more details see next section).

Breaches to the transparency obligation regard mainly: a) publicity requirements, and b) more broadly, the principle of transparency throughout the entire public procurement procedure. With regard to a), contracting authorities artificially split contracts in order not to comply with publicity requirements and/or to be able to directly choose a preferred economic operator. Also, private entities, which carry out projects financed from EU money, fail oftentimes to comply with publicity requirements.(45) In the past, though not so much nowadays, contracting authorities failed to send to SEAP the award notice of certain public procurement contracts – very often such a requirement was seen as a mere formality despite the fact that ANRMAP and the courts have stated that it is crucial for the validity and legality of the procedure as a whole. With regard to b), contracting authorities, when using the award criterion the most economically advantageous tender, fail to clearly detail the criteria used for evaluation and the methodology/algorithm. Contracting authorities also fail to include in the communication of the results of the award procedure all the elements required by law – most often the ‘losing’ tenderers are not properly informed about the reasons why their offers were not chosen. Transparency is also breached when contracting authorities fail to respond to clarifications regarding the award documentation within the timeframe set by the law (3 days).(46)

One interesting question refers to what can be accomplished through using transparency/broad publicity and what requires different types of instruments.

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(44) For example in Germany for small value contracts publication of the participation notice can be done in regional/local newspapers. For more information see D. DRAGOS – R. CARANTA (eds. by), *Outside the EU Procurement Directives – Inside the Treaty?*, DJOF Publishing, Copenhagen, 2012.

(45) Expert Forum, *op. cit.*

(46) ANRMAP, 2014, *op. cit.*, 90-91.

Both policy makers (for example DLAF, the agency from Romania similar to OLAF) and NGOs active in this field have noticed that despite compliance with publicity requirements, at the local level contracting authorities seem to make deals with preferred economic operators. They arrived at this conclusion due to huge differences in the price paid by different contracting authorities for similar goods. The solution in this case is not more publicity/transparency but rather a mechanism through which the maximum price which can be paid for a certain service is set in advance by the monitoring bodies/by law.(47)

With regard to projects financed through the EU Structural Funds, breach of the transparency obligations/principles can bring financial corrections of up to 100% of the value of the contract.(48) In a recent research it was estimated that at the end of 2012 the value of financial corrections for projects financed from 4 operational programs due to breach of transparency provisions accounted for 3% of all corrections applied.(49)

#### 4.2. Faking transparency through e-procurement and internet publicity?

SEAP is without doubt one of the few successes of the Romanian government in the area of developing an information-based society and enhancing e-government in our country. Below is a short presentation of SEAP, based on information provided by the company which developed this system.(50)

SEAP was launched in 2002 and it was considered a unique solution in this part of the world for e-procurement; it was also among the first systems for e-procurement worldwide. SEAP was launched as a pilot project under the name of 'e-market'. From 2002 to 2005 a total of 470,000 procurement procedures had been carried out through this e-market. At the end of 2006 SEAP (the extended version of e-market) was launched. Currently the system functions under the form of a single web portal called e-licitatie.ro. Also starting in 2000, the legal framework supporting this system was created with the goal to carry out all public procurement through e-licitatie.ro (online or offline).

According to the company which developed SEAP, the system has the capacity to support thousands of users connected simultaneously, and access

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(47) IPP, 2012, *op. cit.*, 58; Expert Forum, *op. cit.*

(48) EGO no. 66/2011 regarding the prevention, identification and sanctioning of wrongdoings in obtaining and using European funds and/or public national funds that are complementary to the European ones.

(49) IPP, Association of Municipalities from Romania, and Tuca, Zbarcea & the Associates, Notes for Determination of Errors and for Establishing Financial Corrections in Projects Financed from EU Structural Funds, available at <http://www.ipp.ro/library/IPPConcluziicorectii.pdf>, last accessed on February 4, 2014.

(50) TotalSoft, SEAP, available at [http://www.totalsoft.ro/dezvoltare\\_software\\_seap](http://www.totalsoft.ro/dezvoltare_software_seap), last accessed on January 14, 2014.

to the system is based on digital certificates. It can be accessed by a variety of users: contracting authorities, tenderers, ANRMAP, the public at large. However, only the contracting authorities can initiate public procurement procedures within the system.

The system allows contracting authorities, after the publication of participation notices, to choose the type of procedure they want to follow – classic or electronic. SEAP allows for various types of public procurement procedures to be carried out by contracting authorities: direct procurement (from online catalogues), requests for quotation carried out on-line as well as off-line; open procedures and e-auctions.

The role of the system is to manage all the notices involved in the public procurement procedures, allowing for the publishing in the system of various types of notices: intention notice, participation notice, award notice, contest notice, result of the solution contest, concession of works or services, and erratum type notice. Importantly, all types of notices are in the format designed by JOUE and starting with January 1<sup>st</sup>, 2007, SEAP was recognized as OJ Sender – all notices above the EU thresholds are automatically sent from SEAP to JOUE.

The system also includes a notification mechanism which allows the participating actors to the system to receive information daily or weekly based on their certain pre-defined interest criteria. Economic operators for example could be notified concerning the public procurement procedures during the last 24 hours for certain products based on the CPV code.

Available data on the functioning of SEAP speak about the impact the system has had since its launching in 2002. Thus, from 2002 to 2011, 1,681,917 public procurement procedures finalized with a winning tender were registered in the system. The total amount for these procedures is 7,388,432,851 Euros. There were a total of 306,388 catalogue products published in SEAP, and the number of notices sent to JOUE is above 45,000.

However, the information presented above portrays just the bright side of the story (which cannot be denied). Studies done by NGOs as well as numerous blogs of practitioners, lawyers, and economic operators involved in public procurement show the dark side of SEAP.

Despite the fact that EGO No. 34/2006 required the use of SEAP for the publicity of all award procedures, as well as for carrying out a certain percentage of public procurement procedures through electronic means (at least 40% from the total value of finalized procurement contracts during one year), SEAP is perceived more as a punishment than as a support tool by the contracting authorities.<sup>(51)</sup> This is why despite the legal provisions in place,

(51) Vass Lawyers, SEAP can do better, February 2nd, 2011, available at <http://www.vasslawyers.eu/ro/articole-de-specialitate/seap-poate-si-mai-bine/>, last accessed on February 4, 2014.

there are public procurement contracts operated outside SEAP. A Romanian research think tank estimates that the value of public procurement operated outside SEAP accounts for 5 to 10 billion Euros. This is happening however in a context in which the estimated value of public procurement carried out through SEAP accounted for 15 billion Euros in 2012, an increase by 50% compared to 2009 and 2010.<sup>(52)</sup> Sometimes numbers can be misleading because in the last years the number of procedures carried out entirely online has increased but the value of these contracts is low.

When referring to the challenges encountered while using SEAP we need to make a distinction between those users which use SEAP in order to participate in public tenders (contracting authorities, economic operators, and the monitoring bodies) and the public at large. The challenges leading to reduced transparency in public procurement and the solutions are different for each situation.

For users the barriers limiting access to SEAP include:<sup>(53)</sup> registration to the system is cumbersome, for it cannot be done exclusively on-line, and involves documents sent by mail to the operator of SEAP; the requirement to use a digital signature (not all economic operators have it); a different electronic format depending on the complexity of the procedure – small value contracts should have fewer requirements; lack of clear procedures for situations when the entire public procurement procedure is carried out online – the members of the evaluation commission cannot separately fill out the evaluation report and thus cannot have a dissenting opinion (very often the solution is to fill out additional off line reports); unequal technical and human resources especially at the level of small local authorities; fees associated with the use of the system, etc. Policy solutions should target each of these barriers with an emphasis on creating additional “rewards” for using SEAP, more training, no additional costs (free digital signature, no fees for using the system) as well as solving the technical problems of the system (frequent interruptions, help desk which answers slowly/never answers, upload of certain documents too slow and time consuming, etc.).

The public at large can be generally interested in various categories of information that concern the public procurement process – both aggregated data about public procurement in general as well as specific, individual public procurement procedures. The absolute quantity of information comprised in SEAP is huge but not conducive for research purposes. The system does not organize information in such a way as to facilitate the access of an interested person to all the documents

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(52) IPP (Institute for Public Policy), Sustainable Public Procurement in Romania: Executive Summary, available at [www.ipp.ro/protfiles.php?IDfile=207](http://www.ipp.ro/protfiles.php?IDfile=207), last accessed on February 4, 2014.

(53) Vass Lawyers, *op. cit.*

concerning a certain public procurement procedure. Data regarding the initial stages of the procedure – participation notice, award documentation, then the award notice, and further on the contract signed by the contracting authority – are not in one place. The system does not offer the possibility to perform queries concerning the information stocked. One cannot perform for example a search based on CPV codes and associated public procurement procedures. There is no uniformity with regard to similar categories of information which are available in SEAP, which can be misleading for less knowledgeable users. Finally, while SEAP offers a variety of information on contracting authorities, it does not offer similar data regarding the way in which certain economic operators execute public procurement contracts. Some contracting authorities have argued that it would be important if SEAP could offer information especially with regard to poor performing economic operators.<sup>(54)</sup>

With regard to transparency, we also tried to look in our research to whether contracting authorities act proactively in disseminating information concerning their public procurement. For this we looked at the websites of all ministries and to a sample of 150 municipalities at the national level. We tried to identify if certain elements which can increase transparency are present.

- One element that should be present on the website is the annual plan for public procurement. This is a strategic planning tool documenting the needs of the contracting authority. In a previous study,<sup>(55)</sup> done on a sample of central authorities, it was concluded that most of them did not publish online the annual plan. At the time we conducted our research the situation has somewhat changed, in the sense that almost all ministries have such plans published online (in certain cases even the updates to the plan were available). We need to make a distinction however between the initial plan and the public procurement contracts that were actually concluded. Sometimes, in a misleading manner, we have on the web just the initial plan and not the way in which the funds were actually spent. At the level of the local contracting authorities the situation is different – only 20 municipalities in the sample published their annual plans (for 2012 or 2013) online.
- Publication of participation notices, of award notices, etc. At the level of the ministries, most of them publish both participation as well as award notices. At the local level the situation is more diverse; we found that contracting authorities use a variety of strategies to fake transparent behavior: in several cases (see the city of Dej for example) on the website there is a section dedicated to the publication of various notices from the public procurement procedure, however instead of actual docu-

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(54) IPP, 2012, *op.cit.*, 42-43.

(55) *Ibid.*, 44.

ments there is a message stating that they are available in SEAP; other authorities (city of Bistrita), mark a procedure as completed through the award of the contract, but when trying to access the award notice one gets instead only the participation notice; some authorities publish only participation notices for certain types of procedures (city of Iasi only for open outcry auctions for parking places which require the presence of those interested at a certain date/hour). As a general observation we can state that even in cases when publication of notices is done, the user has a difficult time to navigate through the websites of the public authorities. Some have separate sections dedicated to public procurement; others list this information under transparency/public interest documents while others place it under various headings (very often counterintuitive).

- Publication of the signed public procurement contracts. This is still the exception rather than the rule. At the level of the local authorities from the sample we found such contracts published only in one case – the city of Cluj Napoca. Even in this case it is hard to estimate if the modifications to the initial contract (if any) are included in the published document. Earlier studies found this to be also the case even when individuals requested the contract under Law 544/2001 on access to public sector information which states in art. 11 that the contracting authority should provide the requester with the public procurement contracts.

Our empirical research, which goes along the lines of previous studies done by NGOs/think tanks, has a two-fold conclusion. First, some progress has been made since the previous studies were carried out. However, the progress made mainly concerns data about the award procedure up to the conclusion of the contract, data which are available as well in SEAP. Data regarding the execution of the contract are missing and are not available in SEAP. This is one area in which the contracting authorities could prove that they are transparent by publishing on their own motion online the signed public procurement contract, its annexes, additional acts, etc.

It has to be mentioned that these conclusions are very much in line with previous studies done in Romania regarding access to information and transparency.<sup>(56)</sup> While legal provisions are somewhat complied with, very little is done with regard to a pro-active approach toward transparency. While we acknowledge that certain goals can be accomplished by strengthening and enhancing implementation of the transparency principle, in the realm of public procurement other measures and mechanisms are needed.

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(56) D. C. DRAGOS – B. NEAMTU – B. COBARZAN, *Procedural Transparency in Rural Romania: Linking Implementation with Administrative Capacity?*, in *International Review of Administrative Sciences*, 2012, 78(1), 134-1. 57.

### 4.3. Recent developments: Transparency through open data

As described in the previous section, the main problem with SEAP vis-à-vis transparency is that it does not provide to the general public/interested researchers/NGOs the information on public procurement contracts in a user-friendly manner. This section describes a recent strategy/tool proposed by the government in order to improve this situation.

The Romanian Government, through the Government Program 2013-2016, decided to establish under the direct coordination of the Prime Minister the Department for Online Services and Design. Among other responsibilities, the Department will manage various efforts and activities aimed at offering a variety of open data about the activity of public institutions which are part of the central public administration. Among the sets of data currently available, are data on public procurement 2007-2013 generated from SEAP. The role of the portal [data.gov.ro](http://data.gov.ro) is to empower citizens to identify, download and use sets of public data generated or owned by public administrations. Developed on the principles of transparency, participation, and collaboration, the portal was modeled following similar models from the United States and the UK.<sup>(57)</sup>

It is important to note that if at the beginning of 2013 Romania ranked 45 in the Open Data Index (created by Open Knowledge Foundation for the OGP Summit 2012), at the end of 2013 our country ranked 15 – the improvement in the ranking was mostly due to the Open Data portal and its integration into the European Open Data portal.<sup>(58)</sup>

### ***5. Instead of conclusions: What strategies should the Romanian government promote in order to fight more effectively against corruption in public procurement?***

As documented by the EU CVM reports from the last years as well as by NGOs and think tanks, corruption in public procurement in Romania continues to be a major problem, despite otherwise significant progress made in the fight against corruption. Policy makers and legislators are faced in this context with a difficult task: to identify the best strategies for curbing corruption in this area. Until now, one could divide the strategies used by the Romanian government into two main categories: legal and institutional provisions that target directly various forms of corruption (for example conflicts of interest); and the use of a precautionary approach in the field of public procurement, meant to

<sup>(57)</sup> Available at <http://data.gov.ro/about>, last accessed on February 4, 2014.

<sup>(58)</sup> Romanian Government, Open Government Partnership (OGP) available at <http://ogp.gov.ro/noutati/romania-in-primele-15-tari-din-lume-in-open-data-index/>, last accessed on February 4, 2014.

limit possible corrupt strategies of contracting authorities and economic operators alike (for example a very low threshold for direct procurement, which was increased to 30,000 Euros only recently; overregulation/gold-plating in the case of below the EU thresholds contracts, etc.). This chapter focused on strategies pertaining to the first category and the main findings seem to suggest that:

- Legislation cannot be further improved – most of the gaps with the existing provisions at EU level/other advanced democracies have been closed. Of course, fine tuning in certain areas is still possible, but legislation has pretty much exhausted its potential to be a trigger in the anti-corruption fight in public procurement.
- Strategies at this point should target legislative implementation and simplification, as well as integrated institutional frameworks. These are needed because a fragmented legal and institutional framework creates implementation loopholes that are exploited by the corrupt actors participating in public procurement.
- Where anti-corruption strategies based on transparency fail, other mechanisms meant to limit behind the curtain agreements between contracting authorities and economic operators should be established.
- It appears that stronger sanctioning mechanism provide an incentive for all actors to behave in a legal way. This is documented by recent developments with regard to projects financed from the EU Structural Funds. An extension of such provisions to all public procurement contracts might prove beneficial.



## CHAPTER 6

### The criminal repression of corruption in public procurement of Tunisia

BY

Ridha JENAYAH

Professeur, Faculté de droit de Sousse (Tunisie)

#### 1. Introduction

Public procurement(1) is, without any doubt, one of the sectors most vulnerable to corruption. Risks of collusion arising between public and private interests in the system of public procurement, as well as the considerable weight of public procurement operations in the economic life,(2) explain the persistence of corruption practices in this field. The prejudice possibly resulting for the community broadly justify the reinforcement of the criminal repression arsenal.

This concern was already perceptible in the *Ancien Régime*. The preamble of the law of May 23th 1998 containing modifications to the Penal Code (PC) highlighted that “*le projet de loi vise à incriminer les comportements frauduleux violant les principes de l’achat public*”.(3) The 2008 ratification by Tunisia of the United Nations Convention against Corruption (UNCAC) reinforced the formal adhesion of former managers to this fight.(4)

After the Revolution of January 14th 2011, the imperative of public administration integrity became a key issue in the public debate.(5) The downfall of the authoritarian and corrupted regime of Ben Ali disclosed the extent of fraud in public procurement that the *Rapport public de la Commission nationale d’investigation sur les pratiques de corruption et de malversation* (CNIPCM) in the *Ancien Régime* only confirmed.(6)

(1) Decree No. 2014-1039, March 13, 2014, on the regulation of Public Procurement (JORT No. 22-2014, 68).

(2) Public Procurement represents approximately 18% of Tunisia’s GDP. V. OCDE (2013), *Examen de l’OCDE du cadre d’intégrité dans le secteur public en Tunisie*, 69.

(3) Law 23 May 1998, No. 33. See R. KHEMAKHEM, *Les crimes de corruption dans la loi du 23 mai 1998*, in *RJL*, No. 6, June 1998, 11-84.

(4) Merida Convention, 31 October 2003 as ratified by the law No. 2008-16, 25 February 2008.

(5) See A. JENAYAH, *Intégrité et lutte contre la corruption dans les marchés publics en droit français et tunisien*, dissertation for “Master 2 recherche en droit public des affaires”, Université Paris1, Panthéon-Sorbonne, Paris, 2013.

(6) The national Investigative Commission on corruption and embezzlement (*Commission nationale d’investigation sur les pratiques de corruption et de malversation*, CNICM) has been settled by the law-decree No. 2011-7, 18 November 2011 to investigate on corruption practiced in the Ancien Régime.

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During the period following the Revolution,(7) new institutions fighting against corruption appeared.

However, social relationships, stakeholders' behaviours and political culture are not without consequences on penal weapons. At this level, we should admit that the new managers remain reluctant to promote a coherent penal system allowed to efficiently repress frauds in public procurement. The will to keep dominance on the beginning of prosecutions and the persistent weaknesses of the incrimination system explain the disappointing results in the fight against corruption in public procurement.(8)

## ***2. Specificities of criminal law for procurement contracts***

In a rule-of-law State, the existence of an open and adequate system of recourse before an independent and impartial judge is essential to ensure compliance with the rules on public procurement. These rules aim at preserving public procurement integrity. Repression of their violation should maintain the balance between public and private interests at stake.

### **2.1. Administrative and criminal liability in the field of government procurement**

In administrative law, the concepts of Administrative fault "*faute de service*" and duty of obedience "*devoir d'obéissance*" are essential to determine the basis and limits of administrative liability of public officials. However, these norms have not any effect on public procurement criminal law, as "*fautes de service*" may well be considered as offenses under criminal law.(9)

Administrative fault and criminal offence in public procurement: Public procurement is subject to a set of rules with different origins and finalities. Some of them, of administrative nature, have the objective of sanctioning violations of the integrity obligation that burdens on public officials. Some others, of penal nature, aim at sanctioning fraudulent practices that may cause prejudice to the public interest. Complexity of the repression process, which is made ineluctable by the coexistence of various irregularities, makes improvement of the criminal repression system essential to the fight against corruption.

Under criminal law, the dominant principle is legality of crimes and penalties: crimes have to be strictly defined by law and no one can be indicted for an action

(7) M. R. JENAYAH, *Constitution et Révolution*, Inaugural lecture at the 18<sup>th</sup> session of the International Academy of Constitutional Law (*Académie Internationale de Droit Constitutionnel*, AIDC) *Le droit constitutionnel d'exception*, Tunis, July 2012.

(8) Transparency International, *Corruption Perceptions Index*, 2012.

(9) Cf. R. CHAPUS, *Droit administratif général*, Tome -I, 15<sup>ème</sup> éd., Montchrestien, 2001, 1529.

that is not considered as an offense in a law text. This characteristic première explains why the criterion of imputation of the fault to the service, which in administrative law is essential to exempt the public official from any liability,(10) does not operate under criminal law. The consequence is that, contrary to general principles of administrative liability, the existence of a connection between the official's action and the service is not very important. Criminal liability of public officials can be involved even if the condemned action is an administrative fault.

However, public procurement law is in antinomy with the supply strategy admitted under private law. Contrary to customs occurring in commercial relationships between private persons, public officials are not free to discuss tenders with a determined supplier, as they are subject to a set of rules aimed at preserving the integrity of public procurement: freedom of access to public procurement, equality of treatment among candidates, transparency of procedures and good management of public funds.(11) As a result, criminal liability of a public official can arise for the mere violation of rules governing the signing or execution of a public procurement contract. The incrimination following violation of these rules is the main characteristic of public procurement criminal law.

Duty of obedience and public procurement frauds: a public procurement contract is a complex administrative operation implying collaboration of many people called to intervene in every stage of the contracting cycle. So that these individuals are capable of being pursued under criminal law, it should be shown that the reproached action had a decisive influence in the decision making process. Thus, individuals competent of concluding or approving the conclusion of a public procurement contract on behalf of the Government, a territorial community or a public company are firstly concerned. Officials acting under their authority and intervening decisively in public procurement are also concerned. Nonetheless, article 42 of the PC provides that the individual who acted by virtue of an order of competent authority is not liable under criminal law.

The duty of obedience imposed by article 6 of the general statute of public service(12) justifies without any doubt this solution. However, the question of criminal liability arises every time that the public official carries out an evidently illegal order capable of seriously damaging a public interest. In administrative law, jurisprudence assumes that in this case the subordinate must refuse to perform the instructions of his superior in rank with the risk

(10) About the issue of Administrative fault, see M. R. JENAYAH, *Droit administratif*, 2<sup>ème</sup> éd., CPU, Tunis, 653-655.

(11) The fundamental principles regarding the execution of public procurements were taken by Article 6, decree No. 2014-1039, March 13, 2014, on the regulation of public procurements. These principles have acquired a constitutional rank in virtue of the Conseil constitutionnel statement No. 59-2006 (JORT No. 16 of 23 February 2007, 565).

(12) Law No. 1983-112, 12 December 1983, regarding the main principles governing the public function (JORT No. 82, 13, 16 December 1983, 3214).

of involving his own personal liability.(13) Yet, the extent of this rule remains uncertain, due to the absence of clear rules in the PC.

### 3. Weaknesses of the system of proceedings

Complexity of the corruption system in the field of public procurement imposes the improvement of a deterrent effect and the extension of investigation powers.

#### 3.1. The need to improve the means of detection of corruption

The main obstacle to the fight against fraudulent practices in public procurement is to gather the information that fraud authors try to hide from justice's eye.

Information by Institutional Interlocutors: at first there are several institutional interlocutors that may represent more or less reliable sources of information and thus contribute to the denunciation. Complying with article 29 of the Code of Criminal Procedure (CCP), all the corporate authorities and the public officials that may be acquainted with a crime or an offense have to inform the Public Prosecutor (Procureur de la République).(14) Under this perspective, the judiciary police seems to be the most precious assistant for the public prosecutor.

As far as they are concerned, the bodies exerting internal administrative control(15) (*Contrôle général des dépenses publiques, Inspection générale des services publics, Inspection générale des finances, commissions des marchés*) and control functions(16) and some kind of external audit (*Conseil national de la commande publique, Haute instance de la commande publique, Comité du suivi et d'enquête des marchés publics*) in the field of public procurement, may play an essential role in the detection of public procurement frauds. On the other hand, financial jurisdictions(17) (*Cour des comptes, Chambres régionales des comptes* and *Cour de discipline financière*), as well as the Conseil de la concurrence,(18) have the faculty to inform the public prosecutor's representatives (représentants du parquet) by criminal jurisdictions on all the breaches that they may have known during their inspection. However, transmissions remain

(13) TA, 3<sup>rd</sup> February 1993, *Neski*, Rec., 465.

(14) In the OACA case (*Office de l'aviation civile et des aéroports, OACA*) as a result of an investigative report realized by the General Inspectorate for Public Services (*Inspection générale des services publics, IGSP*) the former CEO of OACA was sentenced to nine years of imprisonment for the offences of fraud and forgery in public procurement, cfr. C. appel de Tunis, Crim., 9 June 2004, n°5193, CCE au nom de l'Etat et de l'Office de l'aviation civile et des aéroports (OACA) c. A. Tlili, unpublished.

(15) On this type of control: OECD, *Integrity Review of Tunisia, The Public Sector Framework*, 2013, 42.

(16) These Commissions' organization, powers and functioning derive from Title V of the CMP entitled "Contrôle préalable des marchés" as amended by Decree No 2012-515, 2 June 2012.

(17) On the monitoring of this body on public spending: OECD, *Integrity Review of Tunisia, The Public Sector Framework, cit.*, 43 - 44.

(18) Law No. 1991-64, 29 July 1991, Art. 20, on competition and prices as amended by subsequent legislation.

exceptional and, strangely, reports on the control of political parties financing are merely “*subject to a confidential report addressed by the Court of Auditors to the President of the Republic and the first responsible of the concerned party*”.(19)

On the other hand, the imbrication between corruption and money laundering obliges financial institutions “*to verify the identity of customers, to take reasonable steps to determine the identity of beneficial of owners of funds deposited into high-value accounts and to conduct enhanced scrutiny of accounts sought or maintained by or on behalf of individuals who are, or have been, entrusted with prominent public functions and their family members and close associates*”.(20) This device in Tunisia is steered by the Commission Tunisienne des Analyses financières (CTAF) having its seat nearby the Central Bank.(21) It allows reporting to judicial authorities the suspect cases of fund flows with a view to freezing and seizing goods coming from laundering operations.(22)

More generally, after the Revolution public authorities chose to create independent agencies against corruption, following the Anglo-Saxon model. Thus, the CNICM(23) has been provided with prerogatives aimed at allowing it to gather the necessary information on corruption facts before they are transmitted to justice (Art. 3). The public report that was written by the Commission in order to comply with its mission allowed revealing the breadth of corruption in public procurement during the former regime.(24) The INLC, which followed to the CNICM, has been established by article 12 of decree-law of November 14th 2011.(25) It was given the mission to detect the scenes of corruption in public and private sectors, as well as to receive requests and information on corruption practices (Art. 13). However, due to political reasons, its execution has been late, and it does not seem to have the necessary means to carry out its missions.

Participation of civil society: Associations – especially those ones in the forefront of the fight against corruption – media and individuals also have a role to play in denouncing frauds in public procurement. The effectiveness of their

(19) Law No. 1968-8, 8 March 1968, Art. 65, particularly amended by the Organic Law No. 2008 - 29 January 2008 on the Cour des Comptes.

(20) United Nations Convention against Corruption (UNCAC), New York, 2004, Art. 52 (1).

(21) Established by Law No. 2003-75, 10 December 2003, Art. 78, concerning the support to the international efforts in the fight against terrorism and money laundering.

(22) See on this issue: Rapport d’Evaluation Mutuelle de la République tunisienne de la lutte anti-blanchiment de capitaux, Groupe d’action financière pour le Moyen et l’Afrique du nord (GAFIMOAN), avril 2007.

(23) *V. supra*, 1.

(24) The national Investigative Commission on corruption and embezzlement during the ancient régime (CNICM) has been established by the law-decree No. 7-2001, 18 February 2011. Since its establishment till 27 October 2011, the date on its mission has expired, the Commission has received 10062 queries. It has carried a preliminary activity in 5206 cases deciding to send more than 300 to courts. Chapter 3 of its reports concerns 14 cases of corruption in public procurement, see Report of the CNICM Tunis, November 2011, 51-84 and statistical annexes.

(25) Law-decree No. 2011-120, 14 November 2011 concerning the fight against corruption, in *JORT*, No. 88-2011, 2746.

action is subordinate to the consecration of an effective right of access to information.(26) Besides, early-warning mechanisms and a regime of immunity for the alerting subject “*whistleblowing*” may usefully contribute to corruption prevention. We have been able to measure the scope of these instruments during the period before the Revolution, as a result of disclosure by Wikileaks of confidential reports of the U.S. embassy in Tunis on corruption practices under the former regime. Yet, legislation allowing protecting public officials who would be tempted to report corruption cases in public procurement. However, experience shows that “*one of the main difficulties in this area is to ensure the protection of the officials who report wrongdoing from reprisals*”.(27)

### 3.2. The need to extend the investigative powers of the investigating authorities

Information, even though essential, cannot be sufficient to sanction individuals suspected of corruption. Still it is necessary to gather evidence likely to convince the criminal courts to impose sentences. For this reason, the investigating authorities should have extensive investigative powers. Due to the complexity of corruption, it is necessary to give those authorities broad powers of investigation.

Investigative powers of investigation authorities and respect for freedoms: Powers of domiciliary visit, search and seizure, as well as rights of communication and hearing are often decisive when it comes to gather the evidence needed to incriminate. Organized by the Code of Criminal Procedure, they must be strictly defined because of their effects on freedoms.

In principle, only the investigating judge can exercise these powers, except in cases of flagrante delicto justifying the intervention of judicial police officers under the control of the competent judicial authority.

Exceptionally, some public officials duly authorized by special legislation may be authorized to use such powers but then under the control of the judiciary authority and respecting the rights of the defence. The extension of these powers to the anticorruption agencies that can be observed today therefore poses serious problems in terms of respect for freedoms.

The problem here is that these authorities have been vested with such powers by legislative texts whose constitutionality is questionable. Neither Article 3 of Decree-Law No. 2011-7 on the CNICM nor Article 31 of Decree-Law No. 2011-120 on the ILNC provide the necessary protection against abusive investigations.

(26) Law-decree No. 2011-41, 26 May 2011, as amended by the law-decree No. 2011-54, 11 June 2011, has settled the right to access to administrative documents. Nonetheless, the scope of application of this provision is very narrow and its implementation has never been effective.

(27) OECD, *Integrity Review of Tunisia, The Public Sector Framework, cit.*, 60.

In ordinary times, the Tunisian Constitutional Council had the opportunity to rule on the constitutionality of such/similar provisions. He then held that Article 65 para. 1 of the draft law enacting the Customs Code, enabling the administration officials to make searches even in private places without specifying the nature and extent of the supervision of a judge on these operations, is contrary to Articles 5 and 12 of the Constitution guaranteeing the inviolability of the home and the rights of the defence.<sup>(28)</sup> Today, after promulgation of the Constitution of the Second Republic on January 27, 2014, Article 24 is more explicit to protect “private life, private home, and confidentiality of correspondence’s and communications”.<sup>(29)</sup>

The new laws legalizing these powers have been adopted under the State of Emergency on the basis of the first Provisional Organization of Public Authorities under the little constitution, i.e., Legislative Decree of March 23th 2011, following the suspension of the constitution of 1959. Even if they do not have all the guarantees provided, the assessment of their constitutionality can only be done by reference to the Constitutional Emergency Law.<sup>(30)</sup>

*The independence of the public prosecutor at issue:* the logic of inquisitorial criminal procedure<sup>(31)</sup> provides that the public action, aimed at eliminating the social disorder resulting from the recognition of corruption cases in public procurement, is the responsibility of the public prosecutor. The outcome of the proceedings often depends on the independence of the prosecutor magistrate, who has enormous powers.

The constitutional status of the latter raises the question of his independence. Article 11 of UNCAC addresses this issue, highlighting the crucial role of prosecutors in the fight against corruption.

The new constitution, adopted on January 27, 2014, includes significant advances in this direction. In this regard, Articles 106 and 107, providing for the extension of fundamental guarantees of independence to those prosecutors, is an important step in this regard. Then, the question of the constitutionality of the provisions contained in Articles 21, 22, 23 and 30 of the CCP arises. On the other hand, the creation of a Constitutional Court pursuant to Article 120 charged in the future to control, a priori, but also a posteriori, the constitutionality of laws will inevitably raise the question of the compliance of these provisions to the New Constitution.

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(28) Cons. Const. Tunisie, statement No. 02-2007, 24 January 2007, in *JORT*, No. 47-2008, 2153.

(29) The New Constitution was approved late on Sunday night, January 26, 2014, after two years of acrimonious debate, in one of the most difficult steps of the democratic transition. It came into force on January 27, 2014, after signing by the President of Republic, the outgoing Prime Minister and the Speaker. It began coming into effect on February 11, 2014, when it was published in the official journal (OGRT, special number, 2014).

(30) See on this issue R. JENAYAH, *Droit constitutionnel d'exception*, Cours général, AIDC, XVIIIème Session, Tunis, juillet 2012.

(31) See on this issue, J.-C. SOYER, *Droit pénal et procédure pénale*, 21<sup>ème</sup> éd., LGDJ, 2012, 640.

Council of Magistracy (*Instance Provisoire de la Magistrature*), intended to replace the dissolved Supreme Council of Magistracy, was established by the Organic Law of May 2nd 2013.(32) Article 12 of this Law contains an explicit reference to the guarantees of independence that have to be recognized by judges.

At present, the main obstacle to putting in motion public action is the fact that the perpetrators of these crimes can be prosecuted only after a complaint to the public prosecutor's department, which assesses the appropriateness of prosecution (Art. 30 CCP). Now, the judges who compose it remain under the direct authority of the Minister of Justice (Art. 22 CCP), therefore undergoing direct pressure. In the new context, a significant increase was certainly seen in the number of investigative procedures started by the prosecutors. Yet, as the same causes of interference by the executive and of courts' lack of means produce the same effects, the treatment of these cases remained well below expectations and were often subject to politics.

*The role of victims in the launch of proceedings:* the UNCAC requires States parties to take the necessary measures to give the right to initiate legal action to obtain compensation to those who have suffered damage. Civil action in the field of infringements of public procurement rules can be brought first, as the victim can override the inertia of the prosecution and trigger itself the public action. However, the victim may also act accessorially, in parallel to the prosecution's public action.

Dealing with frauds in public procurement, the victims may be either economic operators or public purchasers. Thus, the unsuccessful candidates in an award procedure can ideally enforce their right to compensation for the damage suffered. On the other hand, people who were forced into paying undue payments to public officials may assert a direct harm justifying their standing as a civil party.

The contracting public authorities' civil action may seem more problematic because such action is reserved for those who have personally suffered damage caused by the offense (Article 7 of the CCP). This condition seems to be more difficult to establish when dealing with a legal person. There is no doubt, however, it must be regarded as fulfilled when it comes to fraud in public procurement causing some damage to a public community. For this reason, it was finally accepted by the jurisprudence.(33)

#### ***4. The adaptation of the criminal repression of fraud to public procurement***

Awareness of the limits of conventional means of repression of corrupt practices in public procurement has led the government to introduce a new type of crime, more suited to this type of misconduct.

(32) Organic Law No. 2013-13, 2 May 2013 establishing the *Instance Provisoire de la Magistrature*, in *JORT*, No. 37, 1643.

(33) C. appel de Tunis, Crim., 9 July 2004, No. 5193 before mentioned.

#### 4.1. A new type of infraction in criminal law of public procurement

In order to strengthen the fight against corruption, the legislature finally decided to criminalize violations of the rules for the award and execution of public contracts by creating two distinct types of offense: the first, under Article 96 of the Penal Code (PC), is not limited to public procurement. It covers all illegal behaviours that may have caused harm to the administration. The second, under Article 87*bis* of the Code, is specific to public procurement. It tends to punish breaches of rules for the awarding of such contracts.

A catch-all offence: the award of undue advantage which caused harm to the administration: this infraction, provided by article 96 of PC, was ranked in the category of extortion although its scope is wider. It was set up as a crime punished by ten years' imprisonment and a fine equal to the amount of the benefit received or injury suffered by the administration, as well as additional penalties under Article 5 of the Penal Code, of which the most dishonourable is deprivation of civic rights. It is applicable to:

*“tout fonctionnaire public ou assimilé, tout directeur, membre ou employé d'une collectivité publique locale, d'une association d'intérêt national, d'un établissement public à caractère industriel et commercial, d'une société dans laquelle l'État détient directement ou indirectement une part quelconque du capital, ou d'une société appartenant à une collectivité publique locale, chargé de par sa fonction de la vente, l'achat, la fabrication, l'administration ou la garde de biens quelconques, qui use de sa qualité et de ce fait se procure à lui-même ou procure à un tiers un avantage injustifié, cause un préjudice à l'administration ou contrevient aux règlements régissant ces opérations en vue de la réalisation de l'avantage ou du préjudice subi.”*

Applying to public procurement, infringement under Article 96 punishes a recognised conflict of interest. What is punished is the blurring of genres, i.e., the risk that the public official receives or accepts for others an unfair advantage to the detriment of a public community during the purchase, management or control of goods for which he was responsible. The offense is characterized by the fact that the author has done the incriminating act violating the rules of public procurement. This formal design of the offense can collide with the general principles of criminal law according to which there can be no infringement without intent to commit it. Yet, its major interest is precisely to allow characterizing the offense without the need to prove the existence of personal enrichment of the accused.

The Supreme Court had to clarify the element of the damage suffered by the administration and characterizing the offence, considering that:

*“la chambre d'accusation a fait une mauvaise application de la loi en considérant que les accusés ont occasionné un préjudice certain et grave à l'administration sans préciser la nature et la consistance de ce préjudice.”* (34)

(34) C. Cass, Crim., 8 February 2012, No. 88620, 88623, 88631, 88633, 88639, 88721, 88726, 88764, 88810, unpublished.

On the other hand, violations committed during the various stages of award and execution of a public contract certainly fall within the scope of this offense. For example, in a judgment delivered by the Court of Appeal of Tunis in 2004, the *saucissonnage* technique involving the splitting of the amount of a public purchase of works has been found to violate the laws and regulations governing public procurement.<sup>(35)</sup> Similarly, the Supreme Court held that:

*“la chambre criminelle n’a pas violé la loi en montrant le rôle de l’ancien ministre du tourisme dans l’attribution d’un marché de promotion de l’image de la Tunisie en violation délibérée des lois et de l’ensemble des règles et des procédures applicables aux marchés publics, alors surtout qu’il apparaît à travers les pièces du dossier que le bénéficiaire de l’avantage reçu s’était entendu avec le prévenu à tous les stades de la procédure pour que ce dernier affecte une part du budget du ministère à l’augmentation du budget de promotion afin de financer le marché litigieux.”*<sup>(36)</sup>

The sentences are often imposed on the basis of concurrent offences (forgery, misappropriation of public funds, accepting bribes, concealment of stolen goods). The courts in charge are particularly severe and suppress both the principal offender and the accomplices under Article 32-4 of the PC, which provides that:

*“est considéré comme complice et puni comme tel (...) celui qui a prêté, sciemment, son concours aux malfaiteurs pour assurer, par recel ou par tous autres moyens, le profit de l’infraction ou l’impunité à ses auteurs.”*<sup>(37)</sup>

The offense is prescribed starting from the last act of the public official.

The specific offence of favoritism or granting undue advantage in public procurement: It is article 87 *bis* of the Penal Code which established for the first time the principle of the criminalization of violations of freedom of access and equality of candidates in public procurement. This offense is punishable by imprisonment of up to five years as well as the additional penalties provided for in Article 5. It is applicable to:

*“tout fonctionnaire public ou assimilé qui aura agréé, sans droit, soit pour lui-même, soit pour autrui, directement ou indirectement des dons ou promesses de dons, présents ou avantages de quelque nature que ce soit en vue d’octroyer à autrui un avantage injustifié par un acte contraire aux dispositions législatives ou réglementaires ayant pour objet de garantir la liberté de participation et l’égalité des chances dans les marchés passés par les établissements publics, les entreprises publiques, les offices, les collectivités locales et les sociétés dans lesquelles l’Etat ou les collectivités locales participent directement ou indirectement à son capital.”*

However, the *ratione personae* scope of application of this offence, commonly called the offense of favouritism or granting undue advantage, is narrower than that of Article 96. It is even narrower than under the UNCAC. Ideally,

(35) C. Cass. Crim., 9 July 2004, No. 5193, unpublished.

(36) C. Cass. Crim., 27 February 2012, No. 88611, unpublished.

(37) Indeed, in the previously mentioned OACA case, the Court of Appeal of Tunis did not hesitate to condemn the former CEO to nine years’ imprisonment on the basis of Articles 96 and 199 of the CP.

it should apply to all persons who have powers to influence the procurement. From this point of view, the notion of “*fonctionnaire public et assimilé*” appears unreasonably restrictive. It does not apply to persons who hold “*un mandat législatif ou exécutif*”, whatever their status. Moreover, the issue of collegiality of the incriminated act, in case of a secret ballot, is problematic with regard to the principle of the personal nature of criminal liability.

The *ratione materiae* scope of the crime is very broad. It covers all contracts subject to the Code of Public Procurement, including those of public enterprises<sup>(38)</sup> (Article 3 of the CPP). Although some of these companies, namely those operating in a competitive environment, are subject to specific provisions of Chapter 4 of Title VIII of the CPP, they are not exempted from respecting the fundamental principles of public procurement.

The notion of unfair advantage, which is one of the material elements of the offence, must be interpreted in relation to the principles that are intended to ensure freedom of participation and equality of opportunities in public procurement. In its annual reports, published and posted after the Revolution, the Court of Auditors provides many examples: artificial splitting of contracts aimed at circumventing the rules of competition at the stage of manifestation of needs, non-compliance with disclosure deadlines, granting privileged information or writing specifications oriented to promote a specific candidate, direct negotiations with a candidate without competition, abusive statement of unsuccessful “*infructuosité*” and, more generally, any benefit granted to a candidate by an act contrary to the principles of public procurement.<sup>(39)</sup>

Condemnations remain exceptional. The reasons must first be sought in the regime of prescription provided for in Article 5 of the CCP. When dealing with crime, in fact, the prescription period corresponds to three years starting from the date on which the offense was committed. It is suspended by any material impediment to the exercise of public action as well as any act of investigation or prosecution not followed by judgment. Therefore, it is common for this offense to be prescribed as it has been found.

However, beyond the legal and political obstacles, it seems that the existence of the more inclusive infringement of Article 96 is to cause disaffection for this offense.

#### 4.2. The consolidation of the traditional penal system

This system is based mainly on the criminalization of active and passive corruption as well as influence peddling. It is accompanied by related offences.

(38) The notion of public enterprise derives from Article 8, Law No. 1989-9, 1<sup>st</sup> February 1989. On this issue, A. AOUIJ – M<sup>RA</sup>D, *Le droit des entreprises publiques*, Tunis, 2009, 29-36.

(39) A. TOUNAKTI, *Le contrôle de la cour des comptes sur les marchés publics*, in *Contrats publics et Globalisation juridique*, CPU, Tunis, 2010, 171-187.

At the outset it should be noted that the offense of illicit enrichment, defined by Article 20 of the UNCAC as “a significant increase in the assets of a public official that he or she cannot reasonably explain in relation to his or her lawful income”, is not taken into account under Tunisian law.

On the other hand, the criminal liability of legal persons, which is essential to ensure the effectiveness of the fight against corruption, although recently enshrined in Article 32 of the Act of November 14th 2011 on fight against corruption,(40) remains dependent on a reform of the Penal Code specifying the cases and conditions in which these persons could be implicated.

The criminalization of passive corruption and influence peddling: the Penal Code is particularly severe regarding passive corruption. Article 83 considers that there is passive corruption when a public official or similar will accept without a right to do it, either for himself or for others, “*des dons, présents ou avantages de quelque nature que ce soit pour qu’il accomplisse ou s’abstienne d’accomplir un acte lié à ses fonctions*”. This offense is criminalized and punished by ten years’ imprisonment and a fine equal to “*double de la valeur des présents reçus ou des promesses agréées, sans qu’elle puisse être inférieure à dix mille dinars*”. It must be distinguished from active corruption under Article 91 of the Penal Code aimed at suppressing any attempt to bribe a public official or similar “*en vue d’accomplir un acte lié à sa fonction, même juste, mais non sujet à contrepartie, ou de faciliter l’accomplissement d’un acte lié à sa fonction, ou de s’abstenir d’accomplir un acte qu’il est dans son devoir de faire*”. This type of crime is rarely applied.

In the field of public procurement, the offence of passive corruption is recognized when it is established that a public official proposed or agreed to perform an act in exchange for an unfair advantage. Two elements must therefore be proved: the commitment by the corrupt official to do something and the benefit he received. The incriminated act must fall within the office of the public official. It must be an act of his function, mission or mandate, or facilitated by his function, mission or mandate. The penalty shall be doubled if it appears that the corrupt official worked diligently with the briber requesting the undue benefit in exchange for the incriminated act (Article 84).

Article 85 of the Code provides for a less severe penalty of five years’ imprisonment and a fine of 5000 Dinars “*si le fonctionnaire ou assimilé a accepté des dons, promesses, présents ou avantages de quelque nature que ce soit en récompense d’actes qu’il a accomplis et qui sont liés à sa fonction, mais non sujet à contrepartie, ou d’un acte qu’il s’est abstenu de faire alors qu’il est tenu de ne pas faire*”. The difference with Art. 83 is that the public servant or equivalent was not aware, at the time of the exercise of his duties, that he would receive

(40) Article 12 of this Law provides that “*les personnes morales peuvent être poursuivies si la preuve de leur responsabilité est établie dans la commission d’infractions de corruption*”.

an advantage. He exercised his activities in a neutral manner but eventually accepted the undue advantage after the completion of the incriminated act.

Passive corruption is similar to the influence peddling crime under Article 87.

The expected profit for the corrupt is the same in the two offences. It corresponds to “*offres, des promesses, des dons, des présents, ou des avantages quelconques...*”. However, the two offenses differ in their goals, as passive corruption is to do or abstain from doing an act within the jurisdiction of the public official, while influence peddling aim, at “*abuser de son influence réelle ou supposée en vue de faire obtenir d’une autorité ou d’une administration publique des distinctions, des emplois, des marchés ou toute autre décision favorable*”.

Related offences: Regarding the so-called related offenses (bribery, misappropriation of public goods and funds, revolving door offence “*pantouflage*”, participation in a cartel, forgery and use of forgery, misuse of corporate assets, fraud, concealment and laundering), just to name those that may be related to procurement, the Penal Code contains definitions quite similar to those commonly accepted in other countries, even if the regime of sanctions is more or less severe. Bribery and embezzlement of public funds are especially provided for in Articles 95 and 99 of the Code as well as in the Code of public accounting. Sanctions are particularly severe: fifteen years’ imprisonment for bribery, twenty years for embezzlement of public funds, in addition to a fine equal to the refunds of diverted funds or of the value of the interests or gain obtained (Art. 98).

Other texts provide for the breaches of the duty of public office. Article 106 defines the offense as “*le fait, pour tout fonctionnaire public ou assimilé, de se faire délivrer gratuitement, à l’occasion d’une mission, transport sur les lieux, ou tournée, des vivres, des denrées, ou des moyens de transport*”. Punished with a light penalty of three months in prison, this type of breach is a way to punish the approach of gifts that private companies have become accustomed to concede to officials of public procurement in exchange for their “*services*”.

## 5. Conclusion

The study of the system of repression of fraud in public procurement has helped frame the debate around the central question that today agitates the political class, i.e., the moralization of public life.

Beyond the change of regime, we find the same culture of impunity, the same reluctance of policymakers to obey the rules of integrity that should govern the system of public procurement. In these conditions, only profound changes introducing more transparency, participation and independence of authorities in charge of repression of corruption can help ensure the integrity of public procurement.



## **PART II**

# **Corruption in the Award Phase**

**BRUYLANT**



**CHAPTER 1**  
**Integrity challenges in the EU**  
**and U.S. procurement systems**

BY

Daniel I. GORDON\*

Associate Dean for Government Procurement Law,  
George Washington University

Gabiella M. RACCA

Professor of Administrative Law, University of Turin

***1. The different scope of public procurement rules  
in the EU and the U.S. and the relevance of integrity***

It seems of interest to clarify the different perspectives concerning public procurement in the US and the EU in order to highlight the different scopes and effects of their regulations.

The EU Directives define procurement rules that apply to 28 different countries, with different legal systems and diverse cultural and social traditions. This is a horizontal challenge that the United States hasn't had to deal with, since its procurement system applies only to one country, the U.S.(1) Secondly, the EU is dealing with a vertical challenge that the US avoids for constitutional reasons. From a US perspective, it looks impressive that EU procurement directives cover all levels of government, from national procurements to local procurements, including small municipalities. In the US there is a more-or-less uniform federal system, but it does not apply to the States; their procurement systems are legally and factually separate from

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\* Mr. Gordon was the Administrator for Federal Procurement Policy in the Obama Administration.

(1) *The U.S. acquisition system has a long history and is based on a detailed statutory and regulatory scheme.* The roots of the federal procurement system can be traced back to the 19<sup>th</sup> century (and arguably back to the War of Independence in the 18<sup>th</sup> century). Today, the bedrock of the federal procurement laws is the Competition in Contracting Act of 1984, modified by reform legislation from the 1990s, and implemented through the very detailed Federal Acquisition Regulation (the FAR). CICA, as the 1984 statute is often called, was codified in several different parts of the United States Code: in section 2301 and the following sections of Title 10 for defence agencies; in section 251 and the following sections of Title 41 for civilian agencies; and in section 3551 and the following sections of Title 31 for the bid protest provisions). The definitive history of the U.S. federal procurement system is James F. Nagle's, *History of Government Contracting*, (2<sup>nd</sup> ed. 1999).

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the federal system. In the EU, the Public Procurement Directives can be seen as defining only a minimum common denominator for the 28 Member States that must implement them according to different legal systems, different languages and different approaches to procurement. The result is a degree of variation, even though the detailed provisions of EU Directives can become directly applicable to any above-threshold EU procurement. Most of the rules are mandatory and after the implementation term become directly applicable, whenever not correctly implemented, according to a EU Court of Justice ruling.<sup>(2)</sup>

At the international level the GPA defines a “minimum minimum” common to both EU and US systems, a lowest common denominator among very different systems. Contrasted with UNCITRAL, the United Nation Commission on International Trade Law, whose aim is to create a model procurement law, the GPA does not include the level of detail that would be needed for a statute.<sup>(3)</sup>

The EU procurement Directives seem to be moving in the direction of constructing a detailed set of procurement rules, more like the UNCITRAL model law than the WTO GPA, which is an extraordinarily challenging task.<sup>(4)</sup>

The first “whereas” in the draft of the new Directive provides that:

*“The award of public contracts by or on behalf of Member States authorities has to comply with the principles of the Treaty on the Functioning of the European Union, and in particular the free movement of goods, freedom of establishment and the freedom to provide services as well as the principles deriving therefrom, such as equal treatment, non-discrimination, mutual recognition, proportionality and transparency. However, for public contracts above a certain value, provisions should be drawn up coordinating national procurement procedures so as to ensure*

(2) The direct effect of European law has been enshrined by the Court of Justice in the judgement of *Van Gend en Loos* of 5 February 1963. The ECJ stated that European law not only engenders obligations for Member States, but also rights for individuals. Individuals may therefore take advantage of these rights and directly invoke EU acts before national and European courts. While an EU directive is an act addressed to Member States and must be transposed by them into their national laws, in certain cases the Court of Justice recognises the direct effect of directives in order to protect the rights of individuals. Therefore, the Court laid down in its case-law that a directive has direct effect when its provisions are unconditional and sufficiently clear and precise (ECJ, 4 December 1974, *Van Duyn*, in C-41/74). However, it can only have a direct vertical effect. That is, individuals can invoke a European provision in a challenge to a Member State only if the State has not transposed before the deadline provided (ECJ, 5 April 1979, *Ratti* in C-148/78). ECJ, 10 November 2011, *Norma-A SIA – Dekom SIA v Latvijas plānošanas reģions*, in C-348/10 concerning the Remedies Directive (EU Dir. No. 2007/66).

(3) S. ARROWSMITH (Ed.) *Reform of the UNCITRAL Model Law on Procurement: Procurement Regulation for the 21<sup>st</sup> Century*, West Publishing, 2009; ID., *The Past and Future Evolution of EC Procurement Law: From Framework To Common Code?*, in *PCLJ*, Vol. 35, No. 3, 2006, 337-384.

(4) S. ROSE-ACKERMAN, *International Actors and the Promises and Pitfalls of Anti-Corruption Reform*, in *Pennsylvania Journal of International Law*, 2013, 472. D. I. GORDON, *Anti-Corruption Internationally: Challenges In Procurement Markets Abroad – Part II: The Path Forward for Using Procurement Law to Help with Development and the Fight Against Corruption*, in *GW Legal Studies Research Paper*, No. 40, 2013, available at [www.ssrn.com](http://www.ssrn.com).

*that these principles are given practical effect and public procurement is opened up to competition.”* (5)

Actually, harmonization of the European rules is less than one might expect: only 20% or so of public procurements (measured by value) fall within the scope of the directives.<sup>(6)</sup> Nonetheless, according to the EU Court of Justice, all EU procurements should apply the Treaty principles, but those principles are not as demanding.

The limited applicability of the EU Procurement Directives reduces their impact. In fact, cross-border procurement in the EU is rare. European efforts to construct a more uniform procurement system might have facilitated creation of national procurement markets where there were still internal barriers (e.g., between Northern and Southern Italy,<sup>(7)</sup> or among German Laender<sup>(8)</sup>); however, only 1.6% of the public procurement contracts are won by an economic operator from another country.<sup>(9)</sup> One reason may be that the various EU member states' national procurement legal systems are still different and separate despite the efforts of the Directives: legal and language barriers produce a fragmentation of the public procurement marketplace that economic operators are quite used to.

Another reason for such fragmentation is related to the limits of EU Directives, which address the award phase, but not contract management. Contract

(5) Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on *public procurement and repealing Directive 2004/18/EC*, Wh. No. 1. See before: ECJ, 7 December 2000, *Telaustria*, in C-324/98, p. 60-62; ECJ, 21 July 2005, *Coname*, in C-231/03, p. 16-19; ECJ 13 October 2005, *Parking Brizen*, in C-458/03, p. 46-49; ECJ, 13 November 2008, *Coditel Brabant*, in C-324/07, p. 25. ECJ, III, 10 September 2009, *Wasser- und Abwasserzweckverband Gotha und Landkreismunicipalitäten (WAZV Gotha) v. Eurawasser Aufbereitungs- und Entsorgungsgesellschaft mbH*, in C-205/08, p. 44. See also: R. CAVALLO PERIN, *I principi come disciplina giuridica del pubblico servizio tra ordinamento interno e ordinamento europeo*, in *Dir. Amm.*, 2000, 60; R. CARANTA, *The Borders of EU Public Procurement Law*, in D. Dragos – R. Caranta (eds. by) *Outside the Procurement Directives – inside the Treaty?*, Djøf Publishing, Copenhagen, 2012, 25 et seq.

(6) EU Commission, *Evaluation Report Impact and Effectiveness of EU Public Procurement Legislation*, June 2011, 27; G. M. RACCA, *The Electronic Award and Execution of Public Procurement*, in *Ius Publicum Network Review*, 2012, accessible in [http://www.ius-publicum.com/repository/uploads/17\\_05\\_2013\\_19\\_31-Racca\\_IT\\_IUS-PUBLICUM-EN.pdf](http://www.ius-publicum.com/repository/uploads/17_05_2013_19_31-Racca_IT_IUS-PUBLICUM-EN.pdf) and in Social Science Research Network – [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2229253](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2229253).

(7) G. M. RACCA, *Public Contracts – Italy*, in *Ius Publicum Network Review*, 2012, available at <http://www.ius-publicum.com/pagina.php?lang=it&pag=report&id=43>, 4; A. MASSERA, *Italie/Italy*, in R. Noguellou – U. Stelkens (eds. by) *Comparative Law on Public Contracts*, Bruxelles, 2010, 719-720.

(8) M. BURGI, *Public Procurement Law in the Federal Republic of Germany*, in *Ius Publicum Network Review*, 2012, available at <http://www.ius-publicum.com/pagina.php?lang=it&pag=report&id=43>, 6; U. STELKENS – H. SCHROEDER, *Allemagne/Germany*, in R. Noguellou – U. Stelkens (eds. by) *Comparative Law on Public Contracts*, Bruxelles, 2010, 320 et seq. A. RUBACH-LARSEN, *Selection and Award Criteria from a German Public Procurement Law Perspective*, in *PPLR*, 2009, 112.

(9) Rambøll Management, *Cross-border procurement above EU thresholds*, Rambøll study for the EU Commission, May 2011, 38. The study found that direct cross-border procurement accounts for 1.6% of awards or roughly 3.5% of the total value of contract awards published in OJ/TED during 2006-2009 and that 50% of contracts above EU thresholds are awarded within the distance of 100 km. The EU Commission refer to this data in the *Green Paper on the modernisation of EU public procurement policy Towards a more efficient European Procurement Market* – COM(2011) 15 final, 27 January 2011, 4.

management is completely left to the EU Member States, meaning that the EU has no control over the performance of contracts. Because performance can be significantly different from – and less than – what was promised, the result may be to undermine the meaningfulness of the competitive selection, which is the heart of the EU model.(10)

While the reason for the separation the Directives maintain between the award and execution of the procurement may be due to Member States not wanting to lose their sovereignty in the execution of public contracts, the result is considerable uncertainty for economic operators and a challenge to the procurement system's goal of achieving good performance for the benefit of EU citizens.

The failure to address contract execution at the EU level risks causing toleration of performance inferior to what was promised in the contract.(11) In many EU countries this can happen due to incompetence or corruption.(12) As in any country, in EU Member States integrity issues arise in public procurements, including, and perhaps especially, in the execution phase.(13) The two phases of contracting are closely related, of course: it can be easy to win a tender by bidding a low price, if one knows that a much less costly level of performance will be accepted.(14) Because the EU Procurement Directives do not cover the performance phase, no EU remedies can apply. Only recently the ECJ,(15) and

(10) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, 3 February 2014, available at [http://ec.europa.eu/dgs/home-affairs/what-we-do/policies/organized-crime-and-human-trafficking/corruption/anti-corruption-report/index\\_en.htm](http://ec.europa.eu/dgs/home-affairs/what-we-do/policies/organized-crime-and-human-trafficking/corruption/anti-corruption-report/index_en.htm), 26-27; EU Commission, *Green Paper on the modernisation of EU public procurement policy. Towards a more efficient European Procurement Market*, 27 January 2011, COM(2011) 15 final, 25; G. M. RACCA – R. CAVALLO PERIN, *Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption*, in *European Procurement & Public Private Partnership Law Review*, 2013, 287-290.

(11) G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011, Vol. 41, n. 1, 90.

(12) O. BANDIERA – A. PRAT – T. VALLETTI, *Active and Passive Waste in Government Spending: Evidence from a Policy Experiment*, 2009, in *American Economic Review*, 99(4): 1278-1308; PricewaterhouseCoopers study prepared for the European Anti-Fraud office (OLAF), *Identifying and Reducing Corruption in Public Procurement in the EU*, 2013, available at [http://ec.europa.eu/anti\\_fraud/documents/anti-fraud-policy/research-and-studies/identifying\\_reducing\\_corruption\\_in\\_public\\_procurement\\_en.pdf](http://ec.europa.eu/anti_fraud/documents/anti-fraud-policy/research-and-studies/identifying_reducing_corruption_in_public_procurement_en.pdf), 253. S. ROSE-ACKERMAN, *International Actors and the Promises and Pitfalls of Anti-Corruption Reform*, *cit.*, 2013, 481 “Such reforms can both limit corrupt incentives and reduce other forms of waste and inefficiency” ID., *Corruption and government. causes, consequences and reform*, Cambridge, 1999, 59, “Bribes can not only determine who obtains a contract, but also the size and specifications of government purchases. Anti-corruption reforms should focus not just on reducing malfeasance but also on improving the efficiency of government purchasing decisions”.

(13) EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, 2013, in <http://bookshop.europa.eu/>, 12.

(14) G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, *cit.*, 98-100.

(15) ECJ, *Pressetext Nachrichtenagentur GmbH v. Republik Österreich* (C-454/06) [2008] E.C.R. I-4401. See also ECJ, *EU Commission v. Federal Republic of Germany* (C-160/08) [2010]; ECJ, 13 April 2010, *Wall*, in C-91/08; ECJ, 25 March 2010, *Helmut Muller*, in C-451/08; ECJ, 4 June 2009, *Commission v. Greece*, in C-250/07.

subsequently the draft of new Directive, provided that material amendments (significant changes) during execution may constitute the improper award of a new contract without the required public notice – although that situation typically applies to contracts whose scope is being increased through an amendment, rather than a decreasing of the contractual performance standards.(16)

To sum up, the EU Public Procurement market amount in 2011 reached 2,405.89 billion Euros, equal to 19% of the EU GDP, although only 425.44 billion Euros in contracts were published in TED, the EU database, as they are above threshold.

In comparison, the US Federal government currently spends approximately \$500 billion in public procurements each year, an amount that increased during the Clinton and George W. Bush Administrations.(17)

The significant value of the public procurement market and the concern about reducing spending and increasing quality underscore the need for integrity in this sector, which is notoriously vulnerable to corruption.(18) Yet, somewhat surprisingly, the EU Directives do not meaningfully tackle integrity issues nor do they set up a common EU audit system, nor does the new Procurement Directive take the opportunity to fully address the problem through specific rules regarding integrity in EU procurement,(19)

(16) Directive 2014/24/EU, Art. 72. According to the new EU Directive the amendments of the contract shall be considered substantial when it makes the contract substantially different from the one initially concluded “in particular to the scope and content of the mutual rights and obligations of the parties, including the distribution of intellectual property rights” (see: Wh. No. 107).

(17) The amount of money spent on public procurement increased significantly under the Clinton and Bush administrations. While a good part of the spending after 2001 was attributable to spending related to the wars in Iraq and Afghanistan, a great part of the increase from 1992 on was due to the dramatically expanded reliance on contractors to perform services “outsourced” to the private sector.

(18) Today, it is hard to overestimate the impact of corruption in the EU, at least as it is perceived. The European Commission estimates that four out of five EU citizens regard corruption as a serious problem in their Member State. An estimated 120 billion Euros per year, roughly 1% of EU GDP, is siphoned off by corrupt practices. See EU Commission, Communication from the Commission to the European Parliament, the Council and the Economic and Social Committee, *Fighting Corruption in the EU*, 6 June 2011. As reported in the Communication, the total economic costs of corruption cannot easily be calculated. The cited figure is based on estimates by specialized institutions and bodies, such as the International Chamber of Commerce, Transparency International, UN Global Compact, World Economic Forum, *Clean Business is Good Business*, 2009, which suggest that corruption amounts to 5% of GDP at world level.

(19) The principle of integrity was introduced by the Council of the European Union in the compromise text of 24 July 2012 and listed in the wording of the Art. 15 of the Proposal, but subsequently was eliminated. The rules provided that “Contracting authorities shall treat economic operators equally and without discrimination and shall act in a transparent and proportionate manner that avoids or remedies conflicts of interest and prevents corrupt practices”. This text is available at <http://register.consilium.europa.eu/doc/srv?l=EN&t=PDF&gc=true&sc=false&f=ST%2012878%202012%20INIT&r=http%3A%2F%2Fregister.consilium.europa.eu%2Fpd%2Fen%2F12%2Fst12878.en12.pdf>. There are some limited provisions on corruption e.g. on conflict of interest, Art. 21 and on the exclusion of those criminally convicted for corruption in Art. 55.

although it was admitted that Member States “are not fully equipped to tackle [such issues] on their own”.(20)

In the new Directives the member States have refused to explicitly address the issue of fighting corruption in public procurement, although, as even more clearly confirmed recently by the Commission,(21) it is evident that such objective “cannot be sufficiently achieved by the Member States”(22) and will require an intervention at Union level.

On both sides of the Atlantic, the economic relevance of integrity issues in the public procurement sector is evident, but in the US they are addressed uniformly only on a federal level; no common rules cover all the states. While the EU rules in theory apply to all levels of government, in reality uniformity is much less widespread due to the limited scope of the Directives, with their focus on procurements above the threshold and only on the award phase even of those procurements.

## ***2. Flexibility in the choice of procedures in the new EU procurement directive and in the U.S. federal procurement system***

The US system has enormous flexibility regarding the choice of procedure. Since World War II, the use of non-price evaluation criteria and the conduct of “discussions” (the term used for negotiations between the contracting agency and the vendors) have become more and more common. Since the 1970s, procurement officials have been essentially free to choose whether to use negotiated procedures, allowing them to consider factors other than price and to conduct discussions, or to use the “sealed bidding”, under which bids are evaluated only to

(20) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 21 et seq.; EU Commission, Communication from the Commission to the European Parliament, the Council and the Economic and Social Committee, *Fighting Corruption in the EU*, 6 June 2011, 3, in which is also cited Art. 83(1) of the Treaty on the Functioning of the European Union that lists corruption among those crimes for which directives providing minimum rules on definition of criminal offences and sanctions may be established, since corruption often has implications across, and beyond, internal EU borders. Bribery across borders, but also other forms of corruption, such as corruption in the judiciary, may affect competition and investment flows.

(21) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, cit., 24, where is reported that “the proposal also included the setting up of oversight monitoring of the implementation of public procurement rules, red flagging and alert systems to detect fraud and corruption. However, Member States raised fundamental objections to such measures which were considered too cumbersome for their administrations”.

(22) Treaty of the European Union, Art. 5, § 3: “Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level. The institutions of the Union shall apply the principle of subsidiarity as laid down in the Protocol on the application of the principles of subsidiarity and proportionality”.

ensure “responsiveness”, that is, conformance with the tender document (called the solicitation), with the contract generally being awarded to the bidder submitting the lowest-price responsive bid, with discussions prohibited. The choice depends mainly on the subject matter of the contract: the higher the value of the contract, the greater the likelihood that the agency will choose to use negotiated procedures, as it permits considering technical criteria and past performance, in addition to price, as evaluation factors, and allows the government to negotiate with the vendors to discuss their proposals.<sup>(23)</sup> While conducting negotiations has advantages, it obviously is less transparent than sealed bidding, where bids are opened publicly and no discussions with vendors are permitted.

The EU Public Procurement Directive currently in force provides that contracting authorities normally must use either open or restricted procedures. Other procedures, such as negotiation, are considered less transparent and may be used only in defined cases.<sup>(24)</sup> However, the general principles of non-discrimination, equal treatment and transparency apply to all procurement procedures, though in a different way.<sup>(25)</sup>

The declared aim of simplifying and increasing flexibility in the new Procurement Directive can be tested by reading the new provisions for choice of award procedure and evaluation of tenders.

(23) S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform*, *cit.*, 60-63, that reports the procurement problem in U.S. in four stylized categories “purchases that require specialized research and development, such as newly designed military aircraft; purchases of complex, special purpose projects, such as dams or port facilities, that do not involve advances in technology but require managerial and organizational skills; purchases of standard products sold in private markets, such as motor vehicles or medical supplies; and customized versions of products sold privately, such as special purpose computer systems or fleets of police cars”. It is also highlighted the Kelman’s idea “that procurement officers should be given very specific instructions about the goals of procurement and be held accountable for the contract’s ability to fulfil them. They should, however, have considerable flexibility to determine the means”, see S. KELMAN, *Procurement and Public Management: The Fear of Discretion and the Quality of Government Performance*, Washington DC, 1990.

(24) EU Directive No. 2004/18, provides in Art. 30 the cases justifying use of negotiated procedure with prior publication of a contract notice, and in Art. 31 the cases justifying use of negotiated procedure without publication of a contract notice. The new EU Directive on Public Procurement provides the negotiated procedure (only without prior publication of a contract notice) in Art. 32. See also Wh. No. 50 where it is stated that “*In view of the detrimental effects on competition, negotiated procedures without prior publication of a contract notice should only be used in very exceptional circumstances. This exception should be limited to cases where publication is either not possible, for reasons of extreme urgency brought about by events unforeseeable for and not attributable to the contracting authority, or where it is clear from the outset that publication would not trigger more competition or better procurement outcomes, not least because there is objectively only one economic operator that can perform the contract*”. The directives apply only to major contracts, and there are no procedures designed for low-value purchases: for example, there is no equivalent to the “request for quotations” procedure found in the UNCITRAL Model Law on Public Procurement. See: EU Commission, Report from the Commission to the Council and the European Parliament, *EU Anti-Corruption Report*, *cit.*, 27, where is reported the risk of corrupt practices in case of unjustified use of negotiated procedures.

(25) ECJ, 12 December 2002, C-470/99, *Universale-Bau AG v. Entsorgungsbetriebe Siemmering GmbH* (“Universale-Bau”), 2002. E.C.R. I-11617.; S. ARROWSMITH, *The Past and Future Evolution of EC Procurement Law: From Framework to Common Code?*, in *PCLJ*, 2006, 337.

The new Directive on Public Procurement specifically addresses provisions to enhance efficiency of public administration, ensure additional flexibility and eliminate market barriers for SMEs.<sup>(26)</sup> It provides that Member States can use the competitive procedure with negotiation<sup>(27)</sup> or with competitive dialogue,<sup>(28)</sup> in various (exceptional) situations where open or restricted procedures without negotiation are unlikely to lead to satisfactory outcomes.<sup>(29)</sup> In particular, this applies to cases of innovative projects, implementation of major integrated transport infrastructure projects, large computer networks or projects involving complex and structured financing. Problems might arise with the motivation of such choice and their possible challenges. Furthermore such procedures risk being implemented in such a complex manner in many EU Member States that they become unworkable and exposed to endless litigation, as happened with the competitive dialogue.<sup>(30)</sup>

### **3. EU objectivity vs. U.S. subjectivity in the award decision: integrity issues**

A significant difference between the EU and the US approach to evaluation of tenders concerns the relevance of past performance and the objectivity or

(26) Difficulties affecting market access across Europe reduce both the involvement of SMEs and cross-border bidding. Market barriers concern a mix of natural (e.g. language, geographic) and regulatory administrative barriers. See: EU Commission, *Commission Staff Working Paper Executive Summary Of the Impact Assessment Accompanying the document Proposal for a Directive of the European Parliament and of the Council on Public Procurement and the Proposal for a Directive of the European Parliament and of the Council on procurement by entities operating in the water, energy, transport and postal sectors*, 20 December 2011, SEC(2011) 1586 final, where it is stated that “the share of SMEs winning PP contracts has not changed significantly since 2002, nor have cross-border participation rates improved. The most significant factor affecting SME participation is contract value – SMEs have problems bidding for or fulfilling contracts over €300.000”. Instruments that aim to facilitate access to EU PP markets concern the reduction of the evidentiary requirements for bidding. For the EU Commission “adopting the winning bidder approach to providing documentary evidence would reduce administrative costs by 80%”. The proposed Directive suggests the use of lots for contracts with a total value above certain thresholds. Also the improvement of eProcurement and IT tools will favour the access of SMEs to the Public Contracts Sector. Rambøll Management, *Cross-border procurement above EU thresholds*, cit., 87 where a survey reports that around 73% of firms, otherwise active in public procurement, said that they have not made any cross-border tenders in the last three years.

(27) Directive 2014/24/EU, Wh. No. 45. that the negotiations “should aim at improving the tenders so as to allow contracting authorities to buy works, supplies and services perfectly adapted to their specific needs” safeguarding the respect of EU principles. See also Art. 29 of the new EU Directive on public procurement.

(28) Directive 2014/24/EU, Art. 30.

(29) In a sense, the EU Directives are following the pattern of the U.S., in which negotiations were initially permitted only in defined circumstances, and then were allowed more widely, before becoming a free choice, as they are today.

(30) See: S. ARROWSMITH – S. TREUMER (eds.) *Competitive Dialogue in EU Procurement*, Cambridge, 2012, and, in this book G. M. RACCA – D. CASALINI, *Competitive dialogue in Italy*, 458 on the complexity of Italian implementation. Concerning the innovation partnership see Directive 2014/24/EU, Wh. No. 47-49 and Art. 31. Innovation Partnership will involve a competitive procedure with negotiation in order to get an innovative product not yet available on the market.

subjectivity of the choice of the winning tender. The difference mainly concerns the EU's preference for objective, mechanically applied award criteria<sup>(31)</sup> and the American tolerance of subjectivity, both in the evaluation factors and in the tradeoff between price and non-price factors.

### 3.1. Criteria for qualitative selection of tenderers in the EU and past performance in the U.S.

From the EU viewpoint, pre-qualification along with evaluation of the tenderers' capabilities (quality requirements of the economic operators<sup>(32)</sup>) is the first phase of the award procedure, completely separate from the evaluation of the tenders. In the EU, the choice has been to fix a minimum of economic and financial standing and technical and/or professional ability related and proportionate to the subject matter of the contract<sup>(33)</sup> in order for the bidder to be allowed to participate in the contract competition. Any economic operators that meet or exceed the minimum requirement threshold must be admitted.<sup>(34)</sup> The reason for such a rule was concern about the risk of discrimination in favor of national undertakings. This concern led to the EU Directive's excluding the possibility of rating past performance, and in particular, excluding the possibility of evaluating past performance with scores, rather than the pass/fail approach implicit in the EU approach to assessment of potential contractors' eligibility. The result, though, is that the EU neglects an important characteristic of contractors, their track record on prior contracts. The result is that companies with a poor record of performance will generally be allowed to compete for future contracts. While in theory the level of technical requirements could be raised in a way to exclude firms that have not performed well in the past, that risks being considered unjustified, as not proportional, and potentially discriminatory.<sup>(35)</sup> This lack of evaluation and the consequent

(31) EC Directive 2004/18, Wh. No. 46 provides: "Contracts should be awarded on the basis of objective criteria which ensure compliance with the principles of transparency, non-discrimination and equal treatment and which guarantee that tenders are assessed in conditions of effective competition". In the new EU Directive on public procurement see the Wh. No. 90.

(32) EC Directive 2004/18, Artt. 45-52 for the criteria for qualitative selection of the tenderer. In the new EU Directive on public procurement see the Artt. 57-64.

(33) Directive No. 2004/18/EC, for the criteria for qualitative selection see articles 45 to 52. In particular Art. 47 concerning economic and financial standing and Art. 48 regarding technical and/or professional ability. In the new EU Directive on public procurement see the Art. 48.

(34) In the restricted procedure the possible raising of the requirements permits the selection of only a limited number of tenderers. Nonetheless, once the new raised minimum is met, the quality of the tenderers will not be taken into account in the award criteria. Directive No. 2004/18/EC, Art. 44. See: Directive 2014/24/EU, Art. 28.

(35) UK Government, *Buying and managing government goods and services more efficiently and effectively*, published 20 February 2013, available at <https://www.gov.uk/government/policies/buying-and-managing-government-goods-and-services-more-efficiently-and-effectively>. EC Directive 2004/18, Wh. No. 39 "Verification of the suitability of tenderers, in open procedures, and of candidates, in restricted and negotiated procedures with publication of a contract notice and in the competitive dialogue, and the

impossibility to choose on the base of a better record of performance on prior contracts means that the apparent impartiality in the EU system translates into greater risks in the quality of spending and integrity.<sup>(36)</sup>

In the US, the order of evaluation is reversed: first the tender is evaluated and only thereafter the tenderer, as part of the “responsibility” determination, which, like the EU system, is a pass/fail assessment (essentially asking whether the firm is one that the U.S. government is willing to do business with and one that the government believes is capable of performing the contract). That responsibility determination, however, is undertaken only with respect to one firm, the apparent winner of the competition. During the evaluation of tenders, however, the bidders’ past performance will be assessed, typically on a qualitative (not pass/fail) scale, so that a firm’s past performance might be rated “outstanding”, “very good”, or “acceptable”. In the evaluation of tenders in negotiated procurements valued above \$150,000, past performance is a mandatory evaluation criterion. From a U.S. perspective, the EU pre-qualification of bidders seems both anti-competitive and inefficient, since it requires the contracting authority to judge all firms on a pass/fail basis and allows the contracting authority to eliminate firms from the competition before they have had the opportunity to submit a tender.<sup>(37)</sup> Assessing past performance might ensure performance quality and a fair competition based on the effective quality of public spending, thus reducing the opportunities for corruption. In the EU, difficulties arise also because there is no uniformity in the contract management and thus it seems particularly challenging to define a common standard of evaluation of past performance.

### 3.2. European objectivity vs. American subjectivity

The US approach to award of public contracts was historically focused on selection based on the lowest price. However, during and after World War II, there was growing recognition of the acceptability of taking into account non-price factors as well, although doing so was long view as exceptional. In addition, negotiation with bidders came to be viewed as helpful – although initially,

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selection thereof, should be carried out in transparent conditions. For this purpose, non-discriminatory criteria should be indicated which the contracting authorities may use when selecting competitors and the means which economic operators may use to prove they have satisfied those criteria”. See: ECJ, 29 March 2012, *SAG ELV Slovensko and Others* in C-599/10; ECJ, 12 November 2009, *Commission v Greece* in C-199/07; ECJ, 24 January 2008, *Lianakis v Dimos Alexandroupolis* in C-532/06; ECJ, 3 March 2005, *Fabricom SA v Belgian State*, in joined cases C-21/03 and C-34/03.

(36) EU Commission, *Green Paper on the modernisation of EU public procurement policy Towards a more efficient European Procurement Market*, cit., 18.

(37) S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform*, cit., 62. On the issue related to past performance “the use of past performance as a factor in awarding new contracts has proved difficult to implement because there is no generally accepted technique for evaluating performance”.

again, only in exceptional circumstances. Finally, in 1984, with enactment of the Competition in Contracting Act, both use of non-price factors (in addition to price, of course) and the conduct of negotiations (called “discussions”) with bidders came to be viewed as ordinary options for the conduct of a procurement.

The US now routinely allows ‘tradeoff’ contracting decisions (often called ‘best value’ decisions), in which contracting officers are allowed to make subjective selection among competing tenders, rather than selecting based only on price. That said, US government agencies are permitted to use price as the sole criterion in selecting among acceptable tenders, and they sometimes do so. It is not only that non-price selection criteria are permitted. What is noteworthy is the subjective way that the US system permits those non-price criteria to be assessed and then used. (38)

First, there is an element of subjectivity in the assessment of non-price factors that would not be permitted in many other procurement systems. Thus, tenderers’ past performance is a widely used, and often required, evaluation criterion, and the past performance rating that a bidder receives can be assigned by a contracting official on a judgmental basis, (39) without objective criteria. Only in the case of sealed bidding, where price is the sole award criterion, is there no evaluation of past performance. In the 1990s, the assessment of past performance was often based solely on prior work identified by the bidders in their tenders. In their submission, they were required to disclose their “relevant” prior contracts, so that their performance under those contracts could be checked. A past performance database was set up some years ago and despite some difficulties, it is intended to allow the government officials to identify prior contracts without reliance on the tenderer, thus reducing the risk of disclosure of only contracts where past performance was good. (40)

Second, the US system allows the tradeoffs between price and non-price factors to be subjective. The acceptability of subjective tradeoffs has been recognized at least as far back as the 1970s, when GAO declared that contracting officers had discretion in making tradeoffs among competing bids, as long as their decision

(38) D. I. GORDON, *Protecting the integrity of the U.S. federal procurement system: Conflict of interest rules and aspects of the system that help reduce corruption*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, Edward Elgar Publishing, 2014, 42 - 43.

(39) In a recent protest decision, GAO stated, as the standard legal framework for its review of a challenge to an agency’s evaluation of a firm’s past performance, “An agency’s evaluation of past performance, including its consideration of the relevance, scope, and significance of an tenderer’s performance history, is a matter of discretion which we will not disturb unless the assessments are unreasonable or inconsistent with the solicitation criteria”. *Phoenix Management, Inc.*, B-405980.7 *et al.*, May 1<sup>st</sup>, 2012.

(40) The evaluation and any contractor response comprise the past performance information that is stored in government databases (e.g., Past Performance Information Retrieval System (PPIRS), Federal Awardee Performance and Integrity Information System (FAPIS)) and may be used in future source selection decisions. See: KATE M. MANUEL, Congressional Research Service Report for Congress, *Evaluating the “Past Performance” of Federal Contractors: Legal Requirements and Issues*, 4 February 2013, in <http://www.fas.org/sqp/crs/misc/R41562.pdf>.

was consistent with the publicly announced evaluation criteria and met the test of rationality.(41) That means, for example, that, where a solicitation advised that the government will weight price and past performance equally, two contracting officials could reach different – but both permissible – tradeoff decisions between competing bids. Thus, one contracting officer could decide that bidder A, with an “outstanding” past performance record but offering a price of \$10 million, should receive the contract, rather than bidder B’s \$9 million offer, because bidder B had only “good” past performance. Another contracting officer, faced with the identical facts, could decide that it wasn’t worth the government’s money to spend that extra \$1 million to obtain the benefit of working with a firm with a track record of outstanding performance. That degree of subjectivity can open the system to problems, including problems potentially related to corruption, since it decreases transparency (in the sense that it is not so clear why the government chose the winner). Nonetheless, the problem is subject to multiple accountability mechanisms, in the form of bid protests as well as audits. The system thus provides, or at least attempts to provide, a balance between allowing contracting officials to exercise their discretion and judgment in spending public funds, on the one hand, and ensuring the integrity of public procurement through effective accountability, on the other.(42)

From the EU viewpoint, award of a contract should be objective(43) in order to ensure non-discrimination among economic operators of different

(41) The seminal GAO decision establishing this principle was *Grey Advertising, Inc.*, 55 Comp. Gen. 1111 (1976), 76-1 CPD 325.

(42) D. DELLA PORTA – A. VANNUCCI, *Corrupt exchanges: Empirical themes in the politics and political economy of corruption*, paper prepared for conference, Bielefeld, 2001, they rank discretion as follows: “(i) When public demand and preferences are precisely defined with respect to both qualities and price structure. The award is automatic, and the public agent exercises no discretionary power. (ii) While public demand is precisely defined, general criteria for prices describe the public preferences. Discretionary intervention is necessary. (iii) Public demand is not defined with precision. Public preferences are described by general criteria for both price and quality. The public official has the power to assign weight to the various offers, according to general criteria. (iv) The demand and the public preferences are precisely defined during a bilateral bargaining process, delegated to the public agent. S/he is choosing the private part, while price and other contract conditions are the result of the negotiation process”. This classification is reported by T. SØREIDE, *Corruption in public Procurement Causes, consequences and cures*, 2002, 13. The author observe that “This way of classifying public procurement into various degrees of discretionary authority, or objectivity, is important to understand the inclination to corruption in different situations”. S. ROSE-ACKERMAN, *Corruption and government. causes, consequences and reform, cit.*, 18. “Whenever regulatory officials have discretion, an incentive for bribery exists”.

(43) Directive 2004/18/EC, Wh. No. 46, “Contracts should be awarded on the basis of objective criteria which ensure compliance with the principles of transparency, non-discrimination and equal treatment and which guarantee that tenders are assessed in conditions of effective competition. (...) In order to guarantee equal treatment, the criteria for the award of the contract should enable tenders to be compared and assessed objectively.” See Directive No. 2014/24/EU, Wh. No. 90, “Contracts should be awarded on the basis of objective criteria that ensure compliance with the principles of transparency, non-discrimination and equal treatment, with a view to ensuring an objective comparison of the relative value of the tenders in order to determine, in conditions of effective competition, which tender is the most economically advantageous tender”.

Member States.(44) Such a choice can be implemented with the simplest and most objective award criterion, lowest price. The problem the EU faces is to ensure the objectivity of an evaluation of any other criteria, particularly when their use normally require a subjective assessment.

Selection based on ‘the most economically advantageous tender’ is permitted, as long as the evaluation of quantifiable and non quantifiable quality elements is done through an objective evaluation, including publicly disclosed “relative weightings” of any element.

This commitment to objectivity remains challenging. For example, apart from the case of quantifiable elements (e.g., delivery to be measured in days, distance between the supplier’s warehouse and place of delivery to be measured in kilometers, saving energy to be gauged in Kw/h), the EU system also permits the use of non-quantifiable elements, such as technical merit and aesthetic characteristics. In the evaluation of these qualitative elements, the contracting entities have discretionary power, and their evaluation retains a large subjective component, even when expressed in objective sounding numerical scores.(45) The fact is that subjectively assigned scores, however precisely presented and whatever complex formula is used, do not lead to an objective evaluation. Moreover, even when the assessment of non-price factors is objective (such as assigning points based on the number of days needed for delivery), the tradeoff between those factors and price is inherently subjective: if one tender would have the goods delivered in 15 days and the other would take 20 days, how many euros extra should the contracting authority be willing to pay for the earlier delivery? Of course, in such cases, the ‘monetization’ of non-price factors can be disclosed in the tender documents (for example, each day shorter than 30 days will be translated into an evaluated price credit of 100 euros), so that an objective formula and transparency are preserved.

The goal of objectivity and the reduction of the discretion available to evaluation committees (juries) and contracting authorities has induced some Member States(46) to provide for the use of mathematical formulae in the award of public contracts.(47) That is, the contracting authority is to determine a mathematical formula for both the assessment of the different criteria

(44) C. H. BOVIS, *EU Public Procurement Law*, Cheltenham, 2007, 63-80.

(45) J. SCHULTZ – T. SØREIDE, *Corruption in Emergency Procurement*, in *U4 Anti-Corruption Resource Centre – Issue Paper*, 2006, Corruption “can take place through violations of ordinary procurement rules or through misuse of legal authorisation for discretionary decisions”.

(46) The Italian Public Procurement Code: Legislative Decree No. 163 of 2006, Art. 83, § 5, where in the specification of the rules concerning the most economically advantageous tender, the use of a method that permits identifying the most advantageous offer with a single numeric parameter is provided for. See also: the Government regulation enforcing the IPPC (d.P.R. 5 October 2010, n. 207), Annex P.

(47) F. DINI – R. PACINI – T. VALLETTI, *Scoring rules*, in N. Dimitri – G. Piga – G. Spagnolo (eds.) *Handbook of procurement*, *cit.*, 304 et seq.

and the relative weightings used to determine the most economically advantageous tender.(48) While the mathematical formula translates the scores given by the evaluation committee (jury) into a ranking, the problem often remains that the scores themselves are subjective, and they can tilt the award in favor of one tenderer or another. The jury's assessment thus continues to have a discretionary content, and the mathematical formulas serve mainly to give a semblance of objectivity to a subjective evaluation.(49)

Both the jury's discretionary power of technical assessment and that of the contracting authorities in the evaluation of tenders' qualitative elements must ensure reasonableness, consistency and logic in order to avoid discrimination. Yet, for the reasons explained above, objectivity is only apparent. Moreover, the cost paid for the goal of objectivity can be significant: it may force the contracting authority to make a selection based on a score difference that is minimal – essentially irrelevant, especially when the way the score is developed is taken into account – a higher score of 0.1, with no meaningful evaluation of promised quality, may compel a contracting authority to pick one tender over the other.

The limited evaluation of past performance and the complex scoring schemes in the European system can lead to an award that seems random/irrational, and can raise serious integrity and performance risks. Such risks can arise also when the award is decided at the lowest price if the subject matter and contract conditions are not precisely defined in the contract notice, as often happens in work procurements.(50)

The new EU provision for publication on the OJUE of material modification of contracts and the new limits imposed to material changes aim to ensure the respect of the competitive selection process. Material changes to an existing contract will require a new procurement procedure.(51) The material change

(48) P. S. STILGER *Formulas for Choosing the Most Economically Advantageous Tender – a Comparative Study*, 2011, available at <http://igitur-archive.library.uu.nl/student-theses/2012-0327-200536/StilgerPSMA2011Part%20I.pdf>.

(49) Italian Cons. Stato, VI, 2 March 2004, No. 926, concerning an awarding procedure carried out by Consip S.p.A. for substitute services for canteen meal vouchers. Regarding this case, see also the investigation activity provided by the Italian Competition Authority in <http://www.agem.it/component/domino/open/41256297003874BD/934143B3AF9C783AC125705F002CBAF3.html>. See: Italian Authority for the Supervision of Public Contracts for works, services and supplies, Determinazione, 24 November 2011, n. 7, in <http://www.avcp.it/>; F. DINI, R. PACINI, T. VALLETTI, *Scoring rules*, in N. Dimitri – G. Piga – G. Spagnolo (eds.) *Handbook of procurement, cit.*, 309-310.

(50) G. M. RACCA, *Collaborative procurement and contract performance in the Italian healthcare sector: illustration of a common problem in European procurement*, in *PPLR*, 2010, 119-133; G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011, 89-108.

(51) Directive No. 2014/24/EU, Art. 72, § 5, where is required a new award procedure for all the modifications of a public contracts or a framework agreement not admitted by the par. 1 and 2 of this article. For the ineffectiveness see also the EU Directive No. 2007/66, Art. 2(d).

could lower the level of required performance, thus giving an economic advantage to the winner, and undermining the meaningfulness of the competition. A significant price increase during contract performance could also be considered a material change. In the EU experience the modification after the award are quite widespread and not always justified, as they could be symptoms of inefficiency or of corruption.<sup>(52)</sup> The EU Court of Justice defined the limits to such amendments to existing contracts and the new Directive provides a very detailed list of limits to the modification of contracts during their terms, and the forms of publicity.<sup>(53)</sup>

Unsuccessful tenderers will have an interest in learning of later modification of the contract, because they may have the right (e.g., in Italy<sup>(54)</sup>) to get the contract in case of termination for serious infringements, or to compete in a new procurement procedure if a material modification is required. Unsuccessful tenderers and potential competitors could complain if they are not afforded an adequate opportunity to compete in these situations. Third parties could also have an interest whenever a contractor performs below the standards called for in the contract (which may be due to collusion with the procurement official in charge of contract management). The possibility of action by third parties might serve to deter improper or unjustified modifications to contract terms. Relying too heavily on competitors as a backstop against corruption (or incompetence) during the contract performance can be risky, however; for any number of reasons competitors may lose interest in a requirement, or may simply run out of resources, and so may not provide the healthy check that might be otherwise be expected.

Developments in EU law in this area track the long-standing rule in the United States. The US approach is that a modification that the original bidders, at the time they competed for the contract, could not have foreseen is “outside the scope” of the contract and therefore must be procured separately. That has

(52) G. M. RACCA – R. CAVALLO PERIN, *Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption*, in *European Procurement & Public Private Partnership Law Review*, 2013, 287-290.

(53) Directive No. 2014/24/EU, Artt. 72 and 73. In ECJ case law see: ECJ, 19 June 2008, *Pressetext Nachrichtenagentur GmbH Österreich*, in Case C-454/06; ECJ, 29 April 2004, *Commission v CAS Succhi di frutta*, in Case C-496/99 P; ECJ, 29 April 2010, *Commission v Federal Republic of Germany* in Case C-160/08; ECJ, 13 April 2010, *Wall AG v Stadt Frankfurt am Main*, in Case C-91/08; ECJ, 25 March 2010, *Helmut Muller*, in Case C-451/08; ECJ, 4 June 2009, *Commission v Greece*, in Case C-250/07; ECJ, 15 October 2009, *Acoset*, in Case C-196/08.

(54) Italian code of public contracts, Art. 140. In case of serious infringement, contracting authorities can replace the selected contractor by “scrolling down” the initial ranking until the fifth bidder (except the original contractor). The award is made under the same conditions already proposed by the original contractor. See: G. M. RACCA, *Public Contracts – Italy*, cit. 32 et seq.; G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011, 92 et seq.; C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, in *PCLJ*, 2011, 63 et seq.

been the rule in the US for decades, and it appears to be fully consistent with the newer rule in the EU.(55)

The use of electronic means – ‘e-procurement’ – can increase transparency and predictability, but, if it relies on an unwisely arbitrary system for assessing tenders, it will not make that system more sensible. As the Americans are fond of saying about the use of computers, ‘garbage in, garbage out’. An e-procurement system could, however, facilitate the sharing of information about upcoming or recent procurements with economic operators, and it could make it easier for them to submit their tenders and receive feedback on the, all of which could improve the procurement system and its efficiency.

Reverse auctions are commonly used in US Federal procurements, and there is an open discussion on the need of a further regulation.(56) The Federal Acquisition Regulation does not provide rules on reverse auctions and some negative effects of the absence of guidelines have been noted in a recent report issued by the US Government Accountability Office (GAO).(57) According to the data in that report, five US agencies conducted about 70 percent of the federal government’s reverse auctions and many auctions were run without effective competition.(58) Moreover, GAO noted the lack of data on the largest auctions,(59) the performance (by the service provider) of « open market » auctions outside the procurement system(60) and the change of the award criteria during the award procedure.(61)

In the EU e-procurement is considered a way to improve the internal market of Public Procurement, potentially ensuring a greater participation and objectivity of the evaluation.(62) Nonetheless, it is not yet widespread. IT

(55) *AT&T Commc’ns, Inc., v. Witel, Inc.*, 1 F.3d 1201, 1205 (Fed. Cir. 1993), quoted in O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, in *PCLJ*, 2009, 401, 416.

(56) B. ROBINSON, *DHS Moves Forward with Reverse Auctions*, 2006, available at <http://few.com/articles/2006/10/12/dhs-moves-forward-with-reverse-auctions.aspx>, where it is reported that “The State Department recently said it had conducted 4,700 reverse auctions worth \$169 million, with a savings of close to \$18 million on what it had expected to pay for the items”. See also: C. R. YUKINS, *Use and Regulation of Electronic Reverse Auctions in the United States*, in S. Arrowsmith (ed. by) *Reform of the UNCITRAL Model Law on Procurement: Procurement Regulation for the 21<sup>st</sup> Century*, Danvers, 2009, 471 et seq.; C. R. YUKINS – DON WALLACE JR., *UNCITRAL Considers Electronic Reverse Auctions, as Comparative Public Procurement Comes of Age in the United States*, in *PPLR*, 2005, 183, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=711847](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=711847).

(57) Government Accountability Office, *Reverse Auctions: Guidance Is Needed to Maximize Competition and Achieve cost Savings*, December 2013 (henceforth “2013 GAO Report”), available at <http://www.gao.gov/products/GAO-14-108>.

(58) 2013 GAO Report at 21-22. The report explain that 27% of the auctions involved only one vendor in fiscal year 2012. The amount of fees paid to the private-sector operator for running these auctions was \$ 3.9 million.

(59) 2013 GAO Report at 2.

(60) 2013 GAO Report at 16.

(61) 2013 GAO Report at 19-20. The report states that during the procedure in one-quarter of cases studied non-price factors were used in the evaluation of bids.

(62) G. M. RACCA, *The Electronic Award and Execution of Public Procurement*, cit., 13-22; S. ARROWSMITH, (ed. by) *EU Public Procurement Law: an Introduction*, available at <http://www.nottingham.ac.uk>, 248.

tools need to become strategic in order to better enforce non-discrimination and transparency principles and favour cross-border participation. Correctly addressed, e-procurement and the dynamic purchasing systems<sup>(63)</sup> might improve participation and an open comparison of prices and contract conditions for the benefit of competition, efficiency and integrity.

#### **4. The U.S. experience in aggregation: risks to avoid in the EU**

In the EU system, techniques for joint procurement among government buyers were developed in different EU Member States even before they were called out as an option in the 2004 Directive.<sup>(64)</sup> According to the Directive, a Central Purchasing Body (CPB) can operate either as a wholesaler that buys in order to sell to other contracting authorities, or as an intermediary in charge of the award procedures, providing a catalogue of framework contracts which contracting authorities can use to purchase directly from the supplier.<sup>(65)</sup> Aggregate purchasing<sup>(66)</sup> has taken place on the basis of voluntary cooperation among several contracting authorities, or through contractual cooperation models such as alliances, consortia or corporate models.<sup>(67)</sup> Member States are free to define whether CPBs can operate only in specific sectors, or in predetermined product categories. The provision in the EC Directive 2004/18 referring to CPBs was designed to overcome barriers to cross-border procurement and to modernize and improve procurement systems for the purposes of efficiency and functionality.<sup>(68)</sup> Nonetheless the amount of aggregated procurement in

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(63) Directive No. 2004/18/EC, Art. 33. The new EU Directive on public procurement includes dynamic purchasing systems among the *techniques and instruments for electronic and aggregated procurement* in the Art. 34. See: EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, *cit.*, 31-32; EU Commission, *Evaluation Report Impact and Effectiveness of EU Public Procurement Legislation*, *cit.*, 24; G. M. RACCA, *The role of IT solutions in the award and execution of public procurement below threshold and list B services: overcoming e-barriers*, in D. Dragos – R. Caranta (eds. by) *Outside the Procurement Directives – inside the Treaty?*, Djøf Publishing, Copenhagen, 2012, 385-389.

(64) Directive No. 2004/18/EC, Wh. No. 15. S. ARROWSMITH, *The Past and Future Evolution of EC Procurement Law: From Framework to Common Code?*, *cit.*, 369. C. R. YUKINS, *Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting*, in *PCLJ*, 2008, 554.

(65) Directive No. 2004/18/EC, Art. 1, § 10; Directive No. 2014/24/EU, Art. 2, § 14.

(66) Directive No. 2014/24/EU, Wh. No. 59.

(67) G. M. RACCA, *Collaborative procurement and contract performance in the Italian healthcare sector: illustration of a common problem in European procurement*, *cit.*, 119-133.

(68) Directive No. 2004/18/EC, Wh. No. 15. CPBS would improve the professionalizing of procurements as they would have the specialised skills and expertise in running procurement transactions. CPBs are also better resourced to carry out procurement involving pursuit of strategic objectives (e.g. CPBs would have the expertise to evaluate complex or sophisticated tenders regarding new, innovative or eco-innovative products and services). a CPB can also use instruments for the digitalization of procuring documents and particularly to implement new procedures of selecting bidders such as e-auctions and framework agreements and can build archives of awarding data. S. ARROWSMITH, *Modernising the*

the EU remains extremely varied among Member States. In many Member States there is market closure not only on a national level, but often even on a regional or sub-regional level. This is true, even though it seems inefficient, from a transaction cost viewpoint, to conduct hundreds of thousands of low-value contracts, possibly resulting in a large variation of prices for very similar products (particularly for standardized commodities). This becomes evident whenever the number of economic operators active in a market is very limited. There may be little benefit in running thousands of competitions in which fewer than ten economic operators participate. From an integrity perspective, it would be hard to justify significant price differences of the same item, especially when the higher price paradoxically is paid by the large hospital that buys a bigger quantity in comparison with a small hospital that buys less and pay less.<sup>(69)</sup> A new approach for a complete and comprehensive vision of possible strategies for collaborative procuring policies is definitively needed.

Joint procurement and particularly CPBs can play a substantial role through market analysis and procurement strategies, changing the scale of the procurements envisioned and leading to significant savings in terms of administrative effort and the prices paid with public funds.<sup>(70)</sup> The new EU Directive observes

*“a strong trend emerging across Union Public Procurement markets towards the aggregation of demand by public purchasers, with a view to obtaining scale economies, including lower prices and transaction costs, and to improving and professionalizing procurement management. This can be achieved by concentrating*

*European Union’s public procurement regime: a blueprint for real simplicity and flexibility*, in PPLR, 2012, 71.

(69) Such an improper situation can be considered as a red flag for integrity of the agents involved (purchasers, politicians, etc.). The solution can be an effort to match contract prices to prices that have been determined to be justified, by the just started Italian spending review. The Italian Law Decree 6 July 2011, n. 98, Art. 17, (converted in Law 15 July 2011, No. 111) concerning the rationalization of health expenditure, confers on the Italian Observatory of public contracts (in the Italian Authority for the Supervision of Public Contracts) the task of publishing, from July 1<sup>st</sup>, 2012, reference prices for medical devices, drugs for hospital services, with the greatest impact on health care costs overall. See: [http://www.avcp.it/portal/public/classic/Comunicazione/Pubblicazioni/StudiRicerche/\\_prezzi\\_AmbitoSanitario](http://www.avcp.it/portal/public/classic/Comunicazione/Pubblicazioni/StudiRicerche/_prezzi_AmbitoSanitario). The same law provides that, if significant differences emerge between the reference price and the awarded price, there is an obligation to “renegotiate” the contract prices to align them with the reference prices. The rules identify as “significant differences” those greater than 20% from the reference price. See also Italian Law Decree, 13 September 2012, No. 158 (converted in Law 8 November 2012, No. 189), on the modality to calculate the reference prices and Italian Law 24 December 2012, No. 228 that, from the 1<sup>st</sup> January 2013, provided for the identification of medical devices. The subsequent case-law annulled the methods used for the identification of standard prices. See: T.A.R. Roma, III, 2 May 2013, No. 4399, 4401 and 4404. Recently a spending review Commissioner has been appointed, according to Italian Law Decree 21 June 2013, N. 69, converted in Law 9 August 2013, No. 98, see: [http://www.mef.gov.it/ufficio-stampa/comunicati/2013/comunicato\\_0173.html](http://www.mef.gov.it/ufficio-stampa/comunicati/2013/comunicato_0173.html).

(70) OECD, *Centralised Purchasing Systems in the EU*, 11 January 2011, available at [www.oecd-ilibrary.org/governance/centralised-purchasing-systems-in-the-european-union\\_5kgkqg703zw-en](http://www.oecd-ilibrary.org/governance/centralised-purchasing-systems-in-the-european-union_5kgkqg703zw-en); G. L. ALBANO – M. SPARRO, *Flexible Strategies for Centralized Public Procurement*, in *Review of Economics and Institutions*, 2010, 4-7.

*purchases either by the number of contracting authorities involved or by volume and value over time. However, aggregation and centralization of purchases should be carefully monitored in order to avoid excessive concentration of purchasing power and collusion, and to preserve transparency and competition, as well as market access opportunities for small and medium-sized enterprises.”*(71)

Moreover it is provided that “a Member State shall not prohibit its contracting authorities from using centralised purchasing activities offered by central purchasing bodies located in another Member State”.(72) Such provision open new perspective for EU joint procurement.

In the EU, the path towards aggregation in many Member States has just begun. The four-year limit of framework agreements and the trend favoring a second step of mini-competition among economic operators inside the framework could limit some of the abuse that occurred in the US, at least in the 1990s and the first years of this century, with the US equivalent of framework contracts.(73) Apart from the UK experience, the benefit and risks of aggregation in the EU are still unknown. Significant progress might be attained through building networks among EU CPBs that could effectively open new markets in specific sectors in the EU or at least part of it.(74) Notably, the new Directive says that “Member States shall not prohibit” their contracting authorities from taking advantage of other States’ CPBs’ activities.(75)

The chance to overcome national barriers could foster the fight against unsound procedures and corruption, defining benchmarks and appropriate prices.(76) The ‘Europe 2020’ strategy requires that public procurement policy ensure ‘the most efficient use of public funds and that procurement markets

(71) Directive No. 2014/24/EU, Wh. No. 59.

(72) Directive No. 2014/24/EU, Art. 39(2).

(73) C. R. YUKINS, *Are IDIQS Inefficient? Sharing Lessons With European Framework Contracting*, *cit.*, 561 et seq.

(74) Collaborative procurement in the EU through a network of CPBs is the object of the *Healthy Ageing and Public Procurement of Innovation* (HAPPI) project funded by the EU Commission (DG Enterprises) – rif. call ENT/CIP/11/C/N02C011 – within the framework of the Competitiveness and Innovation Programme (CIP). The project concern the EU joint procurement system in Healthcare. see: <http://www.happi-project.eu/>.

(75) Directive No. 2014/24/EU, Art. 39(2), where in regard to the issue of the Procurement implicating contracting authorities from different Member States the proposal Directive states that “A Member State shall not prohibit its contracting authorities from using centralised purchasing activities offered by central purchasing bodies established in another Member State”.

(76) S. ROSE-ACKERMAN, *International Actors and the Promises and Pitfalls of Anti-Corruption Reform*, *cit.*, 2013, 467, “Objective cross-country information about the possible results of corruption and inefficiency can help spur reforms in individual countries. International bodies could compile benchmark data on the cost and performance of public projects to alert potential whistleblowers and to provide ammunition to reformers”. J. DUGARD, *Corruption: Is there a Need for a New Convention?*, in S. Rose-Ackerman – P. Carrington (ed. by) *Anti-Corruption Policy. Can International Actors Play a Constructive Role?*, Carolina Academic Press, 2013, 159. “Corruption creates obstacles to the realization of social and economic rights and violates civil and political rights by weakening and sometimes destroying the political and judicial institutions that underpin democracy and the rule of law”.

must be kept open EU wide.' Obtaining 'optimal' procurement outcomes, generally reflected in the term 'value for money', through efficient procedures is of crucial importance in the context of the severe budgetary constraints and economic difficulties currently experienced by many EU Member States. The new Public Procurement Directive contains a Chapter on "*Techniques and instruments for electronic and aggregated procurement*". The approval of such rules could open new perspectives of cooperation and joint procurement among contracting authorities of different member States,(77) particularly among CPBs, consortia or alliances of procuring entities (rather than individual contracting authorities).(78) The promotion of value achieved through forms of joint procurement and professionalism in buying organizations would change the perspective on public procurement, providing a more meaningful picture of the market and offering the possibility of promoting innovation and sustainability policies.(79)

The rules provided in the new EU Directive encourage forms of public-to-public cooperation among contracting authorities, favoring the use of tools provided by the EU legal framework, like the European Groupings of Territorial Cooperation (EGTC).(80) In all cases of public-to-public cooperation (even between contracting authorities of different Member States) or occasionally joint procurement, the new EU Directive also clarifies the national law applicable and identifies the single contracting authority responsible for the contract activity covered by the cooperation.(81) The goals of efficiency and greater market opening are also linked to the increased use of electronic tools. The new Directive identifies CPBs as entities that can promote and encourage the use of electronic means in the Internal Market of Public Procurement, providing that "all procurement procedures conducted by a central purchasing body shall be performed using electronic means of communication".(82)

(77) Directive No. 2014/24/EU, Art. 39. G. M. RACCA, *Collaborative procurement and contract performance in the Italian healthcare sector: illustration of a common problem in European procurement*, in *PPLR*, 2010, 119.

(78) The EU founded projects especially for the public procurement of innovation favor such cooperation. See, for example, the call – rif. call ENT/CIP/11/C/N02C011 within the framework of the Competitiveness and Innovation Programme (CIP): the HAPPI project that provides EU networks of CPBs and joint procurement in the sector of "ageing well" and health innovative products and services (G. M. Racca) (<http://www.happi-project.eu/>).

(79) S. ROSE-ACKERMAN, *International Actors and the Promises and Pitfalls of Anti-Corruption Reform*, cit., 2013, 470. Where it is highlighted the relevance of professional networks to share ideas and to establish code of ethics, but also in the training of public officials.

(80) Directive No. 2014/24/EU, Art. 39 (5). About the European Groupings of Territorial Cooperation see EU Regulation 5 July 2006, No. 1082 and the amendments provided with the EU Regulation 17 December 2013, No. 1302.

(81) Concerning *centralised purchasing activities and central purchasing bodies* see Art. 37, for the *occasional joint procurement* see Art. 38; for *Procurement implicating contracting authorities from different Member States* see Art. 39.

(82) Directive No. 2014/24/EU, Art. 37(3).

In this regard, the US experience is quite interesting. After World War II, the US government created an agency, the *General Services Administration* (GSA), to buy commodities, such as office furniture, for all federal agencies. Use of GSA was mandatory, so that federal agencies were required to buy the covered supplies through GSA; they were not allowed to conduct their own procurements. GSA, being a monopoly, was widely viewed as not caring enough about what its customers (the agencies) really wanted, and complaints grew that GSA was offering poor service supplying low-quality products at high prices. The criticism increased when computer-related supplies came into use: if GSA was seen as doing a poor job providing high-quality office furniture at good prices, it was viewed as doing an even worse job providing computer-related goods. The legal framework allowed GSA to ‘delegate’ to agencies its authority for purchasing computer-related goods, but that only tended to reduce GSA’s importance. While some federal agencies may have been enthusiastic about this, the result was the disaggregation of public procurements in the important information technology (IT) arena. The 1990’s procurement reform encouraged agencies to create and use their own framework agreements, typically awarded to more than one economic operator; those contracts were called ‘multiple-award indefinite-delivery, indefinite-quantity’ contracts. Moreover, GSA lost its role as the mandatory source of supply, even for office supplies and other commodities. Instead, GSA was forced to compete with other agencies, in terms of both price and convenience, in the purchase of goods and services under its own framework contracts, the ‘Federal Supply Schedule’ (FSS). The FSS had its own regulation with special rules, special procedures and special issues. GSA focused on increasing the scope of items available on the FSS, vastly expanding the goods and services as well as the number of FSS contractors. Moreover, GSA began advertising, and worked hard to improve the service provided to other agencies, thus presumably earning the fee charged for using the FSS (which eventually dropped from one percent to 0.75 percent). The result was that in the years since 1994, the total sales under the FSS have increased from less than \$5 billion to close to \$40 billion.

In theory, GSA’s ability to offer low prices derives from the “Price Reduction” clause.<sup>(83)</sup> The clause, at least in principle, guarantees that the U.S.

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(83) The “price reduction” clause works by establishing a relationship (such as “equal to” or “lower than”) between a select group of schedule contractors’ commercial customers called the “basis of award”. Thereafter, when contractors lower their basis of award prices, they must correspondingly reduce their schedule price--although commercial transactions above a certain negotiated threshold called the “maximum order threshold” are exempt from the price reductions clause”. In a report regarding implementation of an Obama administration Executive Order ordering agencies to conduct an analysis of existing regulations in search of rules that may be obsolete or excessively burdensome, GSA wrote that the clause was a necessary mechanism. About this see: <http://www.fiercegovernment.com/story/gsa-changing-price-reduction-clause-not-feasible|2011-08-29>; General Services Administration, *Final Plan for Retrospective Analysis of Existing Rules*, August 18, 2011, available at: <http://www.whitehouse.gov/>

government will be getting the best price offered by the contractor to any of the defined class of costumers. In practice, its impact is far more limited, for reasons that go beyond the scope of this discussion. While the clause can ensnare contractors in difficult situations, including allegations of overcharging and even criminal fraud, the FSS continues to be criticized for not offering particularly low prices. There has also been widespread criticism that GSA's employees do not possess the skills needed to obtain good deals for the federal government, thus denying the agencies an expected benefit of a CPB.

Studying the U.S. experience can be useful to people outside the US, suggesting the risk of enforcing aggregation through provisions making purchase through a CPB mandatory. On the other hand, the U.S. experience does suggest the benefit of a CPB, since it avoids the need for a large number of transactions for the purchase of commodities. In addition, the U.S. experience, both with GSA's FSS and the multiple-contractor ID/IQ contracts,(84) underscores the importance of a second-step competition among the undertakings holding framework contracts, at least when a large purchase is planned.

### ***5. Integrity as the key to any procurement system: how to provide transparency and accountability***

Public procurement requires managing conflicting interests among stakeholders to achieve common goals, and it is very political by its nature. Buyers want to buy high-quality goods and services at the lowest price. Sellers want to sell goods at as high a price as possible, and elected "public officials" want successful completion of highly visible programs to help reelection. Citizens want quality public spending.(85) Government procurement might reflect more or less of any one of these interests depending on the political direction of the country; the US federal government procurement system functions as a

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*sites/default/files/other/2011-regulatory-action-plans/generalservicesadministrationregulatoryreformplan-august2011.pdf*. In US case law see: U.S. Court of Appeals for the First Circuit, *U.S. v. Data Translation, Inc.*, No. 92-1496, available at [http://www.leagle.com/decision/19922240984F2d1256\\_12007](http://www.leagle.com/decision/19922240984F2d1256_12007). In this judgment the Court analyses the literal language of the "discount disclosure" clause. See also: <http://www.fedmarket.com/contractors/GSA-Schedule-Price-Reduction-Clause>.

(84) C. R. YUKINS, *Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting*, *cit.*, 545 et seq.

(85) P. TREPTE, *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Public Procurement*, paper to OECD Expert Group meeting on Integrity in Public Procurement, 2005, available at [http://www.oecd-ilibrary.org/economics/transparency-and-accountability-as-tools-for-promoting-integrity-and-preventing-corruption-in-procurement\\_oecd\\_papers-v5-art34-en](http://www.oecd-ilibrary.org/economics/transparency-and-accountability-as-tools-for-promoting-integrity-and-preventing-corruption-in-procurement_oecd_papers-v5-art34-en). See also: OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, 2013, available at: [http://www.oecd-ilibrary.org/governance/implementing-the-oecd-principles-for-integrity-in-public-procurement\\_9789264201335-en;jsessionid=chfihfgm6ktoh.x-oecd-live-02](http://www.oecd-ilibrary.org/governance/implementing-the-oecd-principles-for-integrity-in-public-procurement_9789264201335-en;jsessionid=chfihfgm6ktoh.x-oecd-live-02), 24. The report highlights that weak governance in public procurement hinders market competition and raises the price paid by the administration for goods and services, directly impacting public expenditures and therefore taxpayers' resources, and points out that clean and effective procurement is key for sound stewardship of public funds.

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policy tool. Every procurement system has its “desiderata”:(86) nevertheless, these tasks and objectives are often in conflict. For example, efficiency and accountability can be at odds with one another, since the former requires that procurement work quickly and the latter tends to slow things down.

Sometimes, the use of the right tool can help reconcile these competing goals: for instance, when an agency competes and awards framework agreements, time may not be critical; but it may become critical when the orders are to be let, and the limited number of framework agreement holders can facilitate quick action at that stage.

Transparency is another significant goal, and challenge, in any public procurement system.(87) Transparency has been a core requirement of the US system for much more than a century: public opening of bids, for example, has been required since the 18<sup>th</sup> century. Today, except for small purchases, all upcoming procurements and all contract awards must be publicly posted on the single point of entry website, *www.fedbizopps.gov*.(88) However, a uniform system of public procurement records is still absent in the US, thus limiting effective transparency. A complete and easily accessible database system which would enable every citizen to access all the information related to a specific contract remains an elusive – and costly – goal. To a certain extent, the US system compensates for the weaknesses in transparency through the strength of its bid-protest complaint mechanism, in a sense providing transparency through the accountability system.

The principle of accountability in the US public procurement system has deep roots, going back at least to the 19<sup>th</sup> century. A central role has been played by the agency founded as the General Accounting Office (GAO), under the Budget and Accounting in 1921 (although its name changed in 2004 to the Government Accountability Office, the acronym is unchanged). Originally comprised basically of accountants and budget specialists watching over the federal accounts and books, its staffing and focus have changed, and it now concentrates on the efficiency and effectiveness of federal programs and activities.(89)

(86) S. L. SCHOONER, *Desiderata: Objectives for a System of Government Contract Law*, in *PPLR*, 2002, 103 et seq., where the author introduces nine goals frequently identified for government procurement systems: (1) competition; (2) integrity; (3) transparency; (4) efficiency; (5) customer satisfaction; (6) best value; (7) wealth distribution; (8) risk avoidance; and (9) uniformity.

(87) OECD, *Bribery in Public Procurement. Methods, Actors and Counter-Measures*, 2007, available at <http://www.oecd.org/investment/anti-bribery/anti-briberyconvention/44956834.pdf>, 55 et seq.

(88) The detailed rules for publicizing contract actions are set out in Part 5 of the FAR. D. I. GORDON, *Protecting the integrity of the U.S. federal procurement system: Conflict of interest rules and aspects of the system that help reduce corruption*, in J.-B. Auby – E. Breen – T. Perroud, *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 41.

(89) Now GAO reviews almost anything that the federal government does, whether domestically or overseas. It may examine the efficiency and effectiveness of national parks, just as it examines war expenditures by the military in Afghanistan, or the federal healthcare systems, or the space agency (NASA).

The GAO has also long played a role in providing accountability and transparency in the federal procurement system. Since the mid-1920s, dissatisfied bidders can file complaints, called ‘bid protests’, at GAO, which can lead to a decision by GAO on whether the contracting agency complied with procurement law and regulation. Today, bid protests can also be filed at a semi-specialized court in Washington called the Court of Federal Claims (COFC). (Over the years, different systems have been tried out, including allowing protesters to go to regular federal courts).

Both the GAO and the COFC focus on whether the contracting agency followed the law, and both have expertise in procurement law. At both the GAO and the Court of Federal Claims, protests may be filed either pre-award or post-award. Pre-award protests generally focus on whether a procurement is being conducted in a way that improperly restricts competition. Examples of improper restrictions on competition include an unduly short period for bidders to submit their tenders as well as specifications that unjustifiably exclude some firms from trying to meet the government’s needs. Post-award protests typically focus on whether the contracting agency, in selecting the winning tender, followed the criteria, weighting, and other rules set out in the solicitation.

It may be viewed as surprising that the bid protest mechanism, which represents the primary accountability mechanism for procurement in the US system, rarely uncovers cases of corruption. Dozens of times each year the GAO and the COFC, find that contracting agencies have violated procurement statutes or regulations – but they virtually never point to corruption (which would be referred to the Department of Justice for prosecution, in any event, rather than being addressed in a bid protest). Instead, a ruling against a contracting agency is generally based on the fact that the agency is not following the rules – for example, by weighting cost or other evaluation criteria differently from the weighting scheme called for in the solicitation. When the GAO or the COFC rules against a contracting agency, they will call for corrective action, which typically means going back to the stage in the procurement when the error occurred, fixing the error, and then re-doing the balance of the procurement. Neither forum will call for damages to be paid – the focus is on fixing the procurement, not compensating the bidder. It should be noted that an improperly awarded contract can be terminated in the U.S. system, and most protests are filed after the contract has been signed.

Corruption in the federal procurement system does seem to be relatively rare, when compared with reported corruption in other systems and even in local governments in the US. The one case that American procurement experts might cite as an example of corruption being considered in a GAO bid protest decision is exceptional in every sense: the Darleen Druyun case. Druyun, the highest level civil servant handling procurements for the U.S. Air Force, was

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accused of improperly turning to a senior official from the Boeing Company – a firm competing for Air Force contracts – to obtain a job for her daughter, her daughter’s boyfriend and, ultimately, herself.<sup>(90)</sup> That was clearly a case of corruption, and Druyun confessed to it as part of a plea bargain in court, before a protest came to GAO. Whether Druyun had actually steered any contracts to Boeing was, however, much harder to prove, partly because of the subjective nature of trade-offs in the U.S. procurement system, where Druyun, the official deciding which company’s bid was to be selected for award, had considerable discretion to exercise her judgment.<sup>(91)</sup> Lockheed Martin filed a protest at the GAO alleging that, in one particular competition, Druyun’s selection of Boeing should be overturned. While the GAO never explicitly found that Druyun had acted improperly in selecting Boeing over Lockheed Martin, it did conclude that she was actively involved in the selection of the contractor and that the taint of a corrupt official involved in a procurement was intolerable in terms of the harm it caused to the federal procurement’s system image of integrity; therefore, the GAO ruled in favor of Lockheed Martin.<sup>(92)</sup>

Nonetheless, the overall picture is one of limited corruption in the U.S. federal procurement system. Credit for that does not go primarily to the rules regarding conflicts of interest, but rather to the characteristics set out above. The U.S. has a long tradition of the rule of law – statutes and regulations – governing procurements; the existence of a professional acquisition corps means there are officials with training enforcing the rules, and any improper action requires cooperation from both those officials and others involved, thus complicating the task of anyone trying to corrupt the procurement process; the preference for competition and the requirement for transparency make it legally and practically difficult to direct awards to favored firms; and the extensive and open accountability mechanisms make hiding corrupt actions difficult.

That said, federal employees are covered by a complicated set of rules intended to address conflicts of interest and various other areas of concern. While the rules cover a range of subjects as diverse as the use of government property and restrictions on publishing written material, they are focused

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(90) See the congressional testimony on the matter, presented by the author in his role as a GAO official, *Air Force Procurement: Protests Challenging Role of Biased Official Sustained*, GAO-05-436T, April 14<sup>th</sup>, 2005. D. I. GORDON, *Protecting the integrity of the U.S. federal procurement system: Conflict of interest rules and aspects of the system that help reduce corruption*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 45 et seq.

(91) Perhaps alluding to the difficulty of determining the influence of subjective factors, Druyun stated, in what was essentially her confession, that she “believes that an objective selection authority may not have selected Boeing.” *Lockheed Martin Aeronautics Co. et al.*, B-295401 et al., February 24, 2005, at 4.

(92) *Lockheed Martin Aeronautics Co. et al.*, B-295401 et al., February 24, 2005, at 13-14.

largely on ensuring that federal officials do not use their public positions for private gain and that governmental actions are not affected by the personal interests of federal employees. Violation of the many legal rules can trigger both criminal and civil penalties; the key statute in this area is the Ethics in Government Act of 1978, as amended.<sup>(93)</sup> Under that Act and the implementing regulations, which are issued by the Office of Government Ethics (OGE), certain employees whose responsibilities include the exercise of discretion in areas considered sensitive, and that may include procurement, are required to file financial disclosure forms.<sup>(94)</sup>

It should be recognized that the U.S. allows actions that many would view as at least close to corruption. In particular, lobbying and contributions to political campaigns mean that large amounts of money pass between private actors and government officials. In the Supreme Court's decision in *Citizen United v. Federal Election Commission*, 558 U.S. 310 (2010), the Court struck down monetary limits on political expenditures by corporations, which only reinforced the culture of spending in the political arena by entities with economic interests at stake.

In the EU, accountability of public officials is left to national rules and there is no common European audit system.<sup>(95)</sup> With respect to the procurement system, the EU Remedies Directive has played an important role in ensuring that each Member State has a remedy mechanism for the undertakings to challenge procurement actions by contracting authorities. Nonetheless, the systems are neither uniform nor always appreciated. A common complaint is that the remedy systems often force the public to pay twice: once to the contractor providing the goods or services, and once to the unsuccessful tenderer that submitted a successful protest.<sup>(96)</sup> Critics argue that the Remedies Directive has led to a huge increase of litigation, with little improvement in how procurements are actually carried out.<sup>(97)</sup>

(93) Public Law 95-521, codified in various parts of the United States Code.

(94) 5 U.S.C. app. 4 §§ 101-111; 5 C.F.R. part 2634.

(95) EU Parliament – Directorate General for Internal Policies, *Political and other forms of corruption in the attribution of public procurement contracts and allocation of EU funds: Extent of the phenomenon and overview of practices*, cit., 31.

(96) S. TREUMER, *Damages for Breach of the EC Public Procurement Rule-Changes in European Regulation and Practice*, in *PPLR*, 2006, 159. See also other articles in the same issue of *PPLR* relating to national experience (France, Germany, United Kingdom, Sweden and Norway). After the implementation of the EC Directive No. 2007/66 see: S. TREUMER – F. LICHÈRE (eds. by), *Enforcement of the EU Public Procurement Rules*, Djøf Publishing, Copenhagen, 2011 and D. FAIRGRIEVE – F. LICHÈRE, *Damages as an Effective Remedy*, Oxford, Hart Publishing, 2011; H.-J. PRIESS – P. FRITON, *Designing Effective Challenge Procedures: the EU's Experience with Remedies*, in S. Arrowsmith – R.D. Anderson (eds. by), *The WTO Regime on Government Procurement: Challenge and Reform*, Cambridge, CUP, 2011, 511 et seq.

(97) G. M. RACCA, *Derogations from the standstill period, ineffectiveness and remedies in the new tendering procedures: efficiency gains vs. risks of increasing litigation*, in S. Treumer, F. Lichere (eds. by), Djof, 2011, 99. In the same book see: M. TRYBUS, *An Overview of the United Kingdom Public Procurement*

A particularly challenging provision in the Remedy Directive is the requirement for a mandatory standstill period from the award decision to the signing of the contract.<sup>(98)</sup> The purpose of provision is clear: once a contract has been signed, in most countries (unlike in the U.S.) it is generally too late to rescind it, so that a complaint mechanism cannot lead to the problem being fixed. Yet that laudable goal conflicts with the goal of efficiency, because it requires that every European procurement above the threshold must wait, for a minimum of 10 days, before it can move forward, in case someone wants to file a complaint.<sup>(99)</sup> The varying EU implementation means that in some countries, like the UK, this is a 10-day period, the minimum provided in the Directive, while in others, such as Italy, it is 35 days.<sup>(100)</sup> The result is that a huge number of procurements are blocked in order to allow redress of the few where errors may have occurred. Moreover, often the correction is not undertaken and further litigation occurs, with further delays.

The EU Remedy Directive underscores the importance of combating illegal direct awarding of contracts and award of contracts concluded in breach of the standstill period, which the Court of Justice of the European Union has defined as “the most serious breach of Community law in the field of public procurement on the part of a contracting authority”. The intent was to introduce effective, proportionate and dissuasive sanctions to address these problems.<sup>(101)</sup> The Directive provides for declaring a contract ineffective if it is the result of an illegal direct award and alternative penalties like fining the contracting authority or shortening the contract duration.<sup>(102)</sup> The Directive gives priority to correcting award procedures and admits compensation for damages only when it is no longer possible to award the contract to the economic operator who should have been entitled.<sup>(103)</sup>

The US experience of, on the one hand, excluding any possibility of awarding damages, and, on the other hand, providing that any unlawfully awarded

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*Review and Remedies System with an emphasis on England and Wales*, 232-233 and R. CARANTA, *Many Different Paths, but Are They All Leading to Effectiveness?*, 90-92.

(98) Directive No. 2007/66/EU amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts, Art. 2a, where a standstill period is provided to allow an effective review of the contract award decisions taken by contracting authorities; ECJ, 28 October 1999, *Alcatel Austria AG v. Bundesministerium für Wissenschaft und Verkehr* decision in C-81/98.

(99) Directive No. 2007/66/EU, Art. 2a (2). See also Wh. No. 5, where it is stated that “The duration of the minimum standstill period should take into account different means of communication. If rapid means of communication are used, a shorter period can be provided for than if other means of communication are used”, and Wh. No. 6, “The standstill period should give the tenderers concerned sufficient time to examine the contract award decision and to assess whether it is appropriate to initiate a review procedure”.

(100) Italian Public Procurement Code, d.lgs. 12 April 2006, No. 163, Art. 11, par. X.

(101) Directive No. 2007/66/EU, Wh. No. 13.

(102) Directive No. 2007/66/EU, Art. 2e (2).

(103) Directive No. 2007/66/EU, Art. 2e (2), third subpar.

contract can be terminated, could lead Europe towards a discussion on the question of finding a better way to address tenderers' complaints. Ultimately, a solution more like the U.S. one could reduce wasteful spending through damage awards, while better protecting the integrity of the public procurement system.

## 6. Conclusions

The scarcity of public resources requires joint efforts to obtain quality and improve public procurement performance. This is the common challenge of any public procurement system.

Procurement should be considered a strategic function of governments, promoting efficiency throughout the entire cycle from the need assessment, the tendering process and until the final payment.<sup>(104)</sup> Transparency, efficiency and accountability are the assumptions for integrity and a deeper understanding of the different procurement systems permits to highlight the criticalities and the diverse possible solutions.

The European experience of detailed Directives covering only the award phase, with a focus on maximizing objectivity, while understandable, has demonstrated weaknesses. The level of cross-border procurement remains low, and the objectivity of the award, while made cumbersome by the Directives' procedures, remains hard to ensure and often is overcome by the subjectivity of the scores. Moreover, both the focus on objectivity and the detailed nature of the Directives' rules betray a lack of confidence in public officials and in their integrity. In effect, integrity issues in the EU often arise behind the curtain of objectivity, which apparently frees the public official of any liability in the "objective" choice. This apparently objective choice turns into both a lack of accountability in the execution phase and the tolerance of infringements. Often, behind such results there is simply incompetence, but sometimes also malice and corruption. The result for the citizens is in any case a waste of public funds and performance of poor quality.

The EU approach of awarding damages in case of illicit award, presumably to overcome market closure and foster competition, has not proved effective. The procurement remedies system may thus be providing the worst of both worlds: increased litigation with the taxpayers footing the bill, without ensuring effective competition or the quality of spending. A strong political commitment to attaining efficient and sound procedures in the EU is still

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(104) OECD, *Recommendation of the Council on Enhancing Integrity in Public Procurement*, C(2008)105, 2008, available at <http://acts.oecd.org/>, "the Recommendation provides policy makers with Principles for enhancing integrity throughout the entire public procurement cycle, taking into account international laws, as well as national laws and organisational structures of Member countries".

necessary, especially when implementing the new Directives. The different models of joint procurement could ensure improvement of efficiency and of professionalism that should enhance quality of spending and integrity. The US federal procurement system places heavy emphasis on competition, transparency, and accountability. The US has a long tradition of citizen skepticism about government and its merit and, perhaps due to that, it has an equally long tradition of insisting on openness in procurement.<sup>(105)</sup> Yet the US system struggles to provide better quality data on procurement and performance analysis that could improve transparency and effective oversight.<sup>(106)</sup>

The integrity of the public procurement system is related to the qualities of the people involved, either politicians or agents from the public sector, as well as economic operators from the private sector. The compliance systems for the private sphere and the audit and remedy/protest system for the public sphere seem to be the main instruments for pursuing integrity and efficiency. While public procurement systems in both the EU and the US have improved and been modernized over the past quarter century, all the stakeholders, and above all the citizens, have the right to insist on a procurement system that is transparent and efficient, with modern tools, and that delivers high-quality, reasonably priced goods and services to fulfill the government's obligations. Citizens in every country deserve a system that not only functions with integrity, but is seen to do so.

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(105) For examples of 18<sup>th</sup> century public requests for proposals, see JAMES F. NAGLE, *History of Government Contracting* (2<sup>nd</sup> ed. 1999). See: D. I. GORDON, *Bid Protests: The Costs are Real, but the Benefits Outweigh Them*, in *PCLJ*, 2013, accessible also at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2228748](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2228748). and the Report of GAO, *Bid Protests: Trends and Analysis*, August 9, 2013, at <http://www.fas.org/sgp/crs/misc/R40227.pdf>, where some interesting data are reported concerning the trend of bid protest in the US federal system.

(106) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, 2013, *cit.*, 46.



## CHAPTER 2

### Regulating discretion in public procurement: an anti-corruption tool?

BY

Paula BORDALO FAUSTINO

Lawyer and Ph.D. Candidate, University of Nottingham

#### *1. Setting the scene*

One of the reasons why public procurement appears to be susceptible to corruption has to do with the rather wide discretion, which is inherent to the performance of the procurement function. This provides procurement officers with an opportunity to engage in corrupt practices. The likelihood of corruption occurring within the public procurement context is, therefore, often associated with the amount of discretion procurement officers are allowed at each stage of the procurement procedures.<sup>(1)</sup> However, despite giving rise to the opportunity for corruption, it is submitted that the existence of a fairly large margin of discretion is not necessarily a direct cause of corruption: it is the abuse of that discretion that may constitute a corrupt practice.

In line with this view, it has been suggested that putting in place some type of procurement regulation minimizes *per se* the opportunities for corruption.<sup>(2)</sup> Both EU and national legislators have pursued the implementation of preventive measures in order to limit or remove discretion, where it is likely to allow room for corrupt practices to occur. These measures are frequently, but not exclusively, linked to transparency and accountability requirements.<sup>(3)</sup> One procurement feature that seems particularly prone to abuse of discretion is the setting up, disclosure and application of the most economically advantageous tender (MEAT) criterion.

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(1) G. WARE – S. MOSS – E. CAMPOS – G. NOONE, *Corruption in Public Procurement: A Perennial Challenge*, Ch. 9 in E. Campos – S Pradhan (eds. by) *The Many Faces of Corruption*, Washington DC, World Bank, 2007, 296.

(2) P. TREPTE, *Transparency and Accountability as Tools for Promoting Integrity and Preventing Corruption in Public Procurement*, paper to OECD Expert Group meeting on Integrity in Public Procurement, 2005, 13.

(3) For example, the requirement to keep records of decision making in public procurement procedures ad to allow access to those documents by interested parties (Directive 2014/24/EU, Wh. 126).

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The fight against corruption has recently been reiterated as a general goal of the existing and forthcoming public procurement policy at EU level in the *Green Paper on the Modernisation of EU Public Procurement Policy*,<sup>(4)</sup> as well as in the *Commission Staff Working Paper: Executive Summary of the Impact Assessment*.<sup>(5)</sup> These documents follow up on previous EU legislative acts and case law<sup>(6)</sup> by referring to the need to avoid arbitrary decisions by contracting authorities when using the award criteria. These criteria should not confer an unrestricted freedom of choice on the contracting authority, nor allow favoritism of some economic operators to the detriment of others. On the one hand, Art. 67(4) of Directive 2014/24/EU now expressly forbids the said unrestricted freedom of choice.<sup>(7)</sup> On the other hand, that same provision requires award criteria to be set up and applied in such a way as to ensure the possibility of effective competition,<sup>(8)</sup> which matches the prohibition of artificially narrowing competition provided under Art. 18 as a procurement principle.

When transposing EU legislation on public procurement in general, and award criteria provisions in particular, different Member States choose different techniques. Some limit themselves to reproducing the provisions in question, others add to them. It seems apparent that the choice of transposition technique and the nature of the additional provisions reveal the national legislator's approach to regulating public procurement. When it comes to dealing with discretion, mainly as regards the use of the award criteria, it is argued that national provisions tend to reflect the values of the national legal culture, which inspires the regulatory response to corruption. Member States where the risk of corruption is perceived to be low usually allow greater discretion to procurement officers, whereas Member States where the risk of corruption is perceived to be higher tend to reduce or eliminate discretion in the field of public procurement award criteria.

However, the decision to regulate discretion may also stem from a non-corruption related objective: the need to prevent the misuse of discretionary powers. Misuse of discretion by procurement officers, in particular as regards the award criteria, may be due to incompetence or lack of capacity, which does not necessarily amount to corruption. There is no direct evidence to support

(4) COM (2011) 15 final.

(5) Accompanying the document *Proposal for a Directive on Public Procurement* (SEC (2011) 1586 final).

(6) ECJ, 20 September 1988, *Gebroeders Beentjes BV v Netherlands*, in Case C-31/87, 1988, E.C.R. 4635, par. 26; ECJ, 18 October 2001, *SIAC Construction v County Council of the County of Mayo*, in Case C-19/00, 2001, E.C.R. I-7725, par. 37; ECJ, 17 September 2002, *Concordia Bus Finland v Helsinki*, in Case C-513/99, 2002, E.C.R. I-7213, par. 61 and 64; ECJ, 24 November 2005, *ATI EAC Srl e Viaggi di Maio Snc and Others v ACTV Venezia SpA and Others*, in Case C-331/04, 2005, E.C.R. I-10109, par. 21.

(7) This had previously been mentioned in Wh. (1) of Directive 2004/18/EC.

(8) The requirement to assess tenders in conditions of effective competition had previously only been mentioned in Recital (46) of Directive 2004/18/EC.

the idea that more regulation necessarily leads to less corruption or better procurement practices. In fact, imposing stricter regulation might have as a consequence<sup>(9)</sup> the impossibility for procurement officers to properly exercise their discretion, and ultimately their procuring function. So, by focusing solely on the amount of discretion that is available to procurement officers, procurement regulation risks neglecting ways to prevent the abuse of the discretionary powers.

Furthermore, by over-regulating public procurement and over-limiting discretion, it is suggested that the job of a procurement officer might turn into a mechanical application of rules. This, in turn, may have negative impacts in terms of accountability: procurement officers are more likely to make 'bad' procurement decisions but are less capable of being held accountable as long as they follow the rules (since they have been deprived of any discretionary judgment). On top of that, from a behavioral perspective, it is argued that over-regulating and making it harder to exercise discretion might actually constitute a motivation for procurement officers to make an extra-effort to circumvent the rules in order to engage in corrupt practices.

## 2. Discussion

The first topic for discussion considers the relationship between the provisions on the MEAT and related topics such as: the definition of technical specifications, the issue about the conditions for the performance of a contract, the extent of the required link to the subject matter of the contract, and the impact of the level of disclosure of the award criteria. The variable degree of discretion allowed at each step of the procurement procedures may be rooted in the sheer fear of its abuse/misuse (i.e. limiting discretion as a generic anti-corruption tool), or it may actually aim to curb the said abuse/misuse in view of preventing specific corrupt practices arising.

Secondly, a more detailed look at Art. 67 of Directive 2014/24/EU<sup>(10)</sup> on contract award criteria is required. In fact, this recent directive has brought about changes on the topic of discretionary powers associated with the use of award criteria. New rules have been put forward in order to guide contracting authorities on 'how to buy'. For instance, new award criteria are specifically referred to for the first time – e.g. life-cycle costing (including the production process), social and innovative aspects, trading and its conditions, and experience of staff assigned to performing the contract. Art. 67(3) of Directive

(9) F. ANECHARICO – J. JACOBS, *The Pursuit of Absolute Integrity: How Corruption Control Makes Government Ineffective*, Chicago, University of Chicago Press, 1996, Preamble.

(10) Former Directive 2004/18/EC, Art. 53.

2014/24/EU is also original in providing a legislative presumption of the requirement regarding the link to the subject matter of the contract, which favours a broader understanding than had previously been implied.<sup>(11)</sup>

These changes impact on the degree of discretion procurement officers are allowed when setting up and applying the award criteria.<sup>(12)</sup> At first sight, they seem to represent an increase of procurement officers' margin of discretion regarding the choice of award criteria and the extent to which they are still considered to be linked to the subject matter of the contract. This linkage requirement seems to act as the ultimate safeguard regarding the abuse/misuse of discretion when setting up the award criteria. However, the doubt remains as to whether this type of regulatory framing of discretion is likely to give rise to opportunities for corruption.

In the third place, another subject that begs to be discussed is the variety of national regulatory approaches to shaping discretion in the context of public procurement procedures covered by the EU directives, especially as regards the use of award criteria. Illustrations from two country case studies are considered: the UK and Portugal. On the one hand, in Portugal there is a tendency to take a rather restrictive approach to discretion. Therefore, the Portuguese legislator has opted to structure discretion regarding the use of award criteria to a considerable extent (e.g. prohibited award criteria; mandatory rules on evaluation methodology; very demanding disclosure requirements). On the other hand, procurement officers in the UK tend to be allowed a more flexible exercise of their discretion for the benefit of value for money (e.g. very limited requirements; no mandatory rules on evaluation methodology; de minimum disclosure).

The comparison between these two Member States allows an insight on the national legislators' attitude towards the issues of abuse/misuse of discretion which may lead to corruption. This attitude is thought to be shaped by each country's legal culture and perception of the probability of occurrence of the said abuse/misuse of discretion.

### *3. Tentative conclusions*

Regulating discretion in the context of public procurement has been used as a tool to address corruption. Examples can be found both at EU and national levels. However, it is submitted that "legislative corruption proofing" by means of reducing or eliminating discretion, specifically in the field of award criteria,

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(11) See Directive 2004/18/EC, Wh. 46.

(12) See also the mandatory methodology for evaluating the life-cycle costing criterion (Directive 2014/24/EU, Art. 68(3)).

might be motivated by a blind fear of corruption, rather than an informed effort to prevent specific abuses/misuses of discretion which are susceptible of providing opportunities for corruption.

Furthermore, brand new opportunities for corrupt practices might actually be a result of over-regulating discretion (e.g. by creating textual ambiguities behind which procurement officers might seek to hide). Finally, it is proposed that monitoring the use of discretion (namely by placing part of the monitoring function with the tenderers) and enforcing sanctions for the abuse/misuse of discretion might prove more efficient in terms of curbing corruption.

In any case, taking into account that EU regulation is meant to be applied in all Member States, whose national legal cultures are so diverse, it is argued that Member States should be allowed enough regulatory room to choose different approaches to regulating discretion and addressing corruption in the field of public procurement.



**PART III**

**Corruption and Collusion  
in Public Contracts**

BRUYLANT



# CHAPTER 1

## Demand aggregation and collusion prevention in public procurement

BY

Gian Luigi ALBANO

Consip S.p.A., the National Central Purchasing Body, Italy

AND

Department of Economics and Finance,  
University LUISS “G. CARLI” – Rome

### *1. Introduction*

Collusion among suppliers is a major problem for most types of procurement, even though some procurement managers appear still not to be aware of it, let alone to have the necessary skills to recognize which aspects of procurement design tend to have the strongest impact on the risk of collusion. A comment by Graham and Marshall almost three decades ago sounds, in fact, quite current:

*“So prevalent are rings, in fact, that a retired auctioneer once noted that in 40 years of auctioneering, he had yet to attend an auction at which a ring was not present.”*<sup>(1)</sup>

Procurement, be it public or private, is even more subject to the problem than other types of auctions, because suppliers typically interact repeatedly for a long time, know each other well and can coordinate their offers thanks to the transparency of procurement processes, especially those carried out by public entities. It would be fair to say, though, that the role of transparency in facilitating collusion appears to be overestimated as many other features of public procurement markets tend to facilitate cartels’ success so that very little information is in fact needed to enforce anticompetitive agreements.

This chapter will look closely at one specific aspect of public procurement design, namely the degree of demand aggregation and some of its concrete organizational features, and the extent to which this affects the degree of competition in procurement markets. In carrying out such an exercise the reader ought to bear in mind that *i*) very little theoretical research has been

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(1) D. GRAHAM – R. MARSHALL, *Collusive Bidder Behavior at Single-Object Second-Price Auctions*, in *Journal of Political Economy*, 95, 1987, 1221.

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devoted to this topic, let alone empirical investigations; and *ii*) many forces come into play when designing procurement processes so that predictions stemming from stylized economic models often tend to leave aside the most relevant issues, at least from the point of view of those sailing in the stormy weather of real procurement processes.

Demand aggregation does affect competition in public procurement markets by altering the number and the value of “prizes” firms compete for. Moreover, it affects the participation patterns through the tightness of economic requirements. Both aspects are relevant for cartels’ formation and strength.

It is customary to listen to self-declared experts on public procurement using “demand aggregation” and “centralization” interchangeably. This cannot be more distant from *real* procurement design. For instance, the Austrian Federal Central Purchasing Body, *Bundesbeschaffung* (BBG), aggregates a considerable fraction of public bodies’ needs for foodstuffs and awards framework agreements, each one split into more than 90 (!) geographical lots.

Lots design is then the reverse side of the demand aggregation medal. It is one of the most sensitive aspects of procurement design since, if appropriately conceived, it may allow public buyers to reach, at least from an *ex-ante* perspective, an acceptable compromise between savings considerations and the risk of collusion, while promoting the participation of smaller firms in competitive procurement.

Joint bidding is usually considered another effective device facilitating the participation of smaller firms in competitive procurements, even for sizeable contracts. But while vertical consortia among firms are normally considered pro-competitive, horizontal consortia may disguise collusive agreements. Thus, one is left wondering whether it would be more effective to regulate the criteria for consortia formation rather than leaving market forces unleashed and then having antitrust authorities bear the brunt of uncovering any anti-competitive behavior. Finally, we will look at some competition concerns that may arise when demand aggregation is carried out by using framework agreements, as provided by the Directive 2014/24/EU of the European Parliament and of the Council on public procurement.<sup>(2)</sup>

## ***2. The basic economic forces of collusion in public procurement***

Although we all seem to have an intuitive rather than structured idea of what collusion in procurement markets means, it is worth adopting a practical definition for the purpose of the current chapter. Collusion in procurement

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(2) The Directive is available at [http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L\\_2014\\_094\\_R\\_0065\\_01&qid=1396257739781&from=EN](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_2014_094_R_0065_01&qid=1396257739781&from=EN).

markets can be thought of as any conduct adopted by a group of firms that aims at reproducing or approximating the market outcome induced by single, dominant firm. To achieve this objective, according to Stigler (1964)'s seminal contribution,(3) firms need to:

- coordinate their strategies (either tacitly or explicitly);
- determine how to share the collusive profit among themselves;
- punish deviant behavior, that is, retaliate against those breaching the collusive agreement.

Since many of the mechanisms for bid coordination have been discussed elsewhere,(4) in this chapter we will limit ourselves to emphasize that public procurement markets seem to possess intrinsic features that make cartels more stable and/or make cartel formation more likely than in other oligopolistic markets. We can identify a minimal set of pro-collusive characteristics.

*Demand predictability.* Many procurement contracts are instrumental to the daily functioning of public organizations (e.g., telephone services, IT and medical equipment, building and road maintenance). Although downturns in the business cycle also affect public spending, public demand arguably remains more predictable than private demand.

*Barriers to entry.* In public procurement, barriers to entry may stem from different sources. Economic and technical participation requirements adversely affect mostly smaller businesses. Moreover, submitting a tender *per se* requires a specialized (mainly, administrative) expertise, requiring dedicated personnel. Being fixed, participation costs hurt smaller firms more than bigger ones. In concessions for public services, barriers to entry are endemic due to the amount/quality of information about the service gathered by the concessionaire over a long period of time. Thus non-incumbent firms may refrain from bidding for concessions simply because of a lack of information necessary to draft a sustainable business plan.

*Fixed quantities.* In general, cartels suffer from an inherent instability since cartel members have an incentive to cheat on the agreed prices *and/or* quantities, for example, by selling below the agreed price or outside their assigned territory. Consequently, cartels have to spend substantial resources to monitor cartel members' behavior. Cartel enforcement becomes less costly in public procurement since public authorities typically announce that they will contract out a fixed number of units; as a result, demand does not depend on submitted prices and participating firms need to focus mainly on the financial dimension of the tender.

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(3) G. J. STIGLER, *A Theory of Oligopoly*, in *Journal of Political Economy*, 72, 1964, 44-61.

(4) See Chapter II and III (Part III) in this book; and R. C. MARSHALL – L. M. MARX, *The Economics of Collusion*, The MIT Press, 2012, for a thorough and enlightening (non-technical) analysis of the economic forces of collusion.

*Demand fragmentation.* Similar, albeit non-identical, contracts are awarded every year by a large number of public authorities. In Italy, as of 2013 the National Authority for Public Contracts (known with the acronym of Avcp) served more than 15,000 contracting authorities, that is, public organizations that can carry out procurement procedures. Were these to buy similar products/services independently of each other, public demand would in fact be split in thousands of separate lots, which would make market sharing agreements quite cozy. Thus for any given value of aggregated public demand, the higher the level of demand fragmentation – that is, the higher the number of procurement processes – the easier the risk of collusion among firms. However, a potentially counterbalancing effect is triggered by public demand being chopped in a higher number of contracts. As the average contract value declines more (smaller) firms are in a position to participate – due to less stringent economic requirements – thus enlarging the set of *potential* bidders.

*Market transparency.* Stigler originally noted that “[t]he system of sealed bids, publicly opened with full identification of each bidder’s price and specifications, is the ideal instrument for the detection of price-cutting”.<sup>(5)</sup> Transparency of procurement processes may facilitate collusion since a cartel can promptly identify and punish defecting firms. While transparency is widely advocated as an effective strategy to raise the accountability of public procurement officials, thus reducing the risk of corrupt practices, the availability of large amounts of information may strengthen collusive agreements.

*Scoring rules.* There exist technical aspects of procurement design that may provide, at least marginally, incentives to cartel formation that usually go unnoticed, or more unnoticed than other aspects. Scoring rules are one of those. Scoring rules are mathematical algorithms used to evaluate and rank tenders when the public contract is awarded to the economically most advantageous tender (a.k.a. best value for money) criterion. Scoring rules transform monetary bids into a neutral score. In some cases, each bidder’s economic score depends both on its own tender and on a subset of other bids (possibly all). In particular, when bids are ranked according to their distance from the (simple) average of all bids, firms may have a further incentive to coordinate their strategies.<sup>(6)</sup>

### 3. Demand aggregation and the risk of collusion

In this section, we will further explore to what extent demand aggregation, whatever organizational form it may take, can exert a tangible impact on the degree of competition in procurement markets. We will emphasize that the

(5) G. J. STIGLER, *A Theory of Oligopoly*, cit., 48.

(6) See G. L. ALBANO – M. BIANCHI – G. SPAGNOLO, *Bid Average Methods in Procurement*, in *Rivista di Politica Economica*, 2006, 41-64.

“optimal” degree of demand aggregation should fall on the spectrum between full decentralization and full centralization, the actual position depending on many circumstances and possibly evolving over time.

Buying in bulk may in principle benefit public buyers, since suppliers are in a position to exploit economies of scale, thus operating at a lower unit cost. Economies of scale arise whenever production costs comprise a sizeable fraction of fixed costs, that is, of costs that are independent of the production scale. By increasing production firms are able to operate at a lower *unit* cost. Lower production costs, however, may yield lower purchasing prices *only if* the buyer keeps intact or increases its bargaining power. In those markets where the public sector accounts for a relevant share of the total demand, aggregation *and* contract standardization can put the awardee of a single competitive tendering in a position to significantly increase its market share. This strengthens the public agency’s bargaining power, thus pushing suppliers to compete more fiercely to deliver higher value for money. Yet two forces conflict with each other. For a *given number* of competitors, demand aggregation leads to fiercer competition via an enhanced winner-take-all effect. However, as the size/value of contracts gets larger, smaller firms may find it impossible to participate in the competitive processes – because of more stringent economic participation requirements – thus leading to a lower number of competitors. Consequently demand aggregation does lead to higher savings only if the (adverse) participation effect is less intense than the buyer’s stronger bargaining power. The main lesson is, then, that any savings-driven demand aggregation strategy ought to be designed by anticipating the composition of the relevant market resulting from that specific strategy.

Policy makers, at least at the EU level, seem to be aware of the main costs and benefits of demand aggregation, as noted in the current proposal for a revised European Directive on public procurement:

*“[T]here is a strong trend emerging across Union public procurement markets towards the aggregation of demand by public purchasers, with a view to obtaining economies of scale, including lower prices and transaction costs, and to improving and professionalising procurement management. This can be achieved by concentrating purchases either by the number of contracting authorities involved or by volume and value over time. However, the aggregation and centralisation of purchases should be carefully monitored in order to avoid excessive concentration of purchasing power and collusion, and to preserve transparency and competition, as well as market access opportunities for small and medium-sized enterprises.”*<sup>(7)</sup>

The analysis undertaken so far addresses EU policy makers’ concerns by highlighting under what circumstances demand aggregation may generate benefits to the whole system. However, this potential advantage may come at a cost.

(7) <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0896:FIN:EN:PDF>, 19.

By reducing participation and competition, demand aggregation may facilitate anti-competitive behaviour.<sup>(8)</sup> Conversely, demand fragmentation could foster participation and competition. Consequently, the potential benefits from demand aggregation in terms of savings may be wiped out by a higher risk of collusion that adversely affects savings. As often happens, practice is a much better teacher than highly sophisticated theory.<sup>(9)</sup> “Smart” procurement would require being able to anticipate how the degree of aggregation affects the relevant market, that is, how it affects the number of potential participants. Thus market intelligence and experience (i.e., recording and analysing participation patterns over time) are crucial to fine-tune the appropriate degree of demand aggregation.

Consider, for instance, the case of a particular type of medical equipment such as ultrasound machines. The procurement market in Italy is characterized by around 800-1000 potential buyers (mainly hospitals) and 6 (big) producers. Now one need not be a world-known expert to jump to the (correct) conclusion that a complete demand fragmentation – namely, each potential buyer carrying out its own procurement process – would be bliss for producers/suppliers. Thus some degree of demand aggregation would benefit public buyers and, ultimately, taxpayers.

Aggregation is not, however, a panacea. In fact, one commonly made mistake is the assumption that aggregating demand leads almost inevitably to a one single contract being awarded. In practice, aggregating the demand of several public organizations does not necessarily require awarding one contract whose value is equal to the sum of the single demands. There are in fact potentially many solutions to split the aggregated demand into lots. The EU policy makers also emphasize this last point when stating that:

*“[...] to enhance competition, contracting authorities should in particular be encouraged to divide large contracts into lots. [...] Where contracts are divided into lots, contracting authorities should, for instance in order to preserve competition or to ensure reliability of supply, be allowed to limit the number of lots for which an economic operator may tender; they should also be allowed to limit the number of lots that may be awarded to any one tenderer[...]”*<sup>(10)</sup>

At least three competition-relevant aspects stand up from the text above. Splitting contracts into lots may favour participation by lowering the economic requirements that often hamper the entry of smaller firms into the public procurement market. Second, smaller firms may target those lots where they

<sup>(8)</sup> See, for instance, The Office of Fair Trading, *Assessing the Impact of Public Sector Procurement on Competition*, 2004, 16-20 and 110-125.

<sup>(9)</sup> Most of my thoughts on this subject are borrowed more from my everyday practice as a supervisor of centralized procurement strategies in Italy rather than my background as a Lecturer in Economics. So, at least in this case, I am unashamedly proud of eating my own cooking.

<sup>(10)</sup> Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC.

may enjoy a competitive advantage (say, for logistics-related reasons) with respect to bigger firms. Third, bigger firms are in a position to bid for a bundle of lots so as to maximize the return from economies of scale. However, multiple lots *per se* do not guarantee multiple awardees. That is, it may still be the case that one single (possibly big) firm is awarded all lots. For this reason, the EU policy makers seem to be keen to allow public buyers to make use of a tool ensuring a minimum set of awardees. These two aspects of division into lots and participation/award limit will be the object of the next section.

#### 4. Lots and Competition

As briefly mentioned above, demand aggregation does not necessarily imply awarding one *single* contract. There are at least three main efficiency-driven reasons for splitting a contract into lots:

- *Higher level of competition.* Small firms may compete on a subset of lots thus putting competitive pressure on bigger firms.
- *Benefits from specialization/know-how.* Small firms that traditionally operate in limited geographical areas adapt themselves more quickly to local buyers' changing needs or simply better fulfil local buyers' requirements (say, in terms of logistics).
- *Reduced risk of lock-in.* The higher the degree of competition for each lot (as measured by the number of actual distinct bids) the higher the level of contestability over time, thus the more likely that the supply base will not collapse to a few or, at the limit, to one (big) firm. Obviously, this potential benefit has to be weighed against the cost of switching from one contractor to another.

Once procurement designers are comfortable that demand aggregation should not lead to one single public contract, a new set of problems arises. The first and probably the most important decision concerns the optimal number of lots.<sup>(11)</sup> The second involves the nature of the awarding mechanism used by, say, a centralized agency to award multiple lots, that is, whether different contracts are to be awarded sequentially rather than simultaneously.

##### 4.1. The nature of the awarding mechanism

Sequential (lowest-price) competitive tendering procedures for multiple objects are very common in public procurement. Contracts for different but related goods (for example printers, laptops, desktops, monitors, servers) are

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(11) We will not elaborate on this topic since a number of existing contributions have already explored it in depth. See, above all, N. DIMITRI – G. PIGA – G. SPAGNOLO (eds. by), *Handbook of Procurement*, Cambridge University Press 2006, Chapters 7 (“Division into Lots and Competition in Procurement”) and 14 (“Preventing Collusion in Procurement”).

typically awarded separately, that is, sequentially. There are two ways in which a sequential format may ease a collusive agreement among bidders, compared to a simultaneous one. The first, intuitive collusive drawback of a sequential competitive procurement is linked to the ability of cartel members to identify defections and react faster, within the same sequence. This is because in many real world sequential (selling) auctions and procurement tendering procedures, a large amount of information is usually disclosed at the end of each competitive stage, including firms' rankings and prices. Quick detection limits the defector's short run gains, making the enforcement of collusion in the sequential format easier than in a simultaneous one. In the case of procurement of related goods, this effect can be seen as an increase in the frequency of interaction. It is stronger the larger the number of related goods sequentially procured (or the smaller the lots in which a given divisible good is fractioned before being procured). The second effect is linked to the possible asymmetry among colluding suppliers. The viability of cartels is often limited by the presence of so called "mavericks", that is, firms that are difficult to restrain as they have more to gain from undercutting a cartel (or less to gain from being part of it). If tenderers are not alike – be it in terms of market shares, efficiency or access to the credit market – a sequential competitive tendering can facilitate collusion by allowing the ring to soften the maverick's aggressiveness by "splitting the cake" so as to allocate the maverick the last object(s) in a given sequence. This minimizes the maverick's incentive to defect and improves the viability of the ring.

So is there any sensible guidance for public procurement designers if they cannot modify the awarding mechanism, that is, if they are unable to award all lots simultaneously? It has been shown<sup>(12)</sup> that a simple and effective strategy against collusion is a "large-lot-last" policy, that is, tendering the most valuable lot at the end of each sequence, so that the largest deviation cannot be punished before a new sequence of procurement lots starts, which may happen much farther into the future. Since the value of each of the lots procured and their place in the sequence are typically decisions in the hands of the procurer, implementing such a policy appears rather easy.

#### 4.2. From static competition to dynamic competition: award or participation limits?

Let us suppose that a centralised public procurement agency (CPPA) is in the (arguably comfortable) position to determine the optimal level of demand aggregation that would maximize the value of savings *today*. Is it always in

(12) G. L. ALBANO – G. SPAGNOLO, *Asymmetry and Collusion in Sequential Procurement: A Large Lot Last Policy*, in *The B.E. Journal of Theoretical Economics*, Vol. 10, 2010, 1-18.

the CPPA's interest (assuming that the latter's objective function consistently aggregates the objective functions of those public bodies using the CPPA's purchasing arrangements) to adopt a short-term approach to savings maximization? Said differently, to what extent are the aggregation strategies today likely to affect the attainable levels of savings *tomorrow*?

There are at least two good reasons to adopt a longer-horizon approach to competition in public procurement, namely to recognize that the level of participation (and thus the level of competition) *today* affects the level of participation (and, again, the level of competition) *tomorrow*. First of all, participation is costly. Thus bidding unsuccessfully over time for public contracts may become financially too burdensome, especially for smaller firms, which may be forced to stop bidding. As the set of potential participants shrinks over time, the risk of anti-competitive behaviour among the surviving firms becomes, *ceteris paribus*, more than a theoretical matter. Secondly, in procurement markets for specialized services such as ICT services, contractors are able to learn over time crucial information that may help them increase the likelihood that they will be awarded future contracts. This is a documented form of know-how-driven lock in that may adversely affect participation over time. (13)

The considerations set forth above suggest that, in some circumstances, the buyer may find it profitable to limit the degree of competition today in order to preserve a sufficiently high level of participation and competition tomorrow. To be sure, the provision in the current (albeit provisional) text of the European Directive for public procurement, whereby public buyers may use award or participation limits (to increase the number of awardees), seems to be well-rooted in efficiency considerations, provided that we take a deeper and dynamic stance when looking at specific public procurements. However, an immediate and still unsolved question that is likely to spur economic research is whether limiting participation (that is the number of lots for which any given participant is allowed to bid) is more pro-collusive than limiting the number of lots that any one participant can be awarded.

### ***5. Demand aggregation and joint bidding***

The lower participation effect due to demand aggregation discussed in section 3 hinges on the assumption that participating firms always behave as *solo* bidders. Casual observation in public procurement practices reveals also

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(13) Some empirical evidence of an "incumbent effect" in the procurement for ICT services is discussed in G. L. ALBANO – F. DINI – R. ZAMPINO, *Bidding for Complex Projects: Evidence from the Acquisition of IT Services by the Italian Ministry of Economy and Finance*, in M. A. Wimmer – H. Jochen Scholl – M. Janssen – R. Traunmüller (eds. by), *Electronic Government. 8th International Conference*, EGOV 2009. Springer Verlag 2009, 353-363.

the relevance of joint bidding, that is, the practice of two or more similar firms submitting a single bid. Anticompetitive issues may arise when “horizontal” bidding consortia are active, that is, when similar firms that are normally competing with each other submit a single tender. Bidding consortia among potential competitors, whether or not temporary, are rather common in public and private procurement. They have been known for quite a while to researchers because they were (sporadically) used by some oil companies to bid in U.S. auctions for offshore leases.<sup>(14)</sup> In late 1975, however, the U.S. Department of the Interior made a drastic U-turn and forbade the largest crude-oil producers from submitting joint bids for outer continental shelves leases. The presumption was that joint bidding was aimed at reducing the number of bids and thereby lowering prices, although there was little research supporting such a policy change.<sup>(15)</sup>

To be sure, joint bidding does reduce the number of independent bids when smaller firms unable to participate as solo bidders decide not to constitute a consortium. Consequently, if not challenged by competition authorities, *unregulated* joint bidding could easily be used to enforce price fixing agreements among *all* bidders, thus eliminating competition altogether.

That joint bidding consortia can be used as a price-fixing device to eliminate competition altogether is far from being a mere theoretical conjecture. In February 2012, two U.S. oil and gas companies accused of illegally working together in auctions of four natural gas leases on federal land in Colorado agreed to pay \$275,000 each to settle the claim. The case is the first federal challenge to an anti-competitive bidding agreement for mineral rights, according to the U.S. Department of Justice (DOJ). The complaint alleged that the two companies were separately developing natural gas resources in western Colorado. In 2005, the companies allegedly entered into a written agreement whereby they agreed that only one company would bid at the auctions and would then assign an interest in acquired leases to the other company. One firm separately bid at U.S. Bureau of Land Management auctions and won leases with an average price of \$25 an acre, in one instance paying \$2 an acre. According to the DOJ, the United States received less revenue from the sale of the four leases than it would have received had the companies competed against each other at the auctions. As a result, the DOJ determined that the agreement was not part of any “pro-competitive” or “efficiency-enhancing collaboration”. The United

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(14) Our focus in this chapter is on “horizontal” bidding consortia, among similar firms that are normally competing with each other, so we disregard “vertical” consortia between firms specialized in different components of, say, a bundled procurement contract, which are usually admitted and welcome in procurement.

(15) See O. O. ILEDARE – A.G. PULSIPHER, *Joint Bidding Restriction Policy ofr Selective E&P Firms un the U.S. Gulf of Mexico: How Persuasive is Its Effectiveness?*, in *Energy Policy*, 2007, 3126-3133.

States' investigation reportedly resulted from a whistleblower lawsuit filed under the *qui tam* provisions of the False Claims Act. Those provisions allow for private parties to sue on behalf of the United States and, if successful, to receive a portion of any recovered damages.<sup>(16)</sup>

In Italy, a remarkable case is the one investigated by the Italian Competition Authority (ICA) in 1997.<sup>(17)</sup> The Municipality of Milan filed a complaint alleging the existence of a collusive agreement among the insurance companies that were invited to submit a tender for an insurance contract. Indeed, following the “boycott” of two public tenders and a third unofficial tender, the Municipality found itself bound to negotiate privately the insurance service with a single group of companies led by Assitalia. The ICA found that, after the call for tender, some of the main insurance companies joined a consortium to make a co-insurance bid to the Municipality. The ICA argued that the strategy adopted by the bidding consortium, besides eliminating the rivalry among its members, was aimed at deterring other companies from participating in the competitive process.

For this reason, one may wonder whether joint bidding should be subject to some form of regulation. We have shown elsewhere<sup>(18)</sup> that the existence and type of regulation differ enormously across countries in Europe; and that – when present – regulations are in several cases related to the ability of an individual firm to be admitted as a solo bidder. The variety of regulatory approaches found in Europe, sometimes contradictory and including many cases of no regulation at all, seems to point toward a lack of a clear vision, if not bare understanding, of the main consequences of any specific policy. Whether regulation is to be preferred to a free-market approach depends also on organizational features of procurement markets. When a sizeable fraction of public demand is aggregated through a CPPA that awards framework agreements on behalf of other government departments, and if the latter are forced by law to issue purchasing orders by relying on the CPPA's purchasing arrangements, one may reasonably maintain that some forms of regulation of joint bidding are to be preferred so as to minimize the risk that consortia will be used for anti-competitive purposes. It should be noted, though, that, once tenders are submitted and evaluated, the CPPA's and antitrust authorities' objective functions do not necessarily coincide. The latter aims at uncovering and prosecuting cartels at any stage of the procurement process, whereas the former has to deliver good value for money to a set of final users that may not have an outside option. Sometimes good value from money may be the outcome of a collusive agreement.

(16) Details retrieved from <http://www.justice.gov/opa/pr/2012/February/12-at-219.html>.

(17) See ICA Decision No. 5333 of 25 September 1997, Bollettino No. 39/97.

(18) See G. L. ALBANO – G. SPAGNOLO – M. ZANZA, *Regulating Joint Bidding in Public Procurement*, in *Journal of Competition Law and Economics*, 2009, 335-360.

## 6. *The risk of collusion in Framework Agreements*

Framework agreements (FAs) are anticipated arrangements for the delivery of goods and services over a certain period of time. According to both international practices and regulation, three broad definitions of FAs can be identified:

- I. The European Union (EU), in the 2004 procurement Directive,<sup>(19)</sup> defines framework agreements as “agreements between one/more contracting agencies and economic operator(s) (...) to establish the terms governing contracts to be awarded during a given period (...) with regard to price and (...) the quantities envisaged.”
- II. The United States have adopted different variations on FAs such as: Government-Wide Acquisition Contracts (GWAC), Indefinite Delivery/Indefinite Quantity (IDIQ) contracts and Multiple Award Schedules (MAS), all of which imply multiple standing contracts with subsequent competitions for task or delivery orders.<sup>(20)</sup>
- III. The United Nations Commission on International Trade Law (UNCITRAL) defines a framework agreement as a transaction to secure the supply of a product or service over a period of time (periodic/recurrent purchase arrangement, periodic requirements arrangement, periodic supply vehicle).

The three families are linked by two common traits: the aggregation of demand for goods and services to be delivered/provided at different moments in time; and the adoption of a two-stage procurement process. Because of its two-stage nature the conclusion of a FA leads to the emergence of “new market” characterized by two salient features: i) the number of firms will be, in general, lower than the set of competing firms at the first stage; ii) firms in the FA know that they will be competing (through “call-off” competitions) over time for a stream of purchase orders.<sup>(21)</sup> When the FA does not allow entry of new firms at a later stage,<sup>(22)</sup> the resulting market will bear a straightforward resemblance with an oligopolistic market in which firms may be tempted to adopt collusive strategies, thus softening competition to raise profit. Coordination, whether explicit or tacit, is both tempting and feasible since firms interact over

(19) Directive 2004/18/CE, “On the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts”, available at <http://ec.europa.eu>.

(20) A compared analysis on the usage of framework agreements in Europe and US is outlined in C. R. YUKINS, *Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting*, in *PCLJ*, 2008, 545-568.

(21) For a more in-depth economic analysis of framework agreements see G. L. ALBANO – M. SPARRO, *A Simple Model of Framework Agreements: Competition and Efficiency*, in *Journal of Public Procurement*, 2008, 356-378.

(22) Under the 2004 European Directive, this type of “open” arrangement was what is known as a Dynamic Purchasing System.

time. In oligopolistic markets it typically takes a rather simple form. Firms set a high price and keep it stable over time only if no-one undercuts its rivals at any point in time. Cheating is normally deterred by the threat of a possibly ever-lasting price war. In what follows, we will emphasize how the design of the FA and the stream of call-offs may increase the risk of collusion among firms.

The sequence of call-offs could, in principle, be assimilated to a public contract split into several lots, the difference being that lots are awarded at different points in time. For a given number of firms in the FA and for a given overall value of the latter, the higher the number of call-offs the higher the risk of collusion since there will be a higher number of “pie-sharing” arrangements to sustain a collusive scheme. One countermeasure would consist, whenever compatible with final demand, in lowering the number of call-offs (that is, reducing the frequency of interaction) by increasing the value of each call-off. This would reduce the number of potentially feasible collusive allocations. However, firms would probably then be required to have higher financial/economic capacities, which would, in principle, reduce the number of competitors in the FA, thus making collusion more likely.

When deciding whether to adhere to a collusive strategy, each firm needs to evaluate the net benefits from current deviations – namely, short-run profit minus the expected cost arising from other firms’ punishing strategies – against the present value of benefits from cooperation. The latter depends crucially on firms’ ability to predict as precisely as possible the stream of call-offs. The more predictable the stream of call-offs the more confident firms will be on “how much collusion is worth”. Consequently, preventing collusion might mean not announcing in advance the precise stream of purchase orders that will take place in the FA.

There exists another dimension connected with the number of call-offs, namely the degree of symmetry among suppliers. Symmetric firms might be simply interpreted as firms having similar market shares/production costs.<sup>(23)</sup> If suppliers are asymmetric, then symmetric (i.e., of similar value) call-offs may constitute an anti-collusive device, for it makes more difficult to achieve an agreement on how to split the lots. Conversely, when suppliers are fairly symmetric, collusion deterrence might be pursued by a sequence of asymmetric call-offs.

Asymmetry among firms may be a consequence of the first stage of competition. When the FA is concluded by using the economically most advantageous tender (EMAT) criterion, firms may be allowed to “carry forward” a fraction of the awarded technical score. This case may arise<sup>(24)</sup> when participating

(23) The two dimensions are in fact likely to be positively correlated.

(24) “Inherited” technical score was one of the features of the two framework agreements designed by Consip Ltd for acquiring IT services on behalf of the Department of Treasury of the Ministry of Economy and Finance in 2008 and 2011.

firms' technical proposals refer to aspects that are common to all subsequent call-offs. Thus, upon competing for each single call-off firms may inherit the fraction of the initial technical score that was awarded at the first stage. Let us suppose that at the first stage higher-ranked firms display the higher-than-average technical score and lower-than-average economic score. To make this more concrete, consider the following example in which the maximum technical and financial scores are 60 and 40, respectively:

|        | <i>Technical score</i> | <i>Financial score</i> | <i>Total score</i> |
|--------|------------------------|------------------------|--------------------|
| Firm A | 46                     | 8                      | <b>54</b>          |
| Firm B | 40                     | 10                     | <b>50</b>          |
| Firm C | 30                     | 15                     | <b>45</b>          |

The FA is concluded with firms A, B, and C. Assume also that when bidding for the sequence of call-offs, each firm inherits 50% of the technical score awarded at the first stage, that is, firm A starts with 23 points, firm B with 20 and firm C with 15. How will such an asymmetric scenario affect the risk of collusion among firms? Observe first that firms B and C submitted higher discounts than firm A. If the design of the FA forbids firms from raising their prices at the call-off stage above those submitted at the first stage,<sup>(25)</sup> any symmetric “pie-sharing” collusive agreement (that is, firms rotate in winning call-offs by having firm A be awarded the first contract, firm B the second, firm C the third and so on) would leave firm A with higher collusive profit than its competitors. Thus, if firms are alike with respect to other economic dimensions such as market shares/sizes/production costs, incentive-compatibility constraints require the cartel to allocate a higher number of contracts to firm C than to firm B, and a higher number to the latter than to firm A. Thus for a given value of the FA and for a given stream of call-offs, score-heterogeneous firms are likely to find it more difficult to agree on a collusive scheme than firms competing for call-offs on a “level” playing field.

### **7. Concluding remarks**

In this chapter, we have raised a seemingly simple question: to what extent a particular feature of public procurement models, namely the degree of demand aggregation, may lead to a higher risk of anticompetitive behavior in procurement markets? We have maintained that the answer is likely to depend

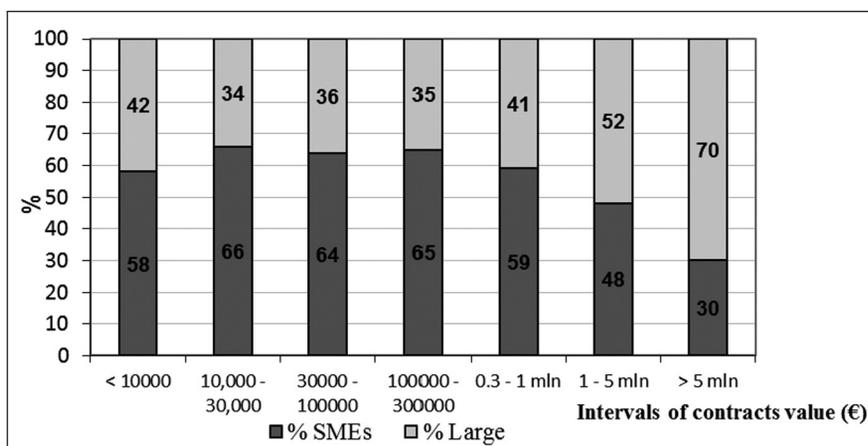
<sup>(25)</sup> The Italian regulation of framework agreements goes in that direction.

on many aspects of procurement design that often go unnoticed or, at least, are not enough emphasized in research papers or workshop discussions.

We have argued that demand aggregation does not necessarily hinge on bundling/merging many separate contracts into one big contract, and that a sound “lots design” may favor the participation of smaller firms, thereby reducing the risk of collusive agreements among bigger firms. The point then becomes whether we have any evidence of procurement design satisfying both features. “Theories” on public procurement design are very seldom backed by adequate evidence. However, we can perform a simple empirical exercise that is compatible with the statement that demand aggregation does not lead to adverse effects in terms of participation (especially by SMEs) and, as a result, does not necessarily generate further competition concerns.

The chart below summarizes some of the findings contained in a study on SMEs’ performance in public procurement markets at the EU level.<sup>(26)</sup> We have also gathered data on SMEs performance in framework agreements awarded by Consip Ltd. During the period march 2011-july 2012, 34% of the contracts/lots were awarded to SMEs. This seems to be in line to what measured at the EU level given that the value of lots in the NFCs awarded by Consip is above € 1 million. In other words, demand aggregation by a CPPA together with an appropriate division into lots does not seem to add any further adverse effect to SMEs performance in public procurement markets.

*Figure 1: Shares of public contracts according to firms’ size in the EU-27 in the period 2006-09.*



(26) Author’s elaborations on data retrieved from *Evaluation of SMEs’ access to public procurement markets in the EU – DG Enterprise and Industry*, GHK Final Report, September 2010.

This does not constitute any conclusive evidence. It is compatible, however, with the initial conjecture that the demand aggregation and an appropriate lots design do not hurt SMEs (in terms of likelihood of success) more than what would happen if contracts of similar values were awarded by many public authorities acting independently from each other. More research, especially grounded on empirical evidence, should be carried out to support policy making and to better advise those involved in design of public procurement strategies.

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## CHAPTER 2

### Prevention and deterrence of bid rigging: a look from the new EU directive on public procurement

BY

Albert SÁNCHEZ GRAELLS

Senior Lecturer in Commercial Law, University of Leicester

#### Introduction

As a departing point and before entering the analysis of the new EU Directive 2014/24 on public procurement,<sup>(1)</sup> it is worth stressing that *the effectiveness of public procurement and its ability to contribute to the proper and most efficient carrying on of public interest obligations is conditional upon the existence of competition in two respects or separate dimensions*. One of them has been expressly recognised for a long time by public procurement regulations, which have tried to foster competition within the specific tender by attracting a relatively large number of participants (or, at least, a sufficient number to ensure effective competition for the given public contract) and by preventing collusion or bid rigging amongst tenderers. *Public procurement rules protect and promote competition* – in this narrow sense – *as a means to achieve value for money and to ensure the legitimacy of purchasing decisions*. From this perspective, competition is seen as a tool, as an instrument to allow the public purchaser to obtain the benefits of competitive pressure among (participating) bidders, as well as a key instrument to deter favouritism and other corrupt practices and deviations of power.

However, a subtler and stronger dependence of public procurement on competition in the market exists,<sup>(2)</sup> but it is implicit and has generally been

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(1) Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC. Most of the considerations made in connection with Directive 2014/24 will be equally or analogously applicable to public procurement conducted under the parallel rules of 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts, and of Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC.

(2) Office of Fair Trading (OFT) | econ, *Assessing the Impact of Public Sector Procurement on Competition*, 2004, available at [oft.gov.uk/shared\\_oft/reports/comp\\_policy/oft742c.pdf](http://oft.gov.uk/shared_oft/reports/comp_policy/oft742c.pdf), last accessed 23 January 2012. See also OFT, *Competition in mixed markets: ensuring competitive neutrality*, 2010, available at [oft.gov.uk/shared\\_oft/economic\\_research/oft1242.pdf](http://oft.gov.uk/shared_oft/economic_research/oft1242.pdf), last accessed 23 January 2012.

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overlooked by most public procurement studies.(3) *In order to attain value for money and to work as a proper tool for the public sector, public procurement activities need to take place in competitive markets.*(4) Public procurement rules assume that markets are generally competitive – in the broad sense – or, more simply, take as a given their economic structure and competitive dynamics.(5) The existence of competitive intensity in the market is usually taken for granted, or simply disregarded, in public procurement studies. In general terms, this approach is correct in that public procurement is not specifically designed to prevent distortions of competition between undertakings. However, issues regarding competition in the market are not alien to public procurement,(6) and need to receive further attention and a stronger emphasis(7) – as indeed, recently seems to be the case, both in procurement practice(8) and case law.(9) Hence, the study of the interaction between procurement and competition needs to keep an eye open for potential competitive impacts in a broader setting than each tender in itself: i.e. has to (also) focus on general market dynamics.

Nonetheless, and without forgetting the broader implications of the design of procurement rules for market competition, this chapter will focus specifically on the issue of collusion in procurement procedures and, more specifically, on the changes and improvements introduced in new EU Directive 2014/24 on public procurement. More specifically, this chapter will try to highlight how bid rigging seems pervasive in the public procurement setting across the European Union,

(3) Exceptionally, the relevance of competition in the market (as protected by competition law) for the proper functioning is stressed by P. A. TREPTE, *Regulating Procurement. Understanding the Ends and Means of Public Procurement Regulation*, Oxford, Oxford University Press, 2004, 57, 61 and 122. See also C. MUNRO, *Competition Law and Public Procurement: Two Sides of the Same Coin?*, in *PPLR*, 2006, 352. Compare with J. F. BRISSON, *Les fondements juridiques du droit des marchés publics*, Paris, Imprimerie Nationale, 2004, 25; and O. BLACK, *Conceptual Foundations of Antitrust*, Cambridge, Cambridge University Press, 2005, 9.

(4) The case has been made convincingly by R. D. ANDERSON – W. E. KOVACIC, *Competition Policy and International Trade Liberalisation: Essential Complements to Ensure Good Performance in Public Procurement Markets*, in *PPLR*, 2009, 67, 70-2. Similarly, stressing the importance to shield public procurement from anticompetitive market practices, see D. E. BRUNK, *Governmental Procurement: "FAR" from a Competitive Process*, in G. PIGA – K. V. THAI (eds. by) *Advancing Public Procurement: Practices, Innovation and Knowledge – Sharing*, Boca Raton, PrAcademics Press, 2006, 156.

(5) G. PIGA – K. V. THAI, *The Economics of Public Procurement: Preface*, *Rivista di Politica Economica*, 2006, 3; K. V. THAI, *Public Procurement Re-examined*, in *Journal of Public Procurement*, 2001, 9.

(6) See W. SAUTER – H. SCHEPEL, *State and Market in European Union Law. The Public and Private Spheres of the Internal Market before the EU Courts*, Cambridge, Cambridge University Press, 2009, 49. Similarly, S. SIMONE – L. ZANETTINI, *Appalti pubblici e concorrenza*, in L. Fiorentino (ed. by) *Lo Stato compratore. L'acquisto di beni e servizi nelle pubbliche amministrazioni*, Bologna, Il Mulino, 2007, 119.

(7) Similarly, see O. DEKEL, *The Legal Theory of Competitive Bidding for Government Contracts*, in *PCLJ*, 2008, 237; B. MUKHOPADHYAY, *Evaluating Public Procurement*, in *Review of Market Integration*, 2011, 21; and P. CHIRULLI, *Public Contracts*, in *International Journal of Public Administration*, 2011, 134.

(8) S. TAYLOR, *The challenge of competitive neutrality in public procurement and competition policy: the U.K. health sector as case study*, in *Competition Policy International*, 2011, 7.

(9) G. S. ØLYKKE, *How does the Court of Justice of the European Union pursue competition concerns in a public procurement context?*, in *PPLR*, 2011, 179.

despite increased enforcement and advocacy efforts (a situation that should come as no surprise to economists, but that may still puzzle lawyers) (§II). On the basis of such (anecdotal) evidence – which justifies the additional efforts to design collusion-preventing procurement devices – the chapter will then proceed to the analysis of two of the instruments and provisions designed to prevent and deter bid rigging that have been included in the new EU Directive on public procurement: the rules on division of contracts into lots (art. 46), and the streamlining of rules controlling the disqualification and exclusion of competition law infringers (art. 57) [presenting the arguments that would have justified a more developed suspension and debarment regime in the revised version of the Directive] (§III). Some brief conclusions will be offered on the current situation regarding prevention and deterrence of bid rigging in the EU public procurement rules (§IV).

## Part I

### ***1. The Apparent Pervasiveness of Bid Rigging Despite Increased Enforcement Efforts***

As mentioned in passing, restrictions of competition generated by undertakings participating in public procurement – mainly related to bid rigging – have so far attracted most of the attention as regards the intersection of competition law and public procurement,<sup>(10)</sup> and economics offers good reasons for this. The analysis of the economic theory and its correlation in actual practice will help us understand better the relevance of developing effective tools to prevent, identify and deter bid rigging in public procurement, and will set the framework for the analysis of the new EU Directive on public procurement that we will attempt later (§III).

### ***2. Brief Economic Background***

It is necessary to stress that, in and by themselves and due to their very intrinsic characteristics, public procurement rules create a (competitive) environment that facilitates collusion. As clearly stressed by the OECD:

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(10) Indeed, this has been the main focus of international efforts, particularly by the OECD, which has recently published detailed guidelines to help design public procurement regulations to prevent collusion; see OECD, *Guidelines for Fighting Bid Rigging in Public Procurement. Helping Governments to Obtain Best Value for Money*, 2009. See also *ibid.*, *Public Procurement: The Role of Competition Authorities in Promoting Competition*, 2007. This is also the focus of recent scholarly studies in this field; for instance, C. CABANES – B. NEVEU, *Droit de la concurrence dans les contrats publics. Pratiques anticoncurrentielles, abus de position dominante, controls et sanctions*, Paris, Le Moniteur, 2008; as well as some practitioners' guidance, see W. E. KOVACIC, *The Antitrust Government Contracts Handbook*, Chicago, ABA Section of Antitrust Law, 1990.

“[t]he formal rules governing public procurement can make communication among rivals easier, promoting collusion among bidders. While collusion can emerge in both procurement and «ordinary» markets, procurement regulations may facilitate collusive arrangements”.(11) The fact that public procurement rules increase the likelihood of collusion among bidders has been convincingly proven in economic literature(12) and it is out of question that, under most common market conditions, procurement regulations significantly increase the transparency of the market and facilitate collusion among bidders through repeated interaction.(13) However, this key (economic) finding has not generated as strong a legislative reaction as could have been expected – and most public procurement regulations still contain numerous rules that tend to increase transparency and result in competition-restrictive outcomes (such as bid disclosure, pre-bid meetings, restrictions on the issuance of invitations to participate in bidding processes to a relatively pre-defined or stable group of firms, etc.).(14) In the end, given that public procurement regulations are likely to facilitate collusion amongst bidders, it is not surprising that a large number of cartel cases prosecuted in recent years have taken place in public procurement settings,(15) and that the main focus of the (still limited) antitrust enforcement efforts in the public procurement setting lies with bid rigging and collusion amongst bidders, as the actual case law shows. In the following section, we will look at some cases that clearly indicate that economic theory translates into practice and, consequently, why preventing and deterring bid rigging

(11) OECD, *Public Procurement: Role of Competition Authorities*, 2007, 7.

(12) For recent references, see G. L. ALBANO et al., *Preventing Collusion in Public Procurement*, in N. Dimitri et al. (eds. by), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 347.

(13) For a theoretical framework see R. P. MCAFEE – J. McMILLAN, *Incentives in Government Contracting*, Toronto, Toronto University Press, 1987, and F. NAEGELEN – M. MOUGEOT, *Les marchés publics: règles, stratégies, politiques*, Paris, Economica, 1993. For recent references, see W. E. KOVACIC et al., *Bidding Rings and the Design of Anti – Collusive Measures for Auctions and Procurements*, in N. Dimitri et al. (eds), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 381. See also S. TANAKA – S. HAYASHI, *Bid-Rigging in Japanese Public Procurement*, in K. V. Thai (ed. by), *Towards New Horizons in Public Procurement*, Boca Raton, PrAcademics Press, 2010, 150.

(14) However, some contracting authorities do adopt certain anti-collusion measures when designing their procurement processes; see L. CARPINETTI et al., *The Variety of Procurement Practice: Evidence from Public Procurement*, in N. Dimitri et al. (eds), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 14.

(15) K. L. HABERBUSH, *Limiting the Government's Exposure to Bid Rigging Schemes: A Critical Look at the Sealed Bidding Regime*, in *PCLJ*, 2000-2001, 97, 98; and R. D. ANDERSON – W. E. KOVACIC, *Competition Policy and International Trade Liberalisation*, cit., 67. It will also be relevant to see whether public enforcement can be coupled with a growing trend of private enforcement of competition rules in the area of public procurement; see M. MACI, *Private Enforcement in Bid-Rigging Cases in The European Union*, in *European Competition Journal*, 2012, 211. In general, for recent discussion of these issues, see the videotaping of an interesting exposition by M. CARPAGNANO, *Profili antitrust: I fenomeni di collusione nella partecipazione alle gare pubbliche*, in *Seminari di specializzazione: 'Il bene concorrenza e le tutele predisposte dall'ordinamento nelle gare pubbliche'*, available at [jus.unitn.it/services/arc|2012|0120/home.html?goback=%2Egde\\_3797103\\_member\\_110211178#a4](http://jus.unitn.it/services/arc|2012|0120/home.html?goback=%2Egde_3797103_member_110211178#a4), last visited 7 May 2012.

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should rank very high in the list of goals of public procurement regulations and, consequently, attract substantial attention in current procurement regulation reform processes.

### 3. Reflections of Economic Theory in Practice

As already indicated, it is worth highlighting that most competition decisions related to public procurement involve bid rigging by tenderers – which may take several forms, such as bid rotation, submission of cover bids, bid hold-up, submission of excessive bids to force an increase in the expenditure ceiling estimated by the tendering authority, etc. According to the OECD, the several types of bid rigging schemes can be conceptualised, so that a general description of each of these practices could be the following:

*Cover bidding.* Cover (also called complementary, courtesy, token, or symbolic) bidding is the most frequent way in which bid-rigging schemes are implemented. It occurs when individuals or firms agree to submit bids that involve at least one of the following: (1) a competitor agrees to submit a bid that is higher than the bid of the designated winner, (2) a competitor submits a bid that is known to be too high to be accepted, or (3) a competitor submits a bid that contains special terms that are known to be unacceptable to the purchaser. Cover bidding is designed to give the appearance of genuine competition.

*Bid suppression.* Bid-suppression schemes involve agreements among competitors in which one or more companies agree to refrain from bidding or to withdraw a previously submitted bid so that the designated winner's bid will be accepted. In essence, bid suppression means that a company does not submit a bid for final consideration.

*Bid rotation.* In bid-rotation schemes, conspiring firms continue to bid, but they agree to take turns being the winning (i.e., lowest qualifying) bidder. The way in which bid-rotation agreements are implemented can vary. For example, conspirators might choose to allocate approximately equal monetary values from a certain group of contracts to each firm or to allocate volumes that correspond to the size of each company.

*Market allocation.* Competitors carve up the market and agree not to compete for certain customers or in certain geographic areas. Competing firms may, for example, allocate specific customers or types of customers to different firms, so that competitors will not bid (or will submit only a cover bid) on contracts offered by a certain class of potential customers which are allocated to a specific firm. In return, that competitor will not competitively bid to a designated group of customers allocated to other firms in the agreement.”(16)

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(16) Indeed, the most common types of bid rigging practices are well described in the OECD, *Guidelines for Fighting Bid Rigging in Public Procurement. Helping Governments to Obtain Best Value for Money*, 2009, available at [oecd.org/dataoecd/27/19/42851044.pdf](http://oecd.org/dataoecd/27/19/42851044.pdf), last visited 7 May 2012.

As we shall see shortly, anecdotal evidence shows that collusion – in any of the abovementioned forms, or in hybrid manner – is pervasive in almost all economic sectors where procurement takes place, but maybe has a special relevance in markets where the public buyer is the main or sole buyer, such as roads and other public works,<sup>(17)</sup> healthcare markets, education, environmental protection, or defence markets – where both EU and national competition authorities have been very active and aggressive recently.<sup>(18)</sup> Some of these cases, however, still show a need for further economic analysis (or a better understanding of the mechanics of bid rigging) on the part not so much of competition authorities, but of review bodies and courts.

### 3.1. Bid rigging in healthcare markets

On 9 June 2011 the Moldovan Competition Authority (ANPC) established the existence of bid rigging practices at the public tenders organized by the Medicines Agency (AMED) for the purchase of anti-diabetic medicines, since two suppliers of pharmaceuticals were submitting their bids with identical prices.<sup>(19)</sup> In this particular case, though, it is worth stressing that collusion was being strengthened by the contracting authority (AMED) by selecting both firms as winning bidders and dividing the purchase volumes equally between them, thus leading to the elimination of competition – which rather naturally led the ANCP to recommend to refrain from dividing purchase volumes among the bidders submitting identical price offers.

In a similar case, on 10 December 2010 the Portuguese Competition Authority issued a prohibition decision concerning a retail price fixing agreement established between a supplier and a retailer of hospital equipment (automated medicine dispenser), which eliminated price competition between the two companies in public tenders for hospital equipment.<sup>(20)</sup> Prior to that, on 7 January 2010 the Lisbon Commerce Court upheld a 2008 decision by the Portuguese Competition Authority imposing a € 13.4 million fine on several pharmaceutical companies for participating in a bid rigging cartel concerning public tenders held by hospitals for the purchase of blood glucose monitoring reagents (test strips).<sup>(21)</sup>

(17) For a worrying description of the pervasiveness of bid rigging in construction markets all over the world, see OECD, *Policy Roundtable on the Construction Industry* (2008) available at [oecd.org/dataoecd/32/55/41765075.pdf](http://oecd.org/dataoecd/32/55/41765075.pdf), last visited 4 October 2011.

(18) On the particular relevance of publicly-dominated markets for the analysis of competition impacts of public procurement, see A. SÁNCHEZ GRAELLS, *Public Procurement and the EU Competition Rules*, Oxford, Hart Publishing, 2011, 37-43.

(19) A. SVETLICINII, *The Moldovan Competition Authority finds bid rigging practices in purchases of anti-diabetic medicines (Medicines Agencies)*, in *e-Competitions*, 9 June 2011, n. 37384.

(20) ECN Brief, *The Portuguese Competition Authority punishes resale price maintenance affecting hospitals' public tenders*, in *e-Competitions*, 10 December 2010, n. 35733.

(21) M. MENDES PEREIRA – N. CARROLO DOS SANTOS, *The Lisbon Commerce Court confirms decision against bid-rigging cartel by pharmaceutical companies but substantially reduces fines (Abbott, Menarini and Johnson & Johnson)*, in *e-Competitions*, 7 January 2010, n. 30637.

Also in a similar case, in March 2008 the Romanian Competition Council fined a pharmaceutical producer and three distributors for participation into a market-sharing cartel active on the insulin market. In this case, involving an auction within the Diabetic National Program in 2003, the products of the same manufacturer were offered through the three distributors, each authorized to participate with different products, so that they did not compete against each other in the auction.(22)

There are similar cases in almost every jurisdiction,(23) and their incidence may be difficult to lower, particularly in countries where the retail price for pharmaceuticals is set by the public authority and/or where public buyers must disclose their estimates or maximum expense ceilings. However, precisely due to some of these regulatory restrictions, not all cases of apparent bid rigging in the healthcare sector (or in other markets) end up with the imposition of fines since the analysis of the available data may be complicated and requires detailed and careful appraisal. For instance, the Bulgarian Commission for Protection of Competition recently closed a probe into alleged bid rigging among suppliers of pharmaceuticals without establishing an infringement, particularly in regard to the transparency-enhancing effects of the domestic regulatory environment (which imposed price ceilings).(24) Similarly, the Polish authority also dropped a case after thorough analysis of data that, *prima facie*, indicated potential collusion.(25) In this regard, clear rules on the application and validity of proof by presumptions is very much needed, due to the relatively easy misreading of actual procurement data. In this vein, it is interesting to see cases like the judgment of the Spanish Supreme Court of October 2009, where some indications in this respect were advanced.(26) But a rather different approach can be found in the case law of the Paris Court of Appeals, which sets a strict standard of proof for undertakings to inhibit the existence of indicia of collusion in tendering procedures.(27) Hence, some further guidance by the European

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(22) G. HARAPCEA, *The Romanian Competition Council fines a pharmaceutical producer and three distributors for participation into a market-sharing cartel active on the insulin market (Eli Lilly Export, A&A Medical, Mediplus Exim and Relad Pharma)*, in *e-Competitions*, 12 March 2008, n. 19850.

(23) For instance, regarding Italy, see L. CROCCO, *An Italian administrative Court confirms that a cartel took place in hospital supplies but slashes down fines (Bristol Myers Squibb)*, in *e-Competitions*, 6 June 2008, n. 23296.

(24) D. FESSENKO, *The Bulgarian Commission for Protection of Competition closes a probe into alleged bid-rigging among suppliers of pharmaceuticals without establishing an infringement (Alta Pharmaceuticals, Roche a.o.)*, in *e-Competitions*, 12 December 2010, n. 34785.

(25) See R. GAGO – P. BOROWIEC, *The Polish competition authority finds pharmaceuticals companies and their distributors not guilty of price fixing and market sharing on the EPO medicines market (Johnson & Johnson, Roche)*, in *e-Competitions*, 14 June 2007, n. 14073.

(26) See J. GARCIA-NIETO – H. AJOUĆ, *The Spanish Supreme Court provides guidance on the application of the proof by presumptions test in the context of a bid rigging case in the healthcare sector (Amersham Health)*, in *e-Competitions*, 3 October 2009, n. 31175.

(27) C. SAUMON – P. DE MONTALEMBERT, *The Paris Court of Appeal confirms the fines imposed in a collective boycotting case and its strict case law on standard of proof (Defibrillators)*, in *e-Competitions*, 8 April 2009, n. 26442.

Court of Justice on the application of the technique of proof by presumptions may be needed (although this is not exclusive of competition enforcement in the procurement setting, but more generally for cartel enforcement).

### 3.2. Bid rigging in public works markets

In this area, some of the most well-known bid-rigging schemes have taken place. For instance, it has been widely reported that the European Commission fined members of lifts and escalators cartels over € 990 million, since between at least 1995 and 2004 those companies rigged bids for procurement contracts, fixed prices and allocated projects to each other, shared markets and exchanged commercially important and confidential information.<sup>(28)</sup> It is also well known that one of the largest cartels ever prosecuted involved the (whole) construction industry in the Netherlands for at least the period 1992-2006, where firms systematically rigged bids by holding meetings prior to tendering for contracts.<sup>(29)</sup>

The construction sector piles up a number of bid rigging decisions in other jurisdictions, where massive cartel investigations have followed the Dutch example. For instance, in September 2009 the UK Office of Fair Trading (OFT) imposed £ 129.5 million in fines on construction firms for colluding with competitors after finding that the companies concerned were engaged in illegal and anti-competitive bid rigging activities on at least 199 tenders from 2000 to 2006, mainly by means of ‘cover pricing’.<sup>(30)</sup> However, the fines have been substantially lowered by the UK’s Competition Appeal Tribunal (CAT),<sup>(31)</sup> raising some issues on the accuracy and practicality of such massive cartel investigations and the ensuing fines – the most disturbing is, in my opinion, that the CAT found that the OFT wrongly equated cover pricing to bid-rigging or “*traditional cartel practices*” (para. 82), stating that “*Its purpose is not (as in a conventional price fixing cartel) to prevent competition by agreeing the price which it is intended the client should pay*” (para. 100). These considerations are difficult to understand, since cover pricing is nothing but a mechanism of (indirect) price fixing in tender procedures, as clearly indicated in recent

(28) E. POST – A. FONT GALARZA – G. CSEREY – R. PLANK, *The European Commission fines cartel in the elevators and escalators sector (Otis, KONE, Schindler and ThyssenKrupp)*, in *e-Competitions*, 21 February 2007, n. 36176.

(29) For a comprehensive explanation of this very outstanding case (due, notably, to the enormous amount of undertakings involved), see the site of the Construction Unit at the Dutch Competition Authority [[nma.nl/en/competition/more\\_industries/construction\\_unit/default.aspx](http://nma.nl/en/competition/more_industries/construction_unit/default.aspx), last visited 4 October 2011].

(30) A. LISTA, *The UK Office of Fair Trading imposed £129.5 million in fines on construction firms for colluding with competitors (Construction Industry Cartel)*, in *e-Competitions*, 22 September 2009, n. 31546.

(31) A. STEPHAN, *The UK Competition Appeal Tribunal cuts fines in the construction cover pricing appeal case (Kier Group and others)*, in *e-Competitions*, 11 March 2011, n. 38585.

OECD guidelines: “long-standing bid-rigging arrangements may employ much more elaborate methods of assigning contract winners, monitoring and apportioning bid-rigging gains over a period of months or years. Bid rigging may also include monetary payments by the designated winning bidder to one or more of the conspirators. This so-called compensation payment is sometimes also associated with firms submitting «cover» (higher) bids”.<sup>(32)</sup> Therefore, in my opinion, the disconnection between cover pricing and price fixing or pure bid rigging that the CAT tries to delineate just seems wrong. Moreover, the CAT ruling is particularly disturbing because, as already pointed out by one commentator, the “divergence in attitude over the seriousness of cover pricing between the OFT and the CAT could lead to further reductions in fines”;<sup>(33)</sup> and, hence, could significantly reduce deterrence in a sector where it is strongly needed in view of the longstanding anti-competitive practices.

Similarly, although in a smaller scale, in 2004 the Hungarian Competition Authority fined construction companies for bid rigging in Budapest public construction tenders after the documents seized in dawn raids at the premises of large construction companies indicated that several relevant players in the Hungarian construction sector had been involved in bid rigging in a number of large public procurements.<sup>(34)</sup> Other, similar cases of sanctions imposed to bid riggers by the Hungarian Competition Authority have however recently been quashed due to insufficient proof of collusion under the theory of the single and continuous infringement.<sup>(35)</sup> Even if the companies had been held by the authority to be involved in at least 11 instances of bid rigging between 2002 and 2006, the reviewing court found that not all of them had been involved in every instance (since some of them did not participate in some of the tenders) and, hence, could not be charged and sanctioned under the theory of the single and continuous infringement – therefore, mandating the reopening of the case and the setting of new fines in view of the data supporting actual involvement by each company. This ruling is also troubling, in my view, due the fact that *bid hold-up* is a text book example of bid rigging practice, as also indicated in OECD guidelines: “*Bid-rigging schemes often include mechanisms to apportion and distribute the additional profits obtained as a result of the higher final contracted price among the conspirators. For example, competitors who agree not*

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(32) OECD, *Guidelines for Fighting Bid Rigging in Public Procurement. Helping governments to obtain best value for money*, 2009, available at [oecd.org/dataoecd/27/19/42851044.pdf](http://oecd.org/dataoecd/27/19/42851044.pdf), last visited 4 October 2011.

(33) S. BARNES, *The UK Competition Appeal Tribunal holds its decision in the construction cover pricing appeal case (Kier Group and others)*, in *e-Competitions*, 11 March 2011, n. 35158.

(34) G. BATHORY, *The Hungarian Competition Authority fined construction companies for bid rigging in Budapest public construction tenders (Alterra)*, in *e-Competitions*, 18 March 2004, n. 21785.

(35) Z. NÉMETH, *A Hungarian Court annuls the decision of the Competition Office having found guilty construction companies of bid rigging taking into account lack of proof of single and continuous infringement (Heves – Nógrád county tenders)*, in *e-Competitions*, 19 April 2011, n. 35772.

to bid or to submit a losing bid may receive subcontracts or supply contracts from the designated winning bidder in order to divide the proceeds from the illegally obtained higher priced bid among them".(36) Hence, requiring proof of actual participation (i.e. submission of a bid) generates a safe harbour for some of the companies involved in this type of collusion.

### 3.3. Bid rigging in other markets

Recent decisions regarding bid rigging in other procurement markets are also worth noting, particularly in those jurisdictions where bid rigging is a criminal offence, such as Germany. Recently, in July 2011, the German Federal Cartel Office imposed fines on manufacturers of fire fighting vehicles and turntable ladders that had been rigging bids for a rather lengthy time period of around 10 years.(37) In this case, the colluding undertakings used the external help of an independent accountant (resembling other cases of illegal exchanges of information, such as the well-known *John Deere* case law),(38) which may raise awareness on the part of competition authorities as to new trends in bid rigging practices.

Not only markets for supplies or works are affected by bid rigging through exchange of information. Services markets have also been the object of recent decisions. For instance, the French Competition Authority fined 14 companies with almost € 10 million for having shared almost all public markets for the restoration of historic monuments. In this case, undertakings organized «roundtables» where they divided the regional restoration building markets in view of the annual schedule prepared and published by the relevant contracting authority. In this case, it is plain to see that an excessive transparency on the part of the contracting authority made collusion simple and easy to monitor. Companies also used cover bids for outside regions where they placed bids for contracts in order to 'inflate numbers' in the appearance of high levels of competition and then exchanged their services.(39)

Shortly after this and also in the services industry, in its decision of 24 February 2011, the French Competition Authority considered that four companies had concluded anticompetitive arrangements between 2005 and 2006 by

(36) OECD, *Guidelines for Fighting Bid Rigging in Public Procurement*.

(37) J. BAIER, *The German Federal Cartel Office imposes fines on manufacturers of firefighting vehicles and turntable ladders*, 27 February 2011, *e-Competitions*, n. 38335.

(38) On the ECJ case law related to information exchange, see C. ROQUES, *L'échange d'informations en droit communautaire de la concurrence: Degré d'incertitude et jeu répété*, in *Concurrences*, N° 3-2009, n. 26897.

(39) M. PUJDAK – A. DHALIWAL, *The French competition authority fines 14 companies 9 803 590 M € for having shared almost all public markets for the restoration of historic monuments*, in *e-Competitions*, 26 January 2011, n. 35150.

fixing their prices to respond to procurements launched in the painting services sector for naval equipment and engineering structures, which covered, in particular, the renovation of quays, cranes and locks in several harbours.<sup>(40)</sup> The French Authority found that the colluding companies had exchanged with each other the prices they intended to offer to the contracting entities and agreed to submit sham bids aimed at creating an impression of genuine competition. It is worth stressing that, in both of the mentioned cases, the French Authority understood the gravity of cover pricing and imposed rather heavy fines – which, however, were reduced in some case in regard of the weak financial situation of some of the companies (an issue that would merit separate analysis).

Almost contemporarily, on 25 March 2011, a Danish District Court convicted two environmental laboratories for bid rigging and imposed fines on each of the two companies and their directors.<sup>(41)</sup> The court found that the two directors intentionally had coordinated prices and agreed to share the bids between them, so that only one company would submit a bid in each of the two open tenders. The companies tried to defend alleging they had formed a consortium to bid jointly in both tenders, which the court dismissed easily, since there was no proof of consortium and the bids had been presented under the name of only one company in each of the procedures.

#### 4. Preliminary Conclusion

Therefore, in view of the anecdotal evidence offered by the abovementioned recent cases, no doubt can be harboured as to the pervasiveness of bid rigging in almost any economic sector where the public buyer sources goods, works and services – therefore, justifying the increasing efforts of competition authorities to prosecute and sanction bid rigging in procurement markets. However, as has also evaporated from some of the judgments by appeal courts in those same cases, *there may be a need for additional backing up of the competition authorities at review level, for which a more economic approach (or a better understanding of the working of collusion in the public procurement setting) may be required.*<sup>(42)</sup> In any case, the relevance and extension of bid

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(40) C. SAUMON – I. FOSSATI-KOTZ, *The French Competition Authority fines four companies for bid rigging in the painting services sector for naval equipment and engineering structures (Philippe Lassarat, Prezioso-Techmilor, Grivetto, Sorespi Bretagne)*, in *e-Competitions*, 24 February 2011, n. 35148.

(41) J. BORUM, *A Danish court imposes fines on two environmental laboratories and their directors for bid rigging (Environmental Laboratory and Milana)*, in *e-Competitions*, 25 March 2011, n. 35708.

(42) See, amongst others, the insightful analysis of R. C. MARSHAL – L. M. MARX, *The Economics of Collusion. Cartels and Bidding Rings*, Cambridge, MIT Press, 2012. See also S. E. WEISHAAR, *Cartels, Competition and Public Procurement. Law and Economics Approaches to Bid Rigging*, New Horizons in Competition Law and Economics, Cheltenham, Edward Elgar, 2013.

rigging strongly supports not only the prosecution of infringers on the basis of competition law, but also the development of engrained or built-in anti-collusion mechanisms in public procurement law. It is plain to see that any actions aimed at preventing and deterring bid rigging in the arena of public procurement rules and their enforcement will be a valuable complement to any further developments on the competition law enforcement front. Therefore, we will now turn to the analysis of the tools that the European Commission is proposing to introduce or improve in the current revision of the EU Directive on public procurement.

## Part II

### *1. Tools to Prevent and Deter Bid Rigging in the New Public Procurement Directive*

As has already evaporated from the analysis in Part I, and given that public procurement strongly relies on competitive markets, there is a strong need to ensure that the design of public procurement rules and administrative practices are fit and appropriate to promote competition and, particularly, to avoid instances of bid rigging. This has been recently emphasized (although in still relatively obscure terms) in the framework of the revision of the 2004 EU public procurement rules – which stresses, for instance, that

*“[w]hilst greater use of repetitive purchasing techniques should have overall positive benefits for [contracting authorities], there are some concerns about market closure and the longer-term access of firms to such tools. This would have to be addressed to ensure transparency and non-discrimination and prevent a restriction of competition.”*<sup>(43)</sup> Indeed, *“[t]he first objective [of this revision process] is to increase the efficiency of public spending. This includes on the one hand, the search for best possible procurement outcomes (best value for money). To reach this aim, it is vital to generate the strongest possible competition for public contracts awarded in the internal market. Bidders must be given the opportunity to compete on a level-playing field and distortions of competition must be avoided. At the same time, it is crucial to increase the efficiency of procurement procedures as such.”*<sup>(44)</sup>

Even if only in relation with centralised procurement, the recitals of the 2011 Proposal for a new Directive on Procurement expressly mentioned the risk of collusion, in the following terms:

<sup>(43)</sup> EU Commission, *Executive Summary of the Impact Assessment Accompanying the Proposal for a Directive on Public Procurement*, SEC(2011) 1586 final, available at [ec.europa.eu/internal\\_market/publicprocurement/docs/modernising\\_rules/SEC2011\\_1586\\_en.pdf](http://ec.europa.eu/internal_market/publicprocurement/docs/modernising_rules/SEC2011_1586_en.pdf), last accessed 23 January 2012.

<sup>(44)</sup> EU Commission, *Green Paper on the modernization of EU public procurement policy-Towards a more efficient European Procurement Market*, available at [eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:DKEY:556316:EN:NOT](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:DKEY:556316:EN:NOT), last accessed 23 January 2012.

“... the aggregation and centralisation of purchases should be carefully monitored in order to avoid excessive concentration of purchasing power and collusion, and to preserve transparency and competition, as well as market access opportunities for small and medium-sized enterprises” [recital (20); emphasis added].

Indeed, all this seems to be significantly in line the general trend underlying this latest revision of the EU procurement Directives (together with modernization and procedural simplification). It is worth stressing that Article 18 of the new Directive 2014/24 on procurement, entitled “Principles of procurement” consolidates the relevance of undistorted competition (or competitive neutrality) by clearly emphasizing that:

*“The design of the procurement shall not be made with the intention of excluding it from the scope of this Directive or of artificially narrowing competition. Competition shall be considered to be artificially narrowed where the design of the procurement is made with the intention of unduly favouring or disadvantaging certain economic operators.”*

In my view, this provision agglutinates the pro-competitive orientation present in the EU procurement Directives from their initial design in the 1970s, and brings to light the underlying principle of competition embedded in their 2004 version<sup>(45)</sup> – which could be defined or phrased in these terms: public procurement rules have to be interpreted and applied in a pro-competitive way, so that they do not hinder, limit, or distort competition. Contracting entities must refrain from implementing any procurement practices that prevent, restrict or distort competition. Therefore, *it seems clear to me that the revision new EU public procurement rules have a clear orientation towards safeguarding (or, at least, promoting) competitive neutrality as a booster for enhanced competition and, in the end, increased value for money through better procurement efficiency.* Therefore, it should be expected that the new Directive contains some rules and instruments oriented towards the prevention and deterrence of bid rigging – which we will analyse below.

As I said elsewhere,<sup>(46)</sup> with the inclusion of Article 18 in the new Directive, it is getting clearer and clearer that market integration in procurement must go hand in hand with promoting and protecting effective competition for public contracts, and the drafting of Article 18 of the new Directive finally overcomes some difficulties in the development of EU procurement rules – which still suffered the problem of being excessively focused on preventing discrimination

(45) A. SÁNCHEZ GRAELLS, *The Principle of Competition Embedded in EC Public Procurement Directives*, Working Paper, University of Nottingham, 2009, available at [ssrn.com/abstract=1928724](http://ssrn.com/abstract=1928724), last accessed 23 January 2012.

(46) A. SÁNCHEZ GRAELLS, *Are the Procurement Rules a Barrier for Cross-Border Trade within the European Market? A View on Proposals to Lower that Barrier and Spur Growth*, in C. Tvarnø, G. S. Ølykke & C. Risvig Hansen, *EU Public Procurement: Modernisation, Growth and Innovation*, Copenhagen, DJØF, 2012, 107-133, available at [ssrn.com/abstract=1986114](http://ssrn.com/abstract=1986114), accessed 5 November 2012.

based on nationality (which has overshadowed other discrimination problems, protectionist policies and competition restrictions and distortions in European public procurement)<sup>(47)</sup> – although a broader objective of fostering competition on the basis of fair and open access to procurement (not only for bidders from different Member States) can already be identified in Directive 2004/18 and is further reinforced in the new procurement Directive.

The introduction of the general principle of competition must be welcomed as a very positive development in EU public procurement law. Surely, the drafting will generate some enforcement difficulties (particularly in view of the insertion of an element of intention that may complicate the extraction of the proper consequences from the principle). However, in my view, this express recognition of the principle will strengthen the push towards a more competition-oriented public procurement system and, in due course, will boost some of the interpretative proposals that seek to maximise participation in procurement and to minimise the anticompetitive effects of the activities of the public buyer.

## ***2. General measures: “collusion-conscious” (and pro-competitive) tender design***

In general, as can be extracted from the OECD guidelines on the prevention of bid rigging in public procurement, there is a number of measures that contracting authorities can adopt to try to minimise pro-collusive features of their tenders, such as:<sup>(48)</sup> 1) defining their requirements clearly and avoiding predictability in procurement; 2) designing the tender process to effectively reduce communication among bidders; 3) carefully choosing evaluation and award criteria; or 4) raising staff awareness about the risks of bid rigging in procurement. Even if it is true that the EU Directives do not contain specific requirements in any of these areas, the rules of the Directives allow for contracting authorities to exercise discretion in regard to all those factors – and, consequently, I think it is safe to assume that the legal framework is well aligned for the design of “collusion-conscious” tender procedures. In this regard, the inclusion of the general principle of competition in Article 18 of the new Directive should raise awareness of contracting authorities on competition implications of procurement rules and tender documents and decisions, and should spur the development of a more competition-oriented public procurement practice.

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(47) A. SÁNCHEZ GRAELLS, *Public Procurement and the EU Competition Rules*, Oxford, Hart Publishing, 2011, 108-110 and 212-219.

(48) OECD, *Guidelines for Fighting Bid Rigging in Public Procurement*, 2009.

### ***3. In particular, the issue of division of contracts into lots and its impact on collusion***

One of the aspects that can have a major impact on collusion incentives is the potential division of the contractual object into lots. Under their 2004 version, EU public procurement Directives regulated neither the division of contracts into lots, nor the bundling of those lots or the aggregation of contracts by the public buyer. The only rules regarding division of contracts into lots aimed at establishing specific criteria for the calculation of the value of the tendered contracts for the purpose of determining the applicability of the EU public procurement regime (art. 9 of directive 2004/18) – and, more specifically, with the purpose of preventing the circumvention of EU rules by the artificial division of contracts into lots whose value remained below the thresholds that triggered their application.<sup>(49)</sup> Other than that, reference to the division of contracts into lots, their bundling or aggregation was only made in relation to contract notices – which, where the contracts were subdivided into lots, must indicate ‘*the possibility of tendering for one, for several or for all the lots*’ (Annex VII A of Directive 2004/18).

Therefore, Member States currently seemed to hold substantial discretion to set domestic public procurement rules on the division of contracts into lots, the bundling or aggregation of lots and contracts to be tendered together, the establishment of rules allowing or not for multiple and/or conditional tendering for different lots in a given tender procedure, etc. However, as mentioned already, it should be stressed that the bundling of requirements into a single contract or the division of that same contractual object into several lots, as well as the rules imposing the minimum or maximum number of lots a single tenderer can bid for, allowing or excluding conditional or ‘package’ bidding and so on, can generate significant effects on competition for those contracts and in the market concerned.<sup>(50)</sup>

Indeed, the bundling of independent requirements into a single contract (or the aggregation of otherwise independent contracts) by one or several public buyers may restrict the number of potential bidders and, therefore, generate

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(49) This has been an issue that has generated substantial litigation, even if the treatment of the division of contracts into lots for jurisdictional purposes in the EU directives is relatively straightforward. See ECJ, Case C-323/96 *Commission v Belgium* [1998] ECR I-5063; ECJ, Case C-16/98 *Commission v France* [2000] ECR I-675; ECJ, Case C-385/02 *Commission v Italy* [2004] ECR I-8121; ECJ, Case C-241/06 *Lämmerzahl* [2007] ECR I-8415; and ECJ, Case C-412/04 *Commission v Italy* [2008] ECR I-619.

(50) For a review of bundling and its effect on competition in the U.S., see D. D. PANGBURN, *The Impact of Contract Bundling and Variable-Quantity Contracts on Competition and Small Business*, in *PCLJ*, 1995-1996, 69; I. AKYUZ, *Bundling into the Millenium: Analyzing the Current State of Contract Bundling*, *PCLJ*, 2000-2001, 123.

anticompetitive effects,(51) and alter the structure of the markets.(52) Put otherwise, dividing contracts into several lots may in most instances increase competition,(53) not only for the specific public contract but also for future contracts,(54) and in more general terms, in the market from which the public buyer is procuring goods and services. The (sub)division of contracts into lots can particularly promote participation by SMEs(55) – thereby broadening competition to the benefit of contracting authorities, as well as reducing the need to resort to more restrictive ‘secondary policies’ aimed at encouraging SME participation (such as set-asides). Therefore, in general terms, dividing contracts into lots or avoiding the aggregation of otherwise independent requirements into a single contract can have significant pro-competitive effects both on the tender and the market.

Nonetheless, *the division of contracts into lots also presents some difficulties or undesirable effects and can generate some additional costs.*(56) Firstly, division of a given contract into lots may not be feasible in the light of the respective works, supplies and services. Therefore, rules regulating the division of contracts into lots should allow for sufficient flexibility so as not to artificially impose the fractioning of the contractual object where it is technically or economically unfeasible, or where it would substantially impair the effectiveness of the procurement process or raise the procurement costs disproportionately. On the other hand, public procurement rules should restrict the ability of contracting authorities to artificially bundle or aggregate otherwise independent needs or requirements if doing so generates a competitive distortion – i.e. if it excludes potential tenderers with a more limited capacity of supply, not integrated vertically, or otherwise not able to meet the bundled requirements, while they would be able to meet some of the requirements if unbundled

(51) See J.-Y. CHÉROT, *Droit public économique*, Paris, Economica, 2nd edn, 2007, 728. For a position against contract aggregation see E. S. SAVAS, *Privatization and Public-Private Partnerships*, New York, Chatham House, 2000,186. See also OFT, *Assessing the Impact of Public Sector Procurement on Competition*, 2004, 16-20 and 110-125.

(52) At least in those cases where bundling of different goods or services induces vertical integration amongst previously independent public contractors; see OFT, *Assessing the Impact of Public Sector Procurement on Competition*, 2004, 89-91 and 118.

(53) R. P. MCAFEE – J. McMILLAN, *Incentives in Government Contracting*, cit., 57-60; and V. GRIMM et al., *Division into Lots and Competition in Procurement*, in N. Dimitri et al. (eds. by), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 168 and 175.

(54) L. CARPINETI et al., *The Variety of Procurement Practice: Evidence from Public Procurement*, in N. Dimitri et al. (eds. by), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 14 and 23-24.

(55) See Commission staff working document – *European code of best practices facilitating access by SMEs to public procurement contracts* [SEC(2008) 2193] at 6-7. Also C. BOVIS, *EC Public Procurement Law*, London, Longman, 1997, 117; L. CARPINETI et al., *The Variety of Procurement Practice*, cit., 23-24; and M. BURGI, *Small and Medium-Sized Enterprises and Procurement Law – European Legal Framework and German Experiences*, in *PPLR*, 2007, 284 and 293 – 294.

(56) See R. P. MCAFEE – J. McMILLAN, *Incentives in Government Contracting*, cit., 57-60.

or not aggregated. Therefore, public procurement rules should encourage lot division, unless it proves to be inadequate or disproportionate to the nature and amount of works, supplies and services concerned.

Secondly, *economic theory has stressed that the division of the contract into lots might yield pro- or anti-competitive results depending on the relationship between the number of lots and the number of interested bidders.* One of the potentially negative effects of the division of the contract into lots is the facilitation of collusion.<sup>(57)</sup> Therefore, setting a number of lots that generates difficulties for coordination and allocation of lots amongst potentially colluding tenderers is highly desirable.<sup>(58)</sup> In this regard, economic theory seems to provide two general criteria: the number of lots should be smaller than the expected number of participants (so that the impossibility of allocating lots to all interested tenderers diminishes the stability of collusion and forces it to spread over several tenders, thereby increasing the likelihood of detection), and the number of lots should exceed the number of incumbent contracts by at least one (implicitly reserving at least the additional lot for a new entrant or new contractor)<sup>(59)</sup>. Therefore, it also seems undesirable to adopt rigid rules setting a specific number of lots into which the contract should be automatically divided, since it could easily fall outside the desirable range for specific contracts and tendering procedures.

Finally, another important issue in the design of rules regarding lot division is to determine whether bidders can engage in multiple or ‘package’ bidding – and, if so, what are the minimum and maximum number of lots for which they can bid – and if conditional bidding is allowed, thus permitting bidders to offer varying conditions dependent upon the number and mix of lots awarded to them. In this regard, economic theory again stresses the importance of setting flexible rules that allow for a trade-off between fostering competition by smaller bidders and allowing larger bidders to exploit economies of scale, as well as for independent decisions to be made by tenderers – since multiple or package bidding will encourage bidders to submit more competitive offers for given packages than they would for independent lots or for all the lots.<sup>(60)</sup>

<sup>(57)</sup> Division of contracts into lots allows for *accommodation*; P. R. MILGROM, *Putting Auction Theory to Work*, Cambridge, Cambridge University Press, 2004, 234-239; and increasing the frequency of bidding increases the likelihood of collusion (*ie* more smaller tenders, or more tenders divided into lots, might give rise to increased opportunities for collusion); see OECD, *Competition in Bidding Markets* (2006) 35. See also V. GRIMM et al., *Division into Lots and Competition in Procurement*, *cit.*, 168.

<sup>(58)</sup> See OECD, *Guidelines for Fighting Bid Rigging in Public Procurement*, 2009, 4.

<sup>(59)</sup> See V. GRIMM et al., *Division into Lots and Competition in Procurement*, *cit.*, 168-169; and K. BINMORE – P. KLEMPERER, *The Biggest Auction Ever: The Sale of the British 3G Telecom Licenses*, *Economic Journal*, 2002, C74.

<sup>(60)</sup> N DIMITRI et al., *Multi – Contract Tendering Procedures and Package Bidding in Procurement* in *ibid.* (eds. by), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 193, 194-215. Basically, the flexibility advanced tries to avoid second-guessing by the public buyer on the value of the

In this regard, it has been stressed that contracting authorities should not limit the number of lots tenderers can bid for in a way which would impair the conditions for fair competition,(61) with maybe the only restriction of setting a relatively low maximum number of lots that a single bidder can be awarded at one time(62) (which constitutes a specific case of awarding constraint).(63) Therefore, it seems desirable to adopt rules so that the public buyer can reduce the minimum size of contracts/lots, and thereby maximize the number of smaller suppliers otherwise excluded, without hindering the ability of larger suppliers to bid for large sets of contracts in the event of their being characterized by positive complementarities.(64)

To sum up, economic theory seems to support the finding that public procurement rules should be designed so as to encourage the division of contracts into lots whenever this is technically and economically feasible, and to allow the contracting authority to set the specific number of lots according to the circumstances of the tender. Similarly, contracting authorities should be able to restrict the maximum number of lots that a single tenderer can be awarded – if awarding the entire contract to a single contractor can generate a negative impact on competition; and particularly when ensuring that one or more lots are available for non-incumbent contractors is relevant to preventing distortions of competition in future contracts and/or in the market concerned. Finally, conditional and ‘package’ bidding should be allowed, in order to minimise the potential inefficiencies that lot division could generate.

The general criterion, in my view, should then be that in the exercise of this discretion as regards the division or aggregation of requirements, the fixing of the number of lots tendered, and the rules for conditional and ‘package’ bidding, contracting authorities must ensure that competition in the market is not distorted and, where possible and feasible, promote competition for the contract – particularly by avoiding the configuration of contracts which result in potentially interested competitors being excluded. As a default rule, division into a large number of lots will be preferable to a division into an insufficient number of exceedingly large lots, since tenderers could compensate for

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lots or bundles, which the bidders are prepared to appraise independently. On the issue of the different values of bundles and its effect on competition, see M. M. LINTHORST et al., *Buying Bundles: The Effects of Bundle Attributes on the Value of Bundling*, in G. Piga and K.V. Thai (eds. by) *International Public Procurement Conference Proceedings – Enhancing Best Practices in Public Procurement*, 2008, 513.

(61) EU Commission, staff working document, *European code of best practices facilitating access by SMEs to public procurement contracts*, SEC(2008) 2193, 6-7.

(62) E. S. SAVAS, *Privatization and Public-Private Partnerships*, cit., 186.

(63) See L. CARPINETI et al., *The Variety of Procurement Practice*, cit., 36.

(64) N. DIMITRI et al., *Multi-Contract Tendering Procedures and Package Bidding in Procurement*, cit., 215. This option might not be optimal in all types of (dynamic) auctions, though (*ibid.* at 206); and also L. M. AUSUBEL – P. CRAMTON, *Dynamic Auctions in Procurement*, in N. Dimitri et al. (eds), *Handbook of Procurement*, Cambridge, Cambridge University Press, 2006, 220 and 226-227.

such an ‘excessive fragmentation’ of the object of the contract by submitting bundled offers – while an insufficient division of the object of the contract cannot be compensated by tenderers submitting partial offers or offers for amounts smaller than the object of the tender (as those bids would be considered non-compliant and, hence, rejected).

Arguably, in order to be effective, the rules and decisions on lot division will need to be complemented with clear award criteria as regards the comparability of offers for a different number of lots, as well as with rules applicable in case the offers submitted do not cover all the lots tendered. In this case, asking bidders to submit offers for the entire contract, for each individual lot and for the packages of lots that they would like to be awarded (with different prices and conditions) would arguably eliminate all the benefits of lot division, since tenderers that could not bid for the entire contract (even under less favourable conditions than they could offer for a given lot or group of lots) would be excluded anyway. Therefore, a preferable rule seems to be to allow the submission of bids for independent or grouped lots, without mandatory requirements regarding the entire contractual object. In case one or various lots could not be covered in the initial tendering, the contracting authority could then engage in re-tendering the pending lots by following a subsequent negotiated procedure with all the participating tenderers [by analogy with Art. 31(1)(a) of directive 2004/18 and now Art. 32(2)(a) of directive 2014/24], or a new open or restricted procedure, depending on the circumstances. Under exceptional circumstances, the option should also be available to the contracting authority not to award any of the lots for which it has received offers if it is clear that this would jeopardize the effectiveness of the follow-up tenders for the remaining lots – which should then be retendered in a single contract. However, if the design of the lots was properly conducted in the first place – i.e. if lots had been designed according to sensible functional and economic criteria, and an effort had been made to ensure their balance – this situation should be largely marginal.

Therefore, as a preliminary conclusion, in my opinion, contracting authorities should resort to division of contracts into lots whenever it is not unfeasible technically or economically, and should set rules that ensure that, while still giving tenderers the largest possible flexibility to submit package and conditional bids, competition is not distorted by undue contract division or aggregation. Rules on contract division should be complemented and reinforced by consistent award criteria and rules on the retendering of unawarded lots.

These thoughts seem to have a relatively easy accommodation within the *new provisions on division of contracts into lots included in article 46 of the new EU Directive on public procurement*. However, it is worth stressing that the final text is much less prescriptive than initially thought and that Member States have shown a reluctance to accept the more aggressive policy promoted by the

European Commission in its initial 2011 proposal, which clearly aimed towards the mandatory division of contract requirements in lots by the adoption of a principle of “divide or explain” for contracts above 500,000 Euro, according to which “*Where the contracting authority [...] decides against an award in the form of separate lots, the procurement documents or the individual report [...] shall include an indication of the main reasons for the contracting authority’s decision.*” [Art. 44(1) of 2011 Proposal, as amended by the July 2012 Compromise Text(65)]. This would have been in line with the proposal that public procurement rules should encourage lot division, unless it proves to be inadequate or disproportionate to the nature and amount of works, supplies and services concerned.(66) Nonetheless, the final wording of Article 46 of Directive 2014/24 is more open-ended and leaves it to the discretion of the Member States to create an effective obligation to divide contracts into lots. According to the final wording:

“1. *Contracting authorities may decide to award a contract in the form of separate lots and may determine the size and subject-matter of such lots. Contracting authorities shall, except in respect of contracts whose division has been made mandatory pursuant to paragraph 4 of this Article, provide an indication of the main reasons for their decision not to subdivide into lots, which shall be included in the procurement documents or the individual report referred to in Article 84.*”

In paragraph 4, it is established that

“*Member States may [...] render] it obligatory to award contracts in the form of separate lots under conditions to be specified in accordance with their national law and having regard for Union law.*”

It will be interesting to see how Member States decide to shape their domestic policies on mandatory lot division.

Similarly, allowing for the flexibility supported by economic theory, the rest of Article 46 of the new EU Directive on public procurement sets sensible rules for contract division into lots. On the one hand, it is proposed that contracting authorities may, even where the possibility to tender for all lots has been indicated, limit the number of lots that may be awarded to a tenderer, provided that the maximum number is stated in the contract notice or in the invitation to confirm interest – that is, Article 46(2) of Directive 2014/24 allows for the capping of the total number of lots that one single supplier can be awarded (and this is an awarding constraint recommended by economists). In that case,

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(65) Please note that the initial wording of Article 44 of the 2011 Proposal was more oriented towards lot division: “*where the contracting authority does not deem it appropriate to split into lots, it shall provide in the contract notice or in the invitation to confirm interest a specific explanation of its reasons.*” Arguably, the July 2012 Compromise text watered down the possibilities for judicial review of such a decision not to split the contract into lots.

(66) A. SÁNCHEZ GRAELLS, *Public Procurement and the EU Competition Rules*, cit., 286-290.

contracting authorities shall determine and indicate in the procurement documents the objective and non-discriminatory criteria or rules for awarding the different lots where the application of the chosen award criteria would result in the award to one tenderer of more lots than the maximum number.

The new Directive also includes an interesting rule for the evaluation of independent, partial and bundled offers for a contract divided into lots. According to Article 46(3) of Directive 2014/24, contracting authorities shall first determine the tenders fulfilling best the award criteria for each individual lot. As a result of the evaluation, though, they may award a contract for more than one lot to a tenderer that is not ranked first in respect of all individual lots covered by this contract, provided that the award criteria are better fulfilled with regard to all the lots covered by that contract (i.e., in case the bundled offer is superior to the aggregation of offers for single lots, or partial offers in other bundled offers). Indeed, Member States may provide that, where more than one lot may be awarded to the same tenderer, contracting authorities may award contracts combining several or all lots where they have specified in the contract notice or in the invitation to confirm interest that they reserve the possibility of doing so and indicate the lots or groups of lots that may be combined. In any case, in order to prevent manipulation, contracting authorities shall specify the methods they intend to use for such comparison in the procurement documents – which shall be transparent, objective and non-discriminatory.

In general, then, the rules on contract division and tendering for lots included in the proposal for a new EU Directive on public procurement seem well oriented and substantially aligned with economic theory and, consequently, should contribute to prevent collusion in procurement.

#### ***4. Exclusion of competition law infringers, and outline of a proposal for a fuller suspension and debarment system***

Another important instrument in the prevention and deterrence of bid rigging in public procurement can be found in the rules controlling the disqualification of competition law offenders (in particular, members of a previously discovered cartel). If contracting authorities could exclude potential tenderers that have breached competition law in previous occasions – either in a particular instance or, more permanently, by suspending or debarring them from future participation – the (financial) interests at stake for any undertaking to participate in bid rigging would raise significantly. In case an effective exclusion, suspension and debarment system is in place, cartelists know that they risk not only competition law prosecution, but also losing all chances to secure public contracts for a significant period of time, or

even permanently. That risk of being excluded of a significant tranche of the market (particularly in sectors where public buyers accumulate a significant volume of purchases) seems a powerful tool that has, so far, being used only in a limited manner in EU law. If so, the largeness of the potential (economic) losses should significantly increase the incentive of tenderers to refrain from colluding.<sup>(67)</sup>

In this regard, it is interesting to see that, as a complement to other measures oriented at reducing red tape and fostering participation by SMEs<sup>(68)</sup> – an in order to strengthen competition (i.e. to make the competitive tension between bidders more intense) – the new Directive also includes a specific provision that tries to clarify the rules on disqualification of competition law infringers and, consequently, aims to prevent, deter and punish instances of collusion on public procurement.

To be sure, the 2004 EU procurement rules already contained provisions that would allow contracting authorities or entities to disqualify infringers of competition law, given that breaches of competition law should always be considered instances of grave professional misbehaviour [in particular, under art. 45(2)(c) and (d) of Directive 2004/18].<sup>(69)</sup> This seems clearly established in recital 101 of the new Directive:

*“Contracting authorities should further be given the possibility to exclude economic operators which have proven unreliable, for instance because of violations of environmental or social obligations, including rules on accessibility for disabled persons or other forms of grave professional misconduct, such as violations of competition rules or of intellectual property rights.”*

However, some further clarification and a streamlining of the disqualification procedure would be welcome.

As indicated in the explanatory memorandum of the 2011 Proposal for a new EU Directive, it

*“contain[ed] a specific provision against illicit behaviour by candidates and tenderers, such as [...] entering into agreements with other participants to manipulate the outcome of the procedure [which] have to be excluded from the procedure. Such illicit activities violate basic principles of European Union and can result in serious distortions of competition.”*

<sup>(67)</sup> Implicitly, identifying similar risks of economic loss that would generate anti-collusion incentives (in that case, entry) see R. P. McAfee – J. McMillan, *Incentives in Government Contracting*, cit., 21, 111 and 150.

<sup>(68)</sup> On those measures, see A. SÁNCHEZ GRAELLS, *Are the Procurement Rules a Barrier for Cross-border Trade within the European Market? A view on proposals to lower that barrier and spur growth*, in C. D. Tvarnø, G. S. Ølykke and C. R. Hansen (eds.), *EU Public Procurement. Modernisation, Growth and Innovation*, Copenhagen, DJØF, 2012, 107.

<sup>(69)</sup> See A. SÁNCHEZ GRAELLS, *Public Procurement and the EU Competition Rules*, cit., 253-255; contra, C. BOVIS, *EC Public Procurement: Case Law and Regulation*, Oxford, Oxford University Press, 2006, 16.

More specifically, Article 22 of the 2011 Proposal for a new EU Directive required that, at the beginning of the procedure, tenderers

*“provide a declaration on honour that they have not undertaken and will not undertake to: [...] (b) enter into agreements with other candidates and tenderers aimed at distorting competition.”*

Further, in accordance with Article 68 of the 2011 Proposal, regulating impediments to award,

*“[c]ontracting authorities shall not award the contract to the tenderer submitting the best tender where [...] (b) the declaration provided by the tenderer pursuant to Article 22 is false.”*

Therefore, if the contracting authority became aware of any illicit, anti-competitive behaviour on the part of tenderers, it was required to disqualify them by applying the impediment to award in art 68(b) of the 2011 Proposal. However, I found that solution partial and that it required further thought.

The final text of Directive 2014/24 has suppressed Articles 22 and 68 of the 2011 Proposal and derived the issue to the new drafting of the grounds for the exclusion of tenderers in Article 57. In that regard, it is worth stressing that, according to Article 57(4)(d)

*“Contracting authorities may exclude or may be required by Member States to exclude from participation in a procurement procedure any economic operator in any of the following situations: [...] (d) where the contracting authority has sufficiently plausible indications to conclude that the economic operator has entered into agreements with other economic operators aimed at distorting competition.”*

Moreover, it must be highlighted that, according to Article 57(5),

*“At any time during the procedure, contracting authorities may exclude or may be required by Member States to exclude an economic operator where it turns out that the economic operator is, in view of acts committed or omitted either before or during the procedure, in one of the situations referred to in paragraph 4.”*

Interestingly, Article 57(6) of the new Directive also generates room for self-cleaning actions:

*“Any economic operator that is in one of the situations referred to in paragraphs 1 and 4 may provide evidence to the effect that measures taken by the economic operator are sufficient to demonstrate its reliability despite the existence of a relevant ground for exclusion. If such evidence is considered as sufficient, the economic operator concerned shall not be excluded from the procurement procedure.”*

Some of the relevant aspects of the disqualification regime will still need to be designed at national level, though, since Article 55(7) foresees that

*“By law, regulation or administrative provision and having regard to Union law, Member States shall specify the implementing conditions for this Article. They shall, in particular, determine the maximum period of exclusion if no measures as specified in paragraph 6 are taken by the economic operator to demonstrate its*

*reliability. Where the period of exclusion has not been set by final judgment, that period shall not exceed five years from the date of the conviction by final judgment in the cases referred to in paragraph 1 and three years from the date of the relevant event in the cases referred to in paragraph 4.”*

Overall, the new text overcomes some of the difficulties in the initial disqualification system foreseen in Articles 22 and 68 of the 2011 Proposal.

Indeed, the disqualification system envisaged in Articles 22 and 68 of the 2011 Directive fell short from ensuring that infringers of competition law do not participate in public procurement—mainly, due to two considerations. On the one hand, it only allowed for disqualification prior to award of the contract. However, it can be foreseen that most instances of bid rigging will only be discovered later and, maybe even after the execution of the contract is complete (when the remedy of the impediment to award will be absolutely ineffective) (this is remedied by Art. 57(4) of the new version). On the other hand, it could generate some doubts as to the possibility to apply Art. 45(2)(c) and (d) [renumbered as Art. 55(3)(c) and (d) of the 2011 Proposal] in relation with violations of competition that are not connected with the tender at hand (which is now expressly excluded by the wording of Article 57(4)(d), in what is in my opinion a criticisable restriction of the disqualification mechanism). In my view, even if the new Directive increases legal certainty in some cases, there is still a need for a further developed suspension and debarment system in EU public procurement rules.<sup>(70)</sup>

Given the optional terms in which Article 57 of the new rules is drafted, such open regulation at EU level can give rise to different regimes across different Member States and, consequently, might facilitate strategic behaviour by infringing undertakings – thereby reducing deterrence. In my view, a stricter and uniform system of suspension and debarment of competition law infringers would contribute to strengthening the pro-competitive orientation of the public procurement system and to limiting privately-created distortions of competition.<sup>(71)</sup>

From a comparative perspective, it seems important to highlight that the United States’ Federal Acquisitions Regulation (US FAR) establishes a clearer regime of suspension and debarment of competition infringers. At the very least, it is remarkable that a ‘*violation of Federal or State antitrust statutes relating to the submission of offers*’ constitutes both a cause for suspension [US FAR 9.407-2(a)(2)] and for debarment [US FAR 9.406-2(a)(2)] of the offending contractor. Thus, the infringer can be suspended for a temporary period

<sup>(70)</sup> A. SÁNCHEZ GRAELLS, *Public Procurement and the EU Competition Rules*, cit., 382-385.

<sup>(71)</sup> Which, however, would not be without cost; see G. L. ALBANO et al., *Preventing Collusion in Public Procurement*, in N. Dimitri et al. (eds. by), *Handbook of Procurement*, cit., 347-380.

pending the completion of investigation and any ensuing legal proceedings [US FAR 9.407-4(a)] and, eventually, debarred (i.e. prevented from participating in all public tenders) for a period commensurate with the seriousness of the cause, and generally of up to three years [US FAR 9.406-4(a)(1)]. The decisions on suspension and debarment are not taken by the contracting authority itself, but by a previously designated suspension and debarment official [US FAR 9.406-3(a) and US FAR 9.407-3(a)]. Generally, debarment will exclude the contractor from all public tenders conducted during its extension, unless it is restricted to certain types of contracts or certain contracting authorities [US FAR 9.406-3(e)(1)(iv) in relation with US FAR 9.406-1(c)]. It is worth noting that suspension and debarment decisions are not meant to punish contractors, but to protect the public interest in the proper functioning of the procurement system [US FAR 9.402(b)].

In a nutshell, the general features of the regime established in the US FAR make it seem superior to the current EU public procurement rules in that the decision on the exclusion of the affected tenderer is not discretionary for the specific contracting authority (which might have a conflict of interest, particularly if the competition infringer is a well-known or an incumbent contractor), but adopted by a previously designated authority within the same agency.

Therefore, in light of the US regime, it is my opinion that it is desirable to strengthen the rules contained in the new Directive by adopting a rule whereby competition infringers could be suspended and/or debarred by an authority different from the contracting authority – and, subject to Member States' internal organization, the best alternative seems to be the competition authority or, eventually, the courts. Suspension and debarment should be triggered particularly by mandatory reporting of competition law breaches, but should also be available as a self-standing sanction in case the investigation is initiated by any other means – particularly, competition authorities should be empowered to adopt debarment decisions as a complement of any other competition sanctions and remedies (such as criminal sentences, fines and damages awards).

Such a regime should apply to all breaches of substantive competition law rules (not only collusion in public procurement processes), unless it can be proven that they are irrelevant in the public procurement setting (which seems unlikely): i.e. they should not be automatically limited to cases of bid rigging, and the (high) burden of proving the irrelevance of the anticompetitive practices in the public procurement setting should rest with the infringers. However, in the case of violations of competition law other than collusion in public procurement contracts, the duration and scope of the debarment could be more limited than in the case of the former, and clearly aimed at protecting the public interest in the proper functioning of procurement procedures – i.e. not as an additional or substitutive competition sanction.

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An exception to the suspension and debarment regime could be created to avoid reducing disproportionately or completely eliminating competition in highly concentrated markets (US FAR 9.405)(72) – where the exclusion of a potential contractor would render the procurement procedure largely ineffective. However, in these highly exceptional cases, a waiver of suspension or debarment should only be granted at the request of the affected contracting authorities (which should advance sufficient reasons in the public interest associated to the participation of the suspended or debarred tenderer) and, in any case, it should be substituted with an alternative sanction, such as the imposition of substitute fines or a deferral or extension of the debarment period after market conditions allow for the development of competition (if this is plausible).

Moreover, the provisions related to ‘self-cleaning’ included in Art. 57(6) of the new EU Directive on procurement could help mitigate the effects of suspension or debarment when tenderers actually adopted effective measures to prevent further violations of competition law. In this regard, it should be noted that, under the latter provision, any candidate or tenderer that is in one situation that could trigger exclusion may provide the contracting authority with evidence demonstrating its reliability despite the existence of the relevant ground for exclusion. For this purpose, the candidate or tenderer shall prove that it has compensated any damage caused by the criminal offence or misconduct, clarified the facts and circumstances in a comprehensive manner by actively collaborating with the investigating authorities and taken concrete technical, organisational and personal measures that are appropriate to prevent further criminal offences or misconduct. In such cases, contracting authorities shall evaluate the measures taken by the candidates and tenderers taking into account the gravity and particular circumstances of the criminal offence or misconduct; and, where the contracting authority considers the measures to be insufficient, it shall state the reasons for its decision. Therefore, this is an area where the development of effective competition compliance manuals can gain significant relevance in the future.(73)

To sum up, even if the new Directive does improve upon the rules on the exclusion of tenderers for violations of competition law currently included in the EU public procurement directives, the new system can still be smartened up because it grants full discretion to contracting authorities (which may be in a conflict of interest). After briefly considering the system applicable in the US, it seems desirable to prompt Member States to implement the new EU rules by

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(72) R. E. KRAMER, *Awarding Contracts to Suspended and Debarred Firms: Are Stricter Rules Necessary?*, in *PCLJ*, 2004, 539; and J. S. ZUCKER, *The Boeing Suspension: Has Increased Consolidation Tied the United States Department of Defence's Hands?*, in *PPLR*, 2004, 260.

(73) In general, on competition compliance and the adoption of an effective policy (including self-cleaning measures), see the guidance offered by the EU Commission, in [ec.europa.eu/competition/antitrust/compliance/index\\_en.html](http://ec.europa.eu/competition/antitrust/compliance/index_en.html), accessed 7 May 2012, and the Office of Fair Trading, in [oft.gov.uk/OFTwork/competition-act-and-cartels/competition-law-compliance/](http://oft.gov.uk/OFTwork/competition-act-and-cartels/competition-law-compliance/), accessed 7 May 2012.

granting the competence to suspend and debar infringers to an authority other than the contracting authority (and, preferably, to the competition authority), and to make suspension and debarment decisions mandatorily enforceable by contracting authorities. Suspension and debarment should not only be triggered by mandatory reports of suspected competition violations, but should also be configured as self-standing competition remedies aimed at protecting the public interest in the proper functioning of the procurement system. Limited waivers of the suspension and debarment regime could be introduced to avoid situations in which competition for public contracts might be excessively restricted – subject to adequate substitutive measures.

### Conclusions

This contribution has shown how instances of collusion in the public procurement setting are numerous. In view of such rampant bid rigging activities, it is only natural to try to identify measures aimed at making collusion more difficult and to create procurement-specific sanctions for competition law infringers. The analysis conducted here has not been comprehensive, as there are many issues that can be explored as mechanisms aimed at reducing collusion (especially in relation with evaluation processes and award criteria). However, the contribution has focused on two specific tools that I think could make a substantial difference in the prevention and dissuasion of bid rigging.

In that regard, it has first described how the general rules – and, in particular, the rules included in Article 46 of the new EU Directive on public procurement – create the appropriate, flexible framework for contracting authorities to design tender procedures in a “collusion-conscious” or pro-competitive manner. To be sure, capacity building, training and market intelligence mechanisms are necessary complements to this legal framework, and the actual adoption of a more competition-oriented procurement practice will crucially depend on how contracting authorities exercise their (increased) discretion – both now and after the revision of the EU procurement rules.

As a complementary mechanism, the chapter has then explored the rules on exclusion of competition law infringers and advanced some ideas for the development of a more comprehensive (US-inspired) system of suspension and debarment for cartelists beyond the solutions adopted in the Article 57 of the new Directive – particularly oriented at increasing the (financial) costs of getting involved in instances of *bid rigging*, as well as a mechanism to (indirectly) prevent recidivism in this area. Again, the identification of instances of collusion and the commitment to an actual push for exclusion (suspension, and debarment) of competition law infringers is highly dependent on how contracting authorities exercise their (increased) discretion.

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As a general conclusion, hence, I think that it is important to stress that the *OECD guidelines for Fighting Bid Rigging in Public Procurement* contain relevant, practical recommendations for contracting authorities to follow in the design, running and oversight of their procurement procedures – and that their implementation is already possible within the 2004 EU rules on procurement and may be even easier in the future under the new EU Directive 2014/24 on public procurement.

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**CHAPTER 3**  
**Contracting authorities' inability to fight bid rigging  
in public procurement: reasons and remedies(1)**

BY

Antonio LÓPEZ MIÑO

Head of the Investigation Direction,  
Council of Competition of Galicia (Spain)

Patricia VALCÁRCEL FERNÁNDEZ

Associate Professor, Administrative Law, University of Vigo

***1. Introduction***

On a functional basis, contracting authorities possess a twofold public-private nature. As State prominent parts, mostly Administrations, they are public bodies, holding prerogatives and acting as Regulators to ensure that the contracting activity complies with public contracting laws and procedures. But by appealing to the market to purchase goods and services, those authorities are also economic operators and act as any firm. It is in this very concept of clients or customers of an economic activity that they are bound to fulfil the Competition law requirements.

The overlapping of Regulation and Antitrust law over a particular market usually poses the problem of choosing one or the other to tackle anticompetitive behaviours. This is a race for hooking the prey. Both are entitled to intervene, since they have among their objectives the protection of competition on sectorial markets, but operate at different levels (*ex ante/ex post*). Whereas the U.S. Supreme Court inclines toward the primacy of Regulation (*Trinko, Linkline*), the European Court of Justice defends the 'complementarity' of both disciplines.

Quite different is the case of the Spanish model, where the current Public Procurement law forsakes the contracting authorities to fight bid rigging and wipe colluders out of the procedure. This task is legally assigned to national and regional competition watchdogs.

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This chapter aims at proposing feasible means for contracting authorities to tackle collusion alongside the tender process. These means should contribute to avoid bid rigging or, if they fail, should help the Competition agency to prove the anti competitive behaviour. A breakthrough in this regard is the Directive on Public Procurement, since it entitles the awarding powers to expel those candidates with sound evidence of bid rigging before or during the contracting procedure. This formula seems to bring the solution back to Public Procurement, but favours errors Type I and Type II (false positives and negatives).

## ***2. Public Procurement as a Type of Regulation***

The loosest concept of Regulation, understood as the setting up of binding rules, undoubtedly encompasses public procurement. Squeezing the notion further, Regulation appears as the normative activity of designing the statutory standards, patterns and guidelines – ‘rules’ – which set the pace for certain economic sectors to operate on a legal basis. An array of public bodies, collectively named Regulators, is disposed by law to exert a complex of functions: setting, implementing, checking and supervising Regulation and punishing operators for their breaching.<sup>(2)</sup> From this viewpoint, public procurement is a regulated sector as well.

The full-march liberalization process that has shaken western European economies from the 80’s on gradually led to a more restrictive notion of Regulation, which became canonical thanks to EU Directives. The above process basically consisted of pushing public monopolies down and entrusting the so called ‘markets’ with full entitlement over a great deal of economic activities. These ones had either been born or quickly seized by the Administration, which kept them under public ownership. The management – but not the domain – would be handed over to single agencies, public or private. In the latter case, the transference would take place through public contracting procedures.

From that moment on, public procurement and Regulation differ. The former finds its own limit in a public body that acquires works, supplies or services from the awardee of a competitive procedure. The latter encompasses a large variety of activities and services whose ownership and management belong to market operators but whose acknowledged ‘general economic interest’ calls for submitting them to certain rules, carefully checked by the Regulator.

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(2) M. CAMPOS SÁNCHEZ-BORDONA, *La regulación como finalidad distinta al Derecho de la Competencia*, in J. Guillén Caramés (ed. by), *Derecho de la Competencia y regulación en la actividad de las Administraciones Públicas*, Civitas, 2011, 89.

Nevertheless, such differences don't mean that the contracting authority can be identified as a mere client of the contractor. That body has not only a buyer role. On the contrary, it also exercises a regulatory-like function, in the sense of arranging the object of the contract, for it to be linked with the public interest it embodies. Therefore, Regulation and public procurement are not perfect synonyms, since they do not share the very same features, functions and *raison d'être*. But they participate from a common seminal *substratum*, such as the next chart will show:

|                          | Features                            |   |
|--------------------------|-------------------------------------|---|
|                          | Regulator(3)                        | Contracting Authority   |
| <b>Independence</b>      | Full, regarding State and operators | <i>Public authorities, bodies dependent on them in different degrees.</i>   |
| <b>Internal autonomy</b> | Organizational and operative        | <i>Belonging to public sector</i>   |
| <b>External Autonomy</b> | Checking by Parliaments & Courts    | <i>State and judicial control</i>   |
| <b>Nature</b>            | Public entity (in general)          | <i>Varied (Public bodies, firms &amp; endowments participated by State)</i> |
| <b>Organization</b>      | Collegiate body (in general)        | <i>One-person (in general)</i>  |
| <b>Decisions</b>         | End of administrative intervention  | <i>End of administrative intervention</i>                                   |

| Functions  |  |
|--|--|
| Regulator(4)   | Contracting authority  |
| Supervising operators                                      | <i>Supervising contractors</i>   |
| Checking & sanctioning operators                           | <i>Checking &amp; sanctioning contractors</i>  |
| Drafting rules; advising authorities & courts              | – ----   |
| Regulation <i>ex ante</i> . Check & cut antitrust breaches | <i>Setting administrative &amp; technical standards. No concern on antitrust business.</i> |
| Solve conflicts between operators/ arbitration             | – -----  |
| Studies on better regulation                               | – -----  |
| Grant, revision & withdrawal of licenses                   | <i>Withdrawal of contracts</i>   |

(3) Source: Spanish Ministerio de la Presidencia, *Informe sobre la situación actual de los organismos reguladores y su posible reforma*, 2012, available at: [http://www.lamoncloa.gob.es/consejodeministros/referencias/\\_2012/refc20120120.htm](http://www.lamoncloa.gob.es/consejodeministros/referencias/_2012/refc20120120.htm).

(4) Spanish Ministerio de la Presidencia, *Informe sobre la situación actual de los organismos reguladores y su posible reforma*, cit.

Not every feature assigned by the *Report* to the Regulators has a pair in the contracting authorities' box. When their respective features look alike, the resemblance may be accounted for the identity of reason of both institutions due to a sort of 'convergence evolution' inside their respective niches. The key is, as mentioned above, that whilst the Regulator does not belong to the market where regulated firms operate, the contracting authority is one of the parties of the deal, but endowed with broad powers to protect public interests.

### 3. Applying Antitrust Law to Public Procurement

Antitrust law's crosswise nature has been tailor-made designed for it to sleuth in almost every economic sector, hustling up to punish the fault and repair the alleged damage, if possible. Therefore, no singularity of public procurement justifies its exemption from the antitrust surveillance. Neither that it operates through an administrative procedure, nor that the recipient and awardee of the goods, services or works is a public entity, very often an Administration.<sup>(5)</sup> Competition watchdogs are used to fining both bidders and contractors in cases of breaches of Competition law. After all, every bidder is a firm offering goods and services into the market. *Ergo*, they run the risk of committing any of the infringements quoted in Articles 101 and 102 EU.

*De iure* as well as *de facto*, contracting authorities are economic operators and firms, inasmuch as the provision of goods and services from the market is an economic activity. The interaction between antitrust and public procurement laws comes to a halt only when the organisations fulfil an exclusively social function, their activities are based on the principle of national solidarity and, lastly, they are non-profit-making, paying out statutory benefits that bear no direct relation to the level of contributions. That occurs in the case of organisations managing national health or social security systems. Only when those conditions are met are contracting bodies not considered economic operators, because the product or service purchased is not devoted to an economic activity, taken from the market. It is the well-known *FENIN* doctrine.<sup>(6)</sup>

The principle of speciality also explains why antitrust law finds its place on the field of public procurement. Contracting law's main goal is to define a compulsory path so that public bodies obtain the best product in the market

(5) Even though bid rigging is committed before the procedure starts, through the dealings carried out between presumably rival firms, its reasons and outcomes are undoubtedly linked to the tender process and to the implementation of the contract. It is within them that collusive bargains take effect and their effects spread up. Moreover, it is the contracting authority that first faces the economic damages derived from the overheated prices offered by the candidates.

(6) ECJ, 4 March 2003, *Federación Española de Empresas de Tecnología Sanitaria (FENIN) v. Commission*, T-319/99; ECJ, 11 July 2006, *Federación Española de Empresas de Tecnología Sanitaria (FENIN) v. Commission*, C-205/03 P.

– in terms of price and quality – to meet a public necessity. So, punishing misbehaviours is not embedded into its *DNA*. On the contrary, the essential duty of antitrust law is to punish certain firms' conduct which may damage consumers and bring about real or virtual breaches to the fair competition in the market.

As a matter of principle, the Competition law and authorities complex was not designed to foresee, or to avoid, candidates or awarders that commit the breaches described above.<sup>(7)</sup> This is a seminal barrier in itself. Competition watchdogs lack any strength to impede those infringements, by the reason that they act *ex post facto*. They do not operate within the contracting procedure, checking it from the inside. It does not matter that these features – a repressive goal and their distance from the procedure – have been decided by law. As a matter of fact, both prevent the watchdogs from waging war against antitrust practices *intra muros* (inside) the procedure, and from avoiding awards tainted by a previous collusion among the bidders. And it is not difficult to figure out that a successful bid rigging (unstopped before the award) will ruin the aim of any tender.

#### ***4. The Spanish Case. Fight Against Bid Rigging Channeled Towards Competition Law***

The primary reply of the Spanish Public Procurement model to bid rigging is quoted in the additional provision num. 23<sup>rd</sup> of the current public procurement law (Legislative Decree 3/2011, November, 14<sup>th</sup>, 2011). In spite of being placed within the core law on public contracts, this provision outsources the conflict, by calling upon all the public entities concerned with tenders to supply the national or regional Competition agencies with any evidence – even circumstantial – of bid rigging that they found within the procedure.<sup>(8)</sup>

Although contracting bodies may be assimilated to a *sui generis* regulator, the outsourcing laid down by additional provision num. 23<sup>rd</sup> effectively deprive them of a large portion of their regulatory powers: those formed by the function of guarantying 'antitrust competition' before and alongside the contract life (tender, award and implementation). The outcome is twofold. The Legislative

(7) Advocacy is an increasingly important task for Competition Authorities, but their remedial powers go beyond the power to change conduct and impose fines.

(8) Literally, the 23<sup>rd</sup> provision says (translation by the author): "*Contracting authorities, the State Consultancy Commission on Public Procurement and all the bodies able to decide the special appeal set out in Article 40, are bound to report to the Comisión Nacional de la Competencia all deeds they know while managing the contracting procedure, that may represent a breach of Antitrust law. In particular, they are bound to report any evidence of agreements, decisions of and concerted practices between the candidates which have as their object or effect the prevention, restriction or distortion of competition within the common market within the contracting procedure*".

Decree 3/2011 does set out some methods to shield competition among bidders during the procedure (*competition for the market*). But even though it was notorious that the candidates bargained and came to an agreement on the contract award before the procedure starts, the Legislative Decree did not set own rules for ensuring that, in that case, the bidders must abide by the antitrust rules (*competition in the market*).

Hence, the Legislative Decree puts the contracting bodies out of action in cases where bid rigging success shows that the contract awarding decision was plagued with type-I or type II errors (the colluders win). Such a paradox is almost inevitable although they are absolutely aware of the antitrust law breach. As an example, the Decision *Transporte Ayuntamiento de Las Palmas* adopted by the CNC (Spanish Competition Authority).<sup>(9)</sup>

The city council of Las Palmas started a procedure to award a contract to provide the local transportation service for sporting and educative activities. Once the offers were known, a bidder complained that three other rivals' proposals were exactly the same in terms of price per ticket, in more than nine hundred cases. Over the contracting process, successive reports acknowledged the strong evidence of collusion. Nevertheless, the procedure went on until the contract was awarded to the best rated candidate; indeed, to one whose bids were in question. A few days after the decision, the contracting authority decided *ex officio* to report the case to the Comisión Nacional de la Competencia (CNC).

As the example shows, both logic and reality have proved how useless is a Spanish-like model to confront collusion in public procurement. Bereft of other solutions, the ultimate answer offered by the Legislative Decree 3/2011 was the additional 23<sup>rd</sup> provision reference clause. Since antitrust agencies have been modelled to act after the breach has taken place, it is not an exaggeration to say that Spanish public procurement runs the risk of becoming fully cartelised sooner rather than later.

### ***5. Proposals to Combat Bid Rigging within the Procurement Procedure***

Several features of public procurement make bid rigging easy to anticipate but quite difficult to address through comprehensive solutions. For example, excessive transparency, which is almost endemic to most public contracts; permanent public services ensure the repetition of procedures at the same time for many years; requests for homogeneous products not affected by technological or normative changes; external support from the state or the European

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<sup>(9)</sup> Comisión Nacional de la Competencia (CNC), *Transporte Ayuntamiento de las Palmas*, 25 October 2012.

Union to finance the purchase, which guarantees continuity. These and other factors favour the stability of cartels and erode the incentives to compete. The diagnosis worsens in local markets, where the number of potential candidates is reduced. The same comes about as to certain specific markets dominated by a small group of operators, even oligopolies (energy).

Such anticompetitive proclivities combined with the lack of specific legal resources, suggest that the search for internal remedies should be all-inclusive and far-reaching. That is, remedies must involve the documents (contractual clauses) as well as the professionals of the contracting authority (organic clauses).

### 5.1. Contractual clauses to deter antitrust breaches in public procurement: general clauses and the non-collusion compromise

Broadly speaking, the specific administrative clauses of a contracting procedure contain two types of provisions: 1) those related to its management by the contracting authority; 2) those marking the requisites the candidates have to fulfil to take part in the procedure. These ones are the accurate tanks to store the above mentioned as 'contractual clauses', divided into the overall indicators of competition and the candidate's commitment not to join in collusive practices.

#### 5.1.1. Overall indicators of competition

For the specific administrative clauses that regulate the contract from the very beginning to its complete implementation, the chief issue to protect competition and avoid bid rigging is to attach to them a set of the most important antitrust rules and breaches. The attachment may consist either of a set of rules included within the administrative clauses, or of reference to a separate document, such as a Guide on public procurement and competition law issued by the Competition Authority.

This above solution, even general, is far from being naïve or useless. First, it is an educative factor for the bidders, who cannot credibly argue ignorance about the anticompetitive nature of their conducts. Second, it works as a reciprocal complement to the candidate's commitment, which will be studied below. Third, it is quite a direct way of promoting competition in public procurement, thanks to the easy dissemination provided by the contractor profile Internet site.

A subset of provisions useful to be collected in the contracting file is related to those phases of the contract more inclined to be infected by collusive agreements. For effectiveness, those provisions must necessarily be inserted in the specific administrative clauses.

Among the concrete provisions, of particular importance are those concerning the means of co-participation between two or more firms in the bidding process: Temporary business associations (joint ventures); reliance on the capacities of other entities to prove economic/financial standing or technical and professional ability; and, subcontracting. By their very nature, these three approaches tend to favour collusion, as they are instrumental to join together firms otherwise able to submit separate tenders, or as mechanisms to compensate those participants whose tenders are deliberately unsuitable.

Temporary business associations are an institutional danger of bid rigging since they have been legally conceived and promoted as a means of co-participation, which could disguise cases of collusion. This anticompetitive behaviour is almost sure to occur when (practically) all the bidders belong to the joint venture. In *Terapias Respiratorias Domiciliarias* (r504/01), the investigation unit of the Spanish Competition Authority rejected the argument that the joint venture incurred in breach of article 1 of the Spanish Competition Act (equivalent to Article 101 EU), because it was set up in conformance with all the legal requisites. Nevertheless, the final decision stated that the restrictive effects arise irrespective of the shape and object of the constitutive agreement when the joint firms enjoy sufficient market power and the number of potential rivals is minimum. Otherwise, the finding would reverse when the number of candidates external to the association ensures a sufficient margin of competition.

Relying on the capacities of other entities to prove economic/financial standing or technical and professional ability allows the bidder to obtain the support of other firms on the subjective conditions to bid required by the specific administrative clauses. The Directive builds this figure on the existence of an agreement between the candidate and the third firm about the contents and extension of the support. Whether the agreement is restricted to its core function, no antitrust concerns come out. But it may easily favour cross-collusion between the same firms in different contracting procedures, which would make it more difficult to identify any breach. Subcontracting works the same as reliance, but operates after the contract award. To lower the impact of both types of collusion, contracting authorities should accurately set the conditions and boundaries of the agreement (by rejecting the subcontracting of other bidders or identifying the subcontractors in the tender).

#### 5.1.2. Bidder's commitment not to incur in collusive practices

Unlike the tools discussed above, a written commitment not to collude is a tool directly addressed to any bidder in the very moment of his deciding whether and how to submit a tender for any procedure. Its way of operating is quite simple. The document storing the specific administrative clauses will

attach a standardized form stating, fairly and completely, that the signatory claims that the firm has not fallen and is not falling into collusion in the procedure. Of course, bidders will be allowed to submit their own forms, as long as the level of commitment is the same as that set forth in the standardized one.

The bidder's commitment pursues two main objectives: information about bid rigging and deterrence. The informative function operates within the contracting procedure, providing the candidate with a clear and understandable idea about how important is to meet Competition law and the sanctions for its breach. Information is especially important regarding contracting procedures in local or oligopolistic markets or in markets pervasively dominated by SME's. But the deterrent role of the commitment is undoubtedly the most important. It means that bidders do much more than reading several paragraphs on Competition law and public procurement to know about the rules; their signature is a statement of their ensuring legal behaviour, initially addressed to the contracting authority and to the other candidates. But it will also be very effective before the Competition agency to demonstrate the signer's guilt.

The deterrence function of the commitment can spiral totally out of the bidders' control when the Competition authority demonstrates that one or several candidates have rigged their tenders to predetermine the outcome of the procedure. In that case, the ordinary level of administrative sanction is triggered because of the breaching of antitrust law. But it is in the hands of both authorities to pave the way for the colluders to be criminal responsible, because of falsification of a private document within an administrative procedure (counterfeit). The Spanish Criminal Code punishes with imprisonment from six months to two years anyone who, to harm another person, alters a private document, in one of the ways set out for the counterfeit of public documents.

### 5.1.3. The placet of the General Court on the commitment: the PC-Ware judgement

Admissibility of the commitments is well recognized all over Europe and perhaps does not need judicial support. However, the General Court has admitted such a commitment, at least once, in the *PC-Ware* judgement.<sup>(10)</sup> The Court supported that solution in a smooth and perhaps unconscious way, since the case related to unfair competition (sales at a loss). However, there is no point to conceiving an opposite finding if the Court had to deal with a bid rigging issue. Mainly, because sales below certain price levels belong to the anticompetitive category of predatory prices.<sup>(11)</sup>

(10) General Tribunal Judgment (Second Chamber), 11 May 2010, *PC-Ware Information Technologies v. Commission*, T-121/10.

(11) ECJ, 2<sup>nd</sup> April 2009, *France Télécom v. Commission*, C- 202/07P.

The case started with an application from the firm PC-Ware for annulment of the Commission's decision of 11 January 2008 rejecting the tender submitted by the applicant in a public procurement procedure or, in the alternative, for compensation for the loss allegedly suffered by the applicant as a result of the Commission's conduct of awarding the contract to another rival whose bid was abnormally lower, tantamount to a sale at a loss.

The Financial Regulations, the framework for the Commission's procurement, regulate abnormally lower tenders, but not so sales at a loss. Nevertheless, the technical specifications related to the call for tenders referenced Belgian laws to complement the Community law, "where the Community law does not regulate the specific legal issue" (paragraph 7). Article 40 of the Belgian Law of 14 July 1991 on trade practices and consumer information and protection bans traders from offering a product for sale or selling a product at a loss (paragraph 9). Hence, the applicant argued that, since the Commission neither applied the Belgian law nor rejected the winning proposition, it infringed Article 55 of Directive 2004/18 and Articles 139(1) and 146(4) of the Financial Regulations (paragraph 46).

The General Court dismissed the application, noting that the appeal to Belgian laws was done by one of the technical specifications of the call for tenders at issue. As long as a technical specification does not constitute a procurement rule, it cannot set the subsidiary law (paragraphs 58-62).

What matters to us is paragraph 63, where the Court noted a general principle that

*"(...) in accordance with the principles of sound administration and solidarity as between the institutions of the European Union and the Member States, the Commission was required to ensure that the conditions laid down in the present invitation to tender did not induce potential tenderers to infringe the Belgian legislation likely to be applicable to the contract at issue in the present case (see, by analogy, Case T-139/99 AICS v Parliament, cited in paragraph 62 above, paragraph 41, and Case T-365/00 AICS v Parliament [2002] ECR II-2719, paragraph 63), as that question constitutes an assessment of facts (Case T-365/00 AICS v Parliament, paragraph 63)."*

The Commission could not ignore that the technical specifications demanded from every candidate the commitment of submitting no tender at a loss, for this was an unfair competition practice. But the obligation proposed by the Court was merely formal; the Commission will fulfil it by checking that the commitment has been attached to the tender. Therefore, when the specific administrative clauses requires the above mentioned commitment, what matters for the contracting authority is to check its very presence within the tender file; it is not obliged to a material evaluation.

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## 5.2. Organic clauses. Participation of experts on Competition Law to support the exclusion of bid riggers

Until now, we have suggested that introducing several provisions in the specific administrative clauses and/or the bidder profile, to set a compulsory commitment to be filled out by the candidates, is a serious contribution to avoid collusion, inasmuch as bidders cannot deny having been informed about the antitrust rules concerning public procurement; this will help Competition agencies prove the breach.

But that approach does not meet the aspirations of this chapter, which is intended to show that the (Spanish) public procurement system should be able *per se* to uncover as much as possible collusive behaviours and punish the perpetrators. All of that would mean that the intervention of Competition watchdogs is secondary, setting aside as far as possible the model set out by the additional provision num. 23<sup>rd</sup> of the public procurement law.

The attainment of this goal requires that two pre-conditions be satisfied. First, to find a rule within public procurement law allowing authorities to punish bid riggers. Second, to include experts on Competition law in the staff of the contracting body to ensure the technical accuracy of the penalty.

The first pre-condition is only half satisfied by Spanish law. Article 223 [f), g)] quotes two causes of resolution: the breach of essential contractual obligations, qualified as such in the specific administrative clauses or in the contract, and the infringement of those obligations specifically included in the contract. Article 223 considers “*to resolve*” as equivalent to put an end to the contract. This means that bid rigging does not work as a cause of exclusion of the bidders or candidates during the tender procedure. On the contrary, it may concern only the awardees of the contract. So, a collusion agreement bargained before the procedure and effective during its implementation would be punished only in case the offender is the contractor.

Even this solution requires the contracting body to use an extensive interpretative standard, because it suggests expelling the contractor not by virtue of an infringement related to the implementation of the contract, but concerning its tender. Spanish law allows the agency to declare the nullity of the contract in cases of intentional misconduct from one of the parties. There is no doubt that bid rigging is an obvious example of misbehaviour from bidders, which intentionally agree to invalidate the rivalry inherent to public procurement (2011 Law, article 31 related to Civil Code, Article 1269).

The intervention of experts on Competition during the procedure to award a public contract (second pre-condition) has not been foreseen in the Spanish procurement law. Article 320 entrusts the Mesa de Contratación (Bureau of procurement) with the competence to rate the tenders on the basis of a set of awarding criteria mentioned in Article 150.1 (price, quality, social and environmental clauses, etc...).

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Prohibition of collusion has not been quoted among those standards; and it is difficult for it to be included, since it is not a criterion directly linked to the contract object. Nor can the experts on antitrust law be part of the “Committee of Experts”, whose powers are limited to the assessment of the subjective awarding criteria in case they outweigh the automatically-rated ones (Article 150.2).

In spite of that, the fact is that the Spanish procurement system does not ban experts on Competition law from taking part in the procedure. The intervention can be channelled through the Bureau of procurement without straining the law interpretation: as advisors or as full members of the Bureau.

The law is very loose concerning the Bureau of procurement membership requisites. The only member that must also belong to the contracting authority is the Secretary. Both the Bureau’s financial controller and advisor in law will usually be counted among the staff of the authority; but it is not compulsory. The other members need only be appointed by the contracting body. Hence, this official can freely decide the degree of integration: looser, as advisors or more intense as full-fledge members.

In both cases, the experts have the right to express their opinions about any issue during the procedure concerning Competition law especially regarding those behaviours from the authority or from the candidates likely to breach articles 1 and 2 of the Spanish Competition law (Articles 101 and 102 EU). Their opinions must be attached to the minutes of the Bureau; no matter they are in accordance or disagreement with that of the other members.

The *auctoritas* of the experts will be specially challenged when the differences arise out of a case of suspected collusion. It is presumable that the contracting authority will not dare make a decision against the opinion of the experts on Competition law, for fear of been charged with administrative or criminal responsibility. The obvious difference between the role of the experts as full members rather than advisors of the Bureau is that in the first case they add a voting right to their advice.

### ***6. The Directive 2014/24/EU on Public Procurement: Contracting Authorities Are Prompted to Take the Leading Role Against Bid Rigging***

Even though the 2004 Directives lacked any rule to fight bid rigging and to shield competition in the market on public procurement, the Directive 2014/24/EU on Public Procurement (“the Directive”) makes a valuable attempt.<sup>(12)</sup> It goes so

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(12) Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC.

far as to turn contracting authorities into real Competition agencies regarding their own procedures. For doing so, the Directive admits the non-collusion commitment of the participants and empowers the authorities to expel from the tender process any bidder in case of strong evidence of their participating in a bid-rigging scheme regarding the ongoing procedure.

As sufficient evidence of his willingness not to participate in several misbehaviours, contracting authorities shall accept a commitment from the candidate only in the absence of an administrative or judicial certificate. The commitment will take the form of a declaration under oath or, in Member States where there is no provision for declarations under oath, by a solemn declaration made by the person concerned before a competent judicial or administrative authority, a notary or a competent professional or trade body, in the country of origin or in the country where the economic operator is established [Article 60.2.(a), (b)].

Article 60.2 seems very useful as a means to commit candidates to avoid collusion. However, it does not mention collusive affairs among its objects. Article 60.2 is applicable to conducts quoted in Article 57.4 (b), whilst bid rigging is mentioned in the paragraph (d). Nevertheless, the very nature of the Directive does not ban but favours the transposing law to adopt the same solution for collusion, given the conceptual connexion between bid rigging and the behaviours named in letter (b).

The removal of riggers from the contractual race has been settled on Article 57.5 (2<sup>nd</sup> paragraph) of the Directive: "*Contracting authorities shall at any moment during the procedure exclude an economic operator where it turns out that the economic operator in question is, in view of acts committed or omitted either before or during the procedure, in one of the situations referred to in paragraphs 1 and 2*".(13)

Article 57.5 (2<sup>nd</sup> paragraph) raises a large number of issues. The authorisation to exclude is given to the contracting body on a broad basis, for the enabling practices may be previous or contemporary to the procedure. The article does not explain whether the bargains finalized before the start of the current procedure must be necessarily linked to it or, otherwise, can relate to past contracts as well.

(13) Article 57.4 (d) allows the contracting authority to exclude (*per se* or under request by a Member State) from participation in a procurement procedure any economic operator (...) (d) "*where the contracting authority sufficiently plausible indications to conclude that the economic operator has entered into agreements with other economic operators aimed at distorting competition*". Differences between the wording of Article 57.5 2<sup>nd</sup> paragraph and Article 57.4 (d) seem to mean that the former relates to a candidate's exclusion *during* the ongoing procedure and the latter to the prohibition for a firm to participate in *future* tenders by reason of previous fines imposed on it by a Competition Authority, a Court or even by a prior implementation of Article 57.4 (d).

The useful effect of the Directive would be thwarted if the second option does not prevail. First, Article 57.5 (2<sup>nd</sup> paragraph) is based on punishing collusion, which is more dangerous whether habitual or repeated. Second, this article does not set the current procedure as the temporary boundary to application. Third, the *raison d'être* for specifying “*before or during procedure*” is a warning that collusive agreements can arise once the procedure gets going, because the candidates know who the rivals are and can calculate each bidder's chances to obtain the price. Fourth, it may be easier for the contracting authority to prove past collusions, since they have been acknowledged by administrative or judicial decisions. Fifth, this solution avoids the risk that a negligent or ignorant authority may allow a candidate to participate despite a decision or judgement declaring a past collusion. However, the limit to dig into past cases must be the prescribed time laid down in the national Competition law.

It looks obvious that the main matter of contention for the authority to lawfully decide the exclusion is the degree of conclusiveness achieved by the evidences of bid ridding on the part of the candidates. Committing an error type-I is so easy that a sort of proportionality test should be applied to weigh up both options. Only when the evidence of a collusive behaviour is indisputable and outweighs the chance of unfair expulsion may the contracting authority run the risk of excluding the bidder. Moreover, the decision must be strictly based on the breach of Article 101 EU and take as benchmarks the suite of guidelines released by national and international organisations to detect and fight bid rigging.<sup>(14)</sup>

Article 57.5 (2<sup>nd</sup> paragraph) appears to be a risky but efficient solution to fight collusion in public procurement. Its principal value consists of posing a solution within the tender process by empowering the contracting authority. It also blocks a possible award benefiting the offender, who will be expelled from the current procedure and likely vetoed for future ones, in terms of Article 57.4 (d). However, the actual step forward is to pass from nothing to something, even if imperfect. The scheme proposed is highly dysfunctional and favours both errors type I and II. First, contracting authorities usually lack expertise on Antitrust law; so they will need careful assistance from lawyers or, better, from Competition watchdogs, i.e. exercising advocacy. Second, strong but not undisputable evidences of collusion put forward during the course of the procedure will make the contracting body hesitate, either to call it off up to the solution of the competition setback or to leave it to the end, reporting then the fault to the Competition authority.

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(14) Especially, the OECD documents: *Guidelines* (2009), *Roundtable on collusion and corruption in public procurement* (2010) and *Recommendations* (2012). Moreover, several national Competition authorities have published some material on their own, as a means of advocacy, such as Canada, India, New Zealand, Spain, U.K. and the US.

In conclusion, what the Directive is going to achieve is to pass from a self-crippled Regulator (the contracting authority), helpless before bid rigging, to one capable of winning the battle but potentially loaded with errors of type I and type II.

## 7. Conclusions

Clashes between Regulation and Antitrust law and their respective agencies' roles are pervasive nowadays. Despite the large number of normative texts, legislators gave up ensuring a peaceful cohabitation and left to the Courts the task of defining the operative relationships between both disciplines. Two main schemes have prevailed so far. The US Supreme Court has affirmed the pre-eminence of Regulation and banned antitrust law to meddle when the former must be applied. Conversely, the European Court of Justice has drawn a two-step model, which starts by an statutory *ex ante* control by Regulators, followed by an *ex post* exam from Competition Authorities in light of hypothetical infringements of Antitrust law.

More censurable is the lack of an appropriate answer when public procurement intertwines with Competition law. Neither the American nor the European ways above quoted may consistently rule this situation, since contracting authorities are not full-fledged regulators: they do not enjoy any faculty to check possible antitrust breaches committed in tenders, either on their own or as a first step. That is the reason why Spanish-type procurement systems have relinquished the task of prosecuting bid rigging in favour of Competition agencies, as additional provision num. 23<sup>rd</sup> of the Spanish public procurement law sets out.

The Spanish scheme against bid rigging has been shown to be ill planned. Contracting laws have put the task solely into the hands of Competition watchdogs. Two important obstacles stifle the capacities of these agencies to successfully fight collusion. First, the *ex post*-operating system, a typical feature of every antitrust sanctioning procedure, actually impedes agencies from putting an end to a plot in the course of the contracting course. Second, the agencies' historical lack of consciousness that public procurement is an economic sector the same as any other sets a strategic safe harbor for anticompetitive practices. The paradox is that, even though the second factor is quickly changing, the first one means that antitrust law applied to public procurement is able only to fine but not to stop bid rigging.

This study has attempted to show how ineffectively this device is working and how other ways must be tested. Fully aware of it, the Directive has thrown in its lot to achieve a solution that settles bid rigging within the procedure, before the awarding of the contract. The Directive breaks the previous model by means of appointing contracting authorities as 'vigilantes' against the

collusion cases brought about in their own contracting procedures. It gives them the authority to expel from the procedure in progress any candidate tainted with evidence of collusion. The internal identification of bid rigging does not divest Competition watchdogs of *ex post* checks.

The twist must be praised because it seeks to define an effective procurement law defense against bid rigging, roughly built on the European Court of Justice formula against antitrust concerns on regulated matters. However, the Directive runs the risk of overloading the contracting authorities without providing them with adequate weapons. Internal laws of transposition shall have to establish such weapons, in terms of staff, management and operational systems. Otherwise, the only way ahead will consist of replacing self-crippled contracting authorities by others whose decisions will be plagued with errors of type I and type II.

Regardless of the effectiveness of this or other answers, what must be dealt with is the compatibility of the concept of competition between antitrust and public procurement laws. The word “competition” flames in both banners, but its different meanings emerge in public procurement provisions which in implementation, may be unleashed in antitrust law infringements.

An example is found in the *European Code of best practices facilitating access by SMEs to public procurement contracts* [SEC(2008) 2193]. This Commission staff’s working document argues that fostering the involvement of SMEs in public purchasing will result in higher competition for public contracts, leading to better value for money for contracting authorities. It puts forth eight ideas to promote SMEs’ participation in contracting procedures. The first one, titled “overcoming difficulties relating to the size of the contracts” is parcelled out in five categories: subdivision of contracts into lots; possibility for economic operators to group together and rely on the combined economic and financial standing and technical ability; conclusion of framework agreements with several economic operators; and subcontracting. From the perspective of procurement law, it is obvious that those mechanisms make the contract smaller and so favour the entry of SMEs. But it is also evident that they all are direct or indirect formulas of co-participation which facilitate cartels to be born among bidders. Therefore, the same tool used to intensify competition for public procurement own goals may thwart competition on an antitrust basis, raising the question of the contracting authorities’ responsibility for the commission of antitrust breaches.

## CHAPTER 4

### Debarment in public procurement: rationales and realization

BY

Erling HJELMENG

Professor at the Department for Private Law, University of Oslo

Tina SØREIDE

Senior Researcher and Economist, faculty of Law,  
University of Bergen

#### *1. Introduction*

As a consequence of being found guilty in corruption, fraud and some other offences, firms and individuals can be debarred from participating in future public tenders. Such consequences will not only reduce governments' risk of entering into contracts with corrupt or in other ways dishonest suppliers, but may also have a preventive impact on players' propensity to be involved in certain offences in the first place. While debarment has gained significant traction in the last decade, particularly as a device in the fight against corruption, the rules differ across jurisdictions and international organizations.<sup>(1)</sup> There is broad variation in the specific grounds for debarment, for instance. The World Bank debars suppliers found guilty in collusion, but this is not among the offences listed in the EU legislation. And, while some policy makers

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(1) For introductions to such rules, see among others E. PISELLI, *The scope for excluding providers who have committed criminal offences under the E.U. Procurement Directives*, in *PPLR*, 2000, 267-286; S. SCHOONER, *The paper tiger stirs: rethinking suspension and debarment*, in *PPLR*, 2004, 211-217; S. WILLIAMS, *The mandatory exclusion for corruption in the new EC Procurement Directives*, in *E. L. Rev.*, 2006, 711; T. M. ARNÁIZ, *Grounds for Exclusion in Public Procurement: Measures in the Fight Against Corruption in European Union*, in *International Public Procurement Proceedings*, 2006, 21-23; T. M. ARNÁIZ, *EU Directives as Anticorruption Measures: Excluding Corruption-Convicted Tenderers from Public Procurement Contracts*, in K. V. Thai (ed. by) *International Handbook of Public Procurement*, 2009, London, 105-130; S. WILLIAMS, *Coordinating public procurement to support EU objectives – a first step?* S. Arrowsmith – P. Kunzlik (eds.), *Social and Environmental Policies in EC Procurement Law*, Cambridge, 2009, section 2.4.3 and 4.4.6. Regarding international organizations, see N. SEILER – J. MADIR, *Fight against corruption: sanctions regimes of multilateral development banks*, in *Journal of International Economic Law*, 2012, 5-28; and P. H. DUBOIS – A. E. NOWLAN, *Global administrative law and the legitimacy of sanctions regimes in international law*, in S. Rose-Ackerman – P. Carrington: *Anti-Corruption Policy: Can International Actors Play a Constructive Role?*, 2013, Carolina Academic Press, Durham NC, 201-214.

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prefer lists of firms to be mandatorily debarred, others consider the question of debarment on a case-to-case basis. Without a solid theoretical underpinning for these rules, there seems to be uncertainty in policy environments about what optimal solutions should look like: who should be debarred, and under what circumstances? For how long should they be debarred, and when should it be possible to deviate from the rules?

Such questions have been the motivation for this chapter, and we will address several of them in an attempt to develop principles for the length of debarment and to describe how debarment should depend on firms' efforts to become more trustworthy, so-called *self-cleaning*. EU law, and more particularly the recently revised Public Procurement Directive (hereinafter PPD),(2) will remain the legal frame of reference, even though several of our points are more generally relevant. Section 3 addresses the consistency between the purpose of the rules and the mechanisms at play. Section 4 discusses criteria for efficient debarment rules with a specific focus on the length of debarment and self-cleaning. The space for policy implications under the PPD is described in Section 5. In particular, we explore the opportunities for framing a coherent system under the new Directive.

## 2. EU procurement rules and self-cleaning

The new EU procurement directive of 2014 is, as its predecessor, based on a combination of mandatory and facultative debarment. The relevant parts of the provision on mandatory debarment reads (Article 57(1) and (3), footnotes omitted):

*“Contracting authorities shall exclude an economic operator from participation in a procurement procedure where they have established, by verifying in accordance with Articles 59, 60 and 61, or are otherwise aware that that economic operator has been the subject of a conviction by final judgment for one of the following reasons:*

*(a) participation in a criminal organisation, as defined in Article 2 of Council Framework Decision 2008/841/JHA;*

*(b) corruption, as defined in Article 3 of the Convention on the fight against corruption involving officials of the European Communities or officials of Member States of the European Union (33) and Article 2(1) of Council Framework Decision 2003/568/JHA as well as corruption as defined in the national law of the contracting authority or the economic operator;*

*(c) fraud within the meaning of Article 1 of the Convention on the protection of the European Communities' financial interests;*

(2) Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC.

*(d) terrorist offences or offences linked to terrorist activities, as defined in Articles 1 and 3 of Council Framework Decision 2002/475/JHA respectively, or inciting or aiding or abetting or attempting to commit an offence, as referred to in Article 4 of that Framework Decision;*

*(e) money laundering or terrorist financing, as defined in Article 1 of Directive 2005/60/EC of the European Parliament and of the Council;*

*(f) child labour and other forms of trafficking in human beings as defined in Article 2 of Directive 2011/36/EU of the European Parliament and of the Council.*

*The obligation to exclude an economic operator shall also apply where the person convicted by final judgment is a member of the administrative, management or supervisory body of that economic operator or has powers of representation, decision or control therein.*

*(...)*

*Member States may provide for a derogation from the mandatory exclusion provided for in paragraphs 1 and 2, on an exceptional basis, for overriding reasons relating to the public interest such as public health or protection of the environment.”*

In contrast to the old public procurement directive (2004/18) the issue of self-cleaning is now explicitly addressed in the directive. Article 57(6) and (7) reads:

*“Any economic operator that is in one of the situations referred to in paragraphs 1 and 4 may provide evidence to the effect that measures taken by the economic operator are sufficient to demonstrate its reliability despite the existence of a relevant ground for exclusion. If such evidence is considered as sufficient, the economic operator concerned shall not be excluded from the procurement procedure.*

*For this purpose, the economic operator shall prove that it has paid or undertaken to pay compensation in respect of any damage caused by the criminal offence or misconduct, clarified the facts and circumstances in a comprehensive manner by actively collaborating with the investigating authorities and taken concrete technical, organisational and personnel measures that are appropriate to prevent further criminal offences or misconduct.*

*The measures taken by the economic operators shall be evaluated taking into account the gravity and particular circumstances of the criminal offence or misconduct. Where the measures are considered to be insufficient, the economic operator shall receive a statement of the reasons for that decision.*

*An economic operator which has been excluded by final judgment from participating in procurement or concession award procedures shall not be entitled to make use of the possibility provided for under this paragraph during the period of exclusion resulting from that judgment in the Member States where the judgment is effective.*

*By law, regulation or administrative provision and having regard to Union law, Member States shall specify the implementing conditions for this Article. They shall, in particular, determine the maximum period of exclusion if no measures as specified in paragraph 6 are taken by the economic operator to demonstrate its*

*reliability. Where the period of exclusion has not been set by final judgment, that period shall not exceed five years from the date of the conviction by final judgment in the cases referred to in paragraph 1.”*

The PPD thus implies: (1) an obligation to take relevant self-cleaning measures into consideration, and (2) an obligation to establish rules governing the implementation at the national level. In this respect, a considerable degree of flexibility is conferred upon the Member States.

However, whatever national solutions are chosen by the Member States, they have to be consistent with the basic principles of EU-law, as underlined in the Directive’s Preamble par. 1:

*“The award of public contracts by or on behalf of Member States’ authorities has to comply with the principles of the Treaty on the Functioning of the European Union (TFEU), and in particular the free movement of goods, freedom of establishment and the freedom to provide services, as well as the principles deriving therefrom, such as equal treatment, non-discrimination, mutual recognition, proportionality and transparency.”*

These general principles apply to Member States’ implementation of EU-legislation,<sup>(3)</sup> and clearly, they will influence the implementation of debarment rules. The *principle of equal treatment*, for instance, limits a government’s opportunity to deviate from the rules on an ad hoc basis, whereas the principles of freedom of movement of goods and freedom to provide services, respectively, hinder possible inclinations to debar firms on an arbitrary or discretionary basis. The *principle of proportionality* restricts the length of debarment in terms of protecting the rights of individuals, owners and firms, and averts reactions that are “harsher” than they “need” to be, given the purpose of these specific rules. Implicitly, a supplier who has made convincing efforts in becoming trustworthy, for example by introducing control and compliance systems, reorganized and replaced management, or reconsidered its institutional work ethics and visions, should be considered differently than suppliers who have failed to take such steps.

The principle of proportionality might actually have been the one that motivated, if not compelled, the inclusion of self-cleaning principles. The explanatory memorandum explains the need for such regulation as follows:

*“Allowance should, however, be made for the possibility that economic operators may adopt compliance measures aimed at remedying the consequences of any criminal offences or misconduct and at effectively preventing further occurrences of the misbehaviour. These measures may consist in particular in personnel and organisation measures such as the severance of all links with persons or organisations involved in*

(3) See for instance ECJ, *Hansen & Son*, Case C-326/88, ECR I-2911, par. 17; ECJ, *Messner*, Case C-265/88, ECR I-4209, par. 11 and 14; ECJ, *Karlsson*, Case C-292/97, ECR I-2737, par. 37 and ECJ, *Baumbast*, Case C-413/99, ECR I-7091, par. 91 and 93. See further A. DASHWOOD – M. DOUGAN – B. RODGER – E. SPAVENTA – D. WYATT, *Wyatt and Dashwood’s European Union Law*, 2011, Hart Publishing, 327-28.

*the misbehaviour, appropriate staff reorganisation measures, the implementation of reporting and control systems, the creation of an internal audit structure to monitor compliance and the adoption of internal liability and compensation rules. Where such measures offer sufficient guarantees, the economic operator in question should no longer be excluded on these grounds. Economic operators should have the possibility to request that contracting authorities examine the compliance measures taken with a view to possible admission to the procurement procedure.”*<sup>(4)</sup>

The PPD lists the following four relevant and mandatory actions for self-cleaning to be sufficient for exempting a supplier from debarment:<sup>(5)</sup>

- Collaborate with investigators and provide information about the offence
- Offer compensation for damage caused
- Remove employees from the given area of responsibility
- Internal organizational and administrative measures to prevent such offences in the future

Although these actions must be read as minimum conditions for exemption, it is far from clear how well they serve to renew trust in a convicted supplier – which is the ultimate purpose of the debarment (i.e., citizens must be able to trust public procurement). Those who are to judge whether the self-cleaning is ‘good enough’ will have to consider a range of aspects, including whether the actions are sufficiently comprehensive and credible; whether the efforts should lead to full exemption or a reduction in the debarment period; and whether the graveness of the committed offence should matter in the judgment. These questions are hardly regulated at the national level in any of the Member States and are frequently left to the individual procurement official to decide. Under the current legislation and typical enforcement, there are few reasons to expect that these considerations will be made in an unbiased and predictable way, and the intended trust-generating effects of the debarment rules are far from guaranteed. Principled guidelines on how to nuance these reactions against convicted suppliers should follow logically from the fundamental purpose of not only debarment but also public procurement rules.

### ***3. Purpose and principles***

Although debarment from public tenders may have severe consequences for firms and individuals, sometimes even more severe than the sentence placed on them in courts, the reaction is not intended to be a form of formal

<sup>(4)</sup> EU Commission, COM(2011) 896 final/2011/0438 (COD), 20 December 2011.

<sup>(5)</sup> Seemingly inspired by the solutions chosen in Austria, see A. REIDLINGER – S. DENK – H. STEINBACH, *Self-cleaning under National Jurisdictions of EU Member States – Austria*, in H. Pünder – H.-J. Priëß – S. Arrowsmith (eds. by), *Self-Cleaning in Public Procurement Law*, Carl Heymanns Verlag, 2009, 33-50.

punishment.(6) The purpose of these rules is solely the protection of state finances and government legitimacy.(7)

Citizens have the right to be confident that the state enters into contracts only with trustworthy entities and never allocates state revenues for criminal purposes. Since public institutions act on behalf of society, however, they also have to respect procurement rules introduced to secure the best price-quality combination of the goods and services acquired, and thus secure value for taxpayers' money. These different goals will easily come in conflict.(8) A national, central government, on one hand, and the representatives for the many procurement entities across a country, on the other hand, may have different views on what is more important and how the different principles and rules should apply for different procurement situations. The current directive implies debarment upon certain criteria but encourages each procurement agent to consider a contractor's trustworthiness. For the individual procurement officials, however, the debarment rules will easily come in conflict with their right to select what they consider to be the best supplier. Undeniably, debarment reduces the number of suppliers available and will sometimes force procuring entities to buy at higher prices or lower quality than what they would otherwise select, or from a supplier whose technology is unknown. Quite clearly, there are situations where debarment decreases the 'value for money' in public procurement. These potentially negative consequences of debarment can only be defended by the potential costs of buying from an untrustworthy contractor and the materialization of longer term benefits.

In a longer perspective, it is easier to see how debarment is an investment needed to secure trust in government procurement. With the exclusion of dishonest suppliers, the market is supposedly reduced to trustworthy players, and it will be more difficult for dishonest players to survive in the market for

(6) According to J. TILLIPMAN, *The Congressional War on Contractors*, in *George Washington International Law Review*, 2013, 45:235-250, the purpose of these rules are often misunderstood and she refers to "many legislators desire to transform debarment into a tool of punishment by banishing contractors from the procurement system without regard to contractor due process rights and with little consideration of whether such action is needed or fair" (p. 235; with reference to S. Shaw, *Don't Go Overboard Banning Military Contractors*, Reuters (Aug. 8, 2012). See also the observations made by S. ARROWSMITH – H.-J. PRIEB – P. FRITON, *Self-Cleaning – An Emerging Concept in EC Public Procurement Law?*, in H. Pünder – H.-J. Prieb – S. Arrowsmith (eds. by) *Self-Cleaning in Public Procurement Law*, Carl Heymanns Verlag, 2009, 1-31, 24-27, also printed in *PPLR*, 2009, 257.

(7) ECJ, 9 February 2006, *La Cascina Soc. coop. arl and Zileh Srl v Ministero della Difesa et al.*, in joined Cases C-226/04 and C-228/04, ECR I-1347, the ECJ points to "professional honesty, solvency and reliability" and overriding values underlying the corresponding principles in the former Directive 92/50 (par. 21). Along the same lines, ECJ, 13 December 2012, *Forposta SA and ABC Direct Contact sp. z o.o. v. Poczta Polska SA*, in Case C-465/11, NYR. par. 27, the Court says that "the concept of 'professional misconduct' covers all wrongful conduct which has an impact on the professional credibility of the operator at issue".

(8) These conflicting goals are discussed by R. MAJTAN, *The Self-Cleaning Dilemma: Reconciling Competing Objectives of Procurement Processes*, in *George Washington International Law Review*, 2013, 46(2): 291-347. He calls for more flexible debarment regimes with an opportunity for combining shorter debarment periods with convincing self-cleaning and more frequent use of restitution.

public contracts. The cost of crime increases significantly for those involved and debarment may thus have preventive impacts. As suppliers' integrity increases, fair competition is better ensured, and in the end, the available price-quality combinations in public tenders will improve *as a result of* the debarment rules. Consequently, the short term disadvantages for procurement entities may be compensated for in the longer run.

Such an outcome depends on the rules and how they are practiced. For many procurement officials it will be tempting to make exemptions, as mentioned, but the debarment rules are not supposed to apply only in situations where the convicted suppliers are easy to replace. They cannot apply only to suppliers in markets where alternatives are available – or to those who sell goods or services of inferior quality. Given the fact that market dominance might be the result of corruption or cartel behaviour over time, we may want to avoid exemption from debarment because of a contractor's market position.

Moreover, since every deviation from the rules makes them less predictable, a widespread use of exemptions implies that it will take longer for the listed (long term) benefits to materialize and make up for weakened competition. Given these different perspectives, what are the intuitive criteria for the debarment system to function efficiently in terms of securing trust in government procurement, integrity in the markets, and better price-quality combinations over time?

#### ***4. Criteria for efficient debarment and self-cleaning***

Whether the longer term benefits associated with higher integrity in public procurement markets actually materialize as a result of debarment depends on how the rules are detailed and enforced at the national level. The most obvious condition about predictability, that suppliers actually expect the rules to be applied, will possibly be the most difficult to meet.

##### **4.1. External decision**

Despite prospective longer term benefits, there are many reasons for procurement officials to deviate from the debarment rules. The supplier supposed to be debarred may for instance deliver unique products or services of high quality, for instance, and might be preferred regardless of the offences committed by employees or a branch of its organization. The conclusion might be similar if the supplier is an important employer in the local community. Under other circumstances, there might be a willingness to debar the given supplier but it might prove difficult in practice if, for instance, the supplier has substantial market dominance and is the only one able to deliver the goods or services within a reasonable price frame. Undeniably, there is a risk that procurement entities will prefer

more exemptions than what is optimal given the desired market consequences of the rules on debarment. At the local or institutional level, the entities are likely to focus primarily on their procurement needs given their budget constraints, and to be less concerned about how the rules work for society at large over time. This is not because they don't see the trade-off between short run costs and long term benefits of debarment, but rather because of their mandated focus on their institutional needs; finding alternative suppliers may simply become too expensive or politically costly, as mentioned above. For these reasons, the question of whether self-cleaning is "good enough", or whether deviation from the mandatory debarment can be justified, should not be up to the individual procurement agency to decide. The procurement official should describe the need for exemption or for accepting self-cleaning, but the decision should be made elsewhere – by a separate unit or centrally.

#### 4.2. The length of the debarment period

While predictable enforcement is a necessary condition for debarment to produce longer term integrity effects in the market, it is not necessarily *sufficient* for meeting the objective of renewed trust in public procurement.

Debarment is a serious reaction, and this alone is likely to be seen as a signal of the requirement for absolute integrity. At the same time, it is not necessarily convincing that 2-4 years of debarment from a given market is what it takes for a convicted player to become an honest supplier. Why should we trust the management simply because the firm has been kept out in the cold for a while? And if so, for how long should it be kept out to become trustworthy: two, four or five years?

In line with the law and economics of sentencing, it makes sense to let the reaction increase proportionately with the economic benefit of the committed offence, secondarily, with the severity of the acts. Even if debarment is not a form of punishment, the principle seems right, also in this context, if we believe that the more serious offence should imply a longer wait in order to be perceived as honest enough to participate in public tenders. In contrast, it is difficult to defend a system where the debarment period is fixed, regardless of the crime committed, and therefore, the most intuitive option is some proportionality between the grounds for untrustworthiness and the efforts required to regain trustworthiness. Thus, the debarment period could last longer the more the supplier has benefitted from the crime if this is an indicator of untrustworthiness, and if so, more efforts should be invested in self-cleaning to gain reacceptance in public tenders.

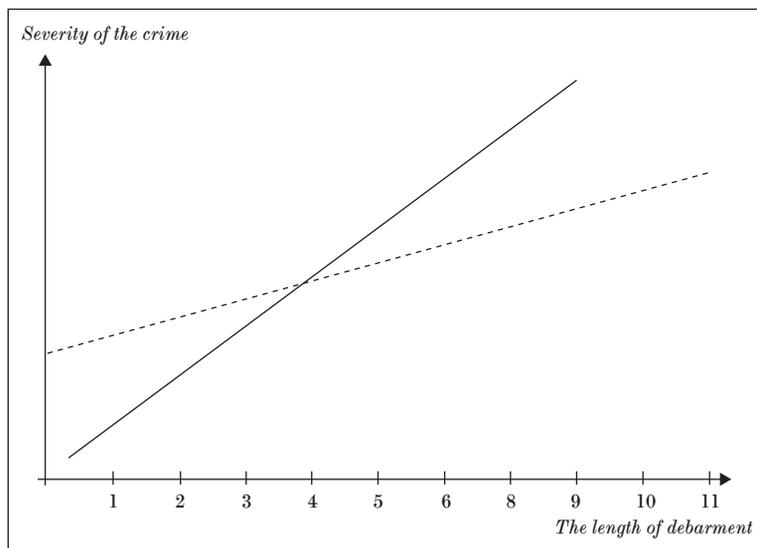
However, even if such proportionality makes sense, the debarment itself will not necessarily imply that the convicted supplier or the government that procures goods and services from it can be trusted. Hence, if the goal is not only to react and ensure a certain preventive effect, but actually to be able to start trusting convicted players, the criteria for an efficient system must

include something that provides grounds for believing that the supplier has actually altered its business strategies. There has to be an element of self-cleaning for the debarment period to end.

### 4.3. Self-cleaning and the debarment period

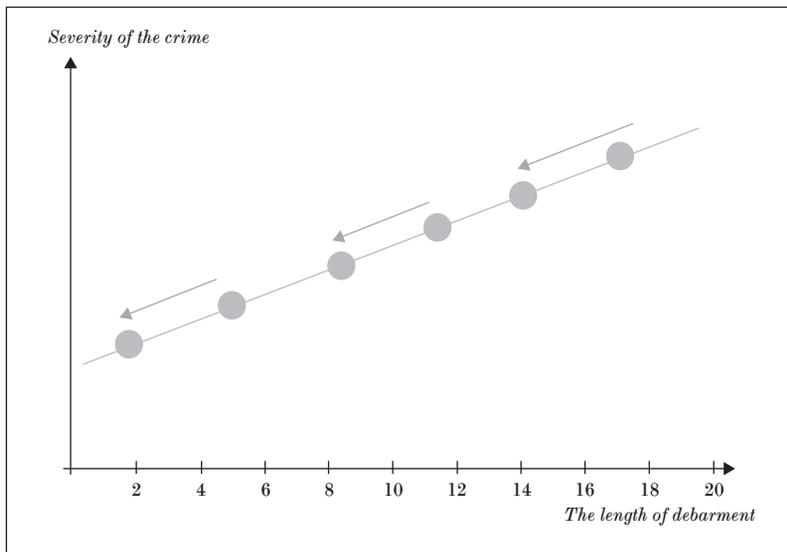
For the reasons listed above, a principle for calculating the debarment period should promote (i) some intuitive consistency between the debarment period and the convicted suppliers' trustworthiness, possibly judging untrustworthiness based upon the contractor's benefit from the offence or the graveness of the act; (ii) a reason to expect higher integrity in the debarred player's business strategy; and (iii) a chance to administer a predictable system where it is not too easy to make exemptions. If these objectives are met, the debarment will also serve its purpose of keeping dishonest contractors at a distance, preventing dishonest behaviour and ensuring trust in government spending. In other words, the debarment period should depend on the committed offence and the credibility of self-cleaning efforts, while at the same time, the arrangement should be manageable from an administrative perspective – and not a façade which can easily be manipulated.

So as to contribute to the discussion of what such a principle may look like, we have illustrated in Figure 1 a curve showing a linear relationship between the crime committed (vertical axis) and the debarment period (horizontal axis). Two curves are included to show the importance of the curve's grade. The steeper the curve, the more the debarment period is commensurate with the seriousness of the crime committed.



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The importance of self-cleaning is illustrated in Figure 2. If credible self-cleaning reduces the debarment period, the whole debarment arrangement not only serves to keep out dishonest players, but in fact incentivizes change towards more honest business strategies. Such an arrangement is not only more reliable in terms of encouraging suppliers to become trustworthy, it also reduces the short-term cost of leaving out convicted players, and accelerates the process towards obtaining the benefits that have motivated the debarment rules.



What Figure 2 illustrates is how a supplier can “climb down the debarment period-curve” by carrying out credible self-cleaning initiatives. If there is no such option to reduce the debarment period through self-cleaning acts, we fail to exploit the opportunity to encourage improved business behaviour. If we want to strongly incentivize compliance, we can let the initial debarment period be very long, for instance up to 10 years depending on the crime committed, and let the debarred firm “climb down” a steep curve as it carries out convincing self-cleaning initiatives. The shorter the initial debarment period and the lower the slope of the curve, the weaker are the incentives to improve.

Debarment rules with “strong incentives” could possibly be considered rigid and strict by some stakeholders since it basically means that a government *forces* convicted suppliers to change. Such an approach should be totally acceptable, however, if it serves both to promote business integrity and the

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price-quality combinations in government spending. Besides, it “forces” only those who want to stay in the market for public procurement, on the principle that governments should demand integrity and collaborate only with trustworthy partners. However, the reasonableness and efficiency of the system will depend on how the criteria for self-cleaning are specified.

#### 4.4. The self-cleaning initiatives

For suppliers to actually be found trustworthy, the self-cleaning initiatives have to be sufficiently credible and assessable for compliance monitoring. In line with the arguments above, the initiatives should be more profound, the larger and less trustworthy the contractor, as perhaps reflected in the gains obtained from the committed crime or the consequences of the acts – as illustrated in Figure 2. The initiatives listed on page 4 – collaboration with investigators, damage compensated, employees repositioned, and administrative reform – could be specified and graded for the severity of the crime. For example, for the relatively minor acts of crime (near the origin of the coordinates) it might be sufficient for the supplier to introduce codes of conduct, improved internal compliance systems, whistle-blower channels and training for employees. When it comes to more serious offences, from which the firms have profited substantially, the self-cleaning initiatives might also have to involve external actors who monitor the firms’ internal and external operations. For the gravest crimes (in the upper right corner of Figure 2), the firm’s owners may have to replace the whole management on top of other initiatives for the supplier to become sufficiently trustworthy for participation in public tenders.

These suggestions are merely examples to illustrate the argument. The bullets on the Figure 2 curve can loosely represent different categories of initiatives required for self-cleaning to be found satisfactory. We will not attempt to specify these criteria; the point is simply that the criteria for self-cleaning *should be* specified and graded for the severity of the committed crime.

### 5. *The scope for development of a coherent policy*

The PPD implies that governments *have to* take self-cleaning initiatives into account when determining a supplier’s debarment period, regardless of how they have specified their rules at the national level. In 5.1, we will explain the mandatory nature of self-cleaning principles in light of basic EU-law principles, before we turn to legal reasons for allowing debarment to depend on the severity of the committed acts (5.2 and 5.3). Our understanding of the space for policy improvement is summarized at the end of the section.

### 5.1. The legal status of self-cleaning

Directive 2004/18 did not provide a clear legal basis for the recognition of self-cleaning as a way out of debarment. However, clarifications on how self-cleaning should affect debarment were demanded already in the preparatory phases of that directive.<sup>(9)</sup> The relevance of self-cleaning was even mentioned explicitly in drafts but removed in the final version of the directive, most likely because of the clear opportunity to make exemptions based on overriding requirements in the general interest.<sup>(10)</sup> Hence, under the old directive an opportunity to allow undertakings having demonstrated that sufficient self-cleaning measures had been taken could be formally based on the exception for overriding requirements in the general interest. This is so because barring criminal contractors from public procurement represents an objective which may justify restrictions on the free movement.<sup>(11)</sup>

However, the principle of proportionality also mandates such a solution, because the debarment of trustworthy undertakings (or rather, undertakings having restored trustworthiness), would fall afoul of both the principle of proportionality and the principle of equal treatment. According to Arrow-smith et al.:

*“contracting authorities are required to accept the existence of self-cleaning measures as a limitation on the mandatory exclusion rules, and hence to admit contractors that have undertaken effective self-cleaning measures.”*<sup>(12)</sup>

This view was confirmed in the 2011 Green Paper on public procurement:

*“An important issue on which the current EU public procurement Directives remain silent is what are referred to as the « self-cleaning » measures, i.e. measures taken by the interested economic operator to remedy a negative situation affecting his/her eligibility. Their effectiveness depends on their acceptance by Member States. The issue of « self-cleaning measures » stems from the need to strike a balance between the implementation of the grounds for exclusion and respect for proportionality and equality of treatment. The consideration of self-cleaning measures may help contracting authorities in carrying out an objective and fuller assessment of the individual situation of the candidate or tenderer in order to decide its exclusion from a procurement procedure.*

*Article 45 allows Member States to take into account self-cleaning measures as far as such measures show that the concerns about professional honesty, solvency and*

<sup>(9)</sup> The issue was first raised in the Opinion of the Committee of the Regions, 2001, OJ C 144/23, par. 2.5.2.

<sup>(10)</sup> S. ARROWSMITH et al., *cit. supra* note 7, 8. That provision has also been included in the 2014 directive, see Article 57(3), cited above.

<sup>(11)</sup> See ECJ, 24 March 1994, *Schindler*, in Case C-275/92, ECR I-1039, par. 57-60, and ECJ, 16 December 2008, *Michaniki AE v Ethniko Symvoulío Radiotileorasis and Ypourgos Epikrateias*, in Case C-213/07, ECR I-9999, par. 59.

<sup>(12)</sup> S. ARROWSMITH et al., *cit. supra* note 7, 25.

*reliability of the candidate or tenderer have been eliminated. However, there are no uniform rules on « self-cleaning », even though measures taken by the economic operator to remedy the situation of exclusion are taken into account anyway by the contracting authorities in some Member States.”*(13)

On this background, the introduction of specific principles governing self-cleaning in the 2014-directive was most welcome. The text of the directive also makes clear that Member States are prevented from excluding undertakings which have implemented relevant measures; “*the economic operator concerned shall not be excluded from the procurement procedure.*”

Keeping apparently honest suppliers debarred will easily come in conflict with the formal purpose of the debarment rules, namely to ensure citizens’ trust in public procurement. Debarment, at least not formally, is not meant to function as an added penalty.(14) If convicted suppliers have become significantly more trustworthy because they have made substantial and credible steps to get out of the situation that caused the crime (as listed in sections above), it will not make much sense to keep them excluded from tenders. Given such steps, the supplier may even have become *more honest* than other players in the market.

Allowing “cleaned” suppliers to take part in tenders promotes competition, which is a clear benefit for the citizens’ whose trust is wanted, and assuming that conditions of self-cleaning hold, it will not imply a higher risk of crime. The preventive impacts are nevertheless ensured by a debarment system that takes self-cleaning into account – since the convicted suppliers are in fact excluded, undue business practices are clearly not accepted, and costly and comprehensive steps are required for these suppliers to regain access to the market.

As well, lack of convincing and mandatory self-cleaning principles may induce courts to render judgments interfering with the functioning of criminal law. For example, in the Norconsult case, the Norwegian Supreme Court refused to impose penal sanctions on one of Norway’s major consulting engineering companies in view of the self-cleaning measures undertaken by it and the potential financial consequences of the sentence.(15) Had a penal sanction been imposed, the undertaking would have been debarred from future public contracts with no guarantee that the cleaning measures would have been considered sufficient by contracting authorities. The case arose from corruption involving three low-level employees on a project in Tanzania.

(13) EU Commission, *Green Paper on the modernisation of EU public procurement policy*, COM(2011) 15 final, 27 January 2011, 52.

(14) The debarment rules are vulnerable to populist interpretation by those who see a need for more repressive criminal law sanctions. TILLIPMAN (2013), see footnote 9, lists several examples of what she calls “inflammatory anti-contractor rhetoric” applied by legislators to defend mandatory debarment.

(15) Norwegian Supreme Court judgment of 28 June 2013 in case 2012/2114 (HR-2013-01394-A).

Allowing the costly consequences of debarment to become more severe than necessary will easily violate Treaty principles, and thus, given our interpretation of these different legislative sources, principles and arguments, it cannot be the Member States' right to exclude a supplier that has taken sufficiently credible self-cleaning steps. Accordingly, sufficient self-cleaning steps should serve to limit a government's opportunity to debar a convicted supplier from public tenders, and legally it is possible to apply a self-cleaning principle consistent with the suggestion of 'climbing down the debarment-curve' as described in Section 4.(16)

### 5.2. The graveness of the offence

Also when it comes to our suggestion of letting the severity of the crime decide the (starting) period for debarment (i.e., the longer, the graver), several sources support such a view. In particular, the proportionality principle makes it difficult to operate with a fixed length of debarment, and suggests a more nuanced relationship between crime committed and reaction.(17)

Under Directive 2004/18, some countries have linked the debarment period to the length of time a supplier is listed in the national crime register.(18) There is variation across countries on this matter. While Denmark(19) applies the judicial record, Germany(20) considers that period too long and the rule too rigid, whereas Sweden finds it *disproportionate* to operate with a 'too long' fixed period.(21)

(16) Many countries, like the Nordic, have implemented the 2004 directive without spelling out the effects of self-cleaning measures in detail. For examples of more specific regulation, see the Austrian Bundesvergabegesetz 2006, § 73 and the German Vergabe – und Vertragsordnung für Bauleistungen. Abschnitt 2 – Vergabebestimmungen im Anwendungsbereich der Richtlinie 2004/18/EG (VOB/A – EG) § 6(4) 3 reads: "Von einem Ausschluss nach Nummer 1 kann nur abgesehen werden, wenn zwingende Gründe des Allgemeininteresses vorliegen und andere die Leistung nicht angemessen erbringen können oder wenn auf Grund besonderer Umstände des Einzelfalls der Verstoß die Zuverlässigkeit des Unternehmens nicht in Frage stellt."

(17) ECJ, 21 June 1979, *Atalanta Amsterdam BV v Produktschap voor Vee en Vlees*, in Case C-240/78, ECR 3127, par. 15.

(18) EU Commission, *Communication from the Commission to the Council and the European Parliament: Disqualifications arising from criminal convictions in the European Union*, COM(2006) 73 final, par. 19-20.

(19) The Danish Competition and Consumer Authority Guidelines to the Procurement Directives, 2006, 149, (in Danish only), accessible on <http://www.kfst.dk/udbudsomraadet/udbudsregler-og-vejledninger-mm/vejledninger/>.

(20) See H.-J. PRIEB – H. PÜNDER – M. STEIN, *Self-cleaning under National Jurisdictions of EU Member States -Germany*, in H. Pünder – H.-J. Prieb – S. Arrowsmith (eds. by), *Self-Cleaning in Public Procurement Law*, Carl Heymanns Verlag, 2009, 51-100 and 60-61.

(21) See the decision from the Swedish Administrative Appeal Court (Kammarrätten), Stockholm in case 3767-09, accessible on [http://www.kkv.se/beslut/\\_0707114847\\_001.pdf](http://www.kkv.se/beslut/_0707114847_001.pdf), and from the Stockholm Administrative Court (Förvaltningsdomstolen), Stockholm in case 25630-10, [http://www.kkv.se/beslut/\\_0712145833\\_001.pdf](http://www.kkv.se/beslut/_0712145833_001.pdf). (In Swedish only).

The 2014-directive introduced a fixed five-year maximum debarment period, in that it imposes an obligation upon the Member States to:

*“determine the maximum period of exclusion if no measures as specified in paragraph 6 [self-cleaning measures] are taken by the economic operator to demonstrate its reliability. Where the period of exclusion has not been set by final judgment, that period shall not exceed five years from the date of the conviction by final judgment in the cases referred to in paragraph 1.”*

This five-year limitation is in line with earlier suggestions. It should be noted, however, that the real maximum time of debarment may be considerably longer than five years because the starting point for the time-limit is set to the time of conviction.<sup>(22)</sup>

The important message here is, however, that although the maximum period is fixed, there is still flexibility for the Member States to enact rules varying the debarment period depending on the graveness of the crime. As well, the fact that the maximum period is five years from a final conviction does not prevent the Member States from introducing rules in line with the principles set out in Section 4 counting from the date the crime was committed.

### 5.3. The policy space for improving the debarment legislation in light of self-cleaning

Despite the many debates about debarment and self-cleaning in public procurement in recent years, the legislation is still highly ambiguous. When it comes to the question of how self-cleaning should matter in terms of the length of debarment, there is significant flexibility for Member States to find their own solutions, particularly since the literature offers little guidance. This chapter has attempted to contribute to the debate, and we have made four specific suggestions based on the purpose of the rules, the opportunity to incentivize compliance with the law, the importance of keeping the harmful consequences of debarment at a minimum, as well as our interpretations of the legal landscape – explained in Section 4:

- A. “administrative principles” to facilitate process, enforcement and predictability – including
  - (i) *external ruling* on debarment and self-cleaning decisions (decisions not to be made by procurement entity); and
  - (ii) clearly formulated *self-cleaning criteria* (which are possible for outsiders to monitor);

<sup>(22)</sup> It is submitted that the chosen solution is not optimal in that the real time limit will depend on the effectiveness of national criminal law procedures. As well, in certain cases it may create disincentives to appeal a judgment to a higher court (because the debarment period will *de facto* be increased in case of a negative judgment).

- B. “mechanisms” – relating to how compliance with the law can be enhanced while the benefits of competition in public procurement are protected – including
- (iii) *incentivized compliance* which means to let suppliers climb further down the debarment period curve the more (credible) self-cleaning initiatives they carry out; and
  - (iv) *proportionality* in terms of letting the (initial) debarment period depend on the severity of the committed acts.

As explained above, Member States have significant policy space for improving their legislation in terms of reaching the goals behind debarment specifically and public procurement rules in general. The policy space is quite clear when it comes to suggestions (ii), (iii) and (iv), as discussed in part 5.1 and 5.2. When it comes to point (i) on external decision, the EU Commission seems to assume that decisions are made by the «contracting authority», that is, the procuring entity, thus in conflict with our suggestion about independent decision and oversight. The EU perspective is confirmed in the EU’s own procurement Regulation, in which it is stated:(23)

*“In order to determine duration of exclusion and to ensure compliance with the principle of proportionality, the institution responsible shall take into account in particular the seriousness of the facts, including their impact on the Communities’ financial interests and image and the time which has elapsed, the duration and recurrence of the offence, the intention or degree of negligence of the entity concerned and the measures taken by the entity concerned to remedy the situation.”*(24)

However, the assumed decision-making process is a matter of administrative organization. The reference to contracting authorities is merely an assumption that these are the units that will end up making the judgments in practice, while in practice it will also be up to each country to let these decision-making procedures function as efficiently as possible. The checks-and-balances aspect of external ruling, combined with the obvious risk of narrow interests or collusion between procurement agent and supplier, in particular in long term business relationships or in geographically limited areas, suggests that it would be difficult for the EU Commission to insist on a system where the procuring entities consider the debarment question. We therefore also assume a certain policy space for better solutions when it comes to this administrative aspect.

(23) Council Regulation No. 1605/02/EC on the Financial Regulation applicable to the general budget of the European Communities, Art. 93(1).

(24) Art. 133a was introduced by Commission Regulation (EC, Euratom) No. 478/2007 of 23 April 2007 amending Regulation (EC, Euratom) No. 2342/2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) No. 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities.

#### 5.4. Coordinated solutions preferred

Even if there is policy space for each member state to optimize these rules, a coordinated approach should be much preferred for the region as a whole. There is a risk that the policy flexibility embedded in the PPD will not only create a patchwork of rules and suppliers who are debarred in one EU country and not in the next, but also that many countries will fail to exploit the beneficial mechanisms described in Section 4 (and listed in keywords in 5.3). Throughout the region, countries have the opportunity to incentivize compliance and reduce the potentially harmful short-run consequences of debarment for competition. Reaping the full benefits will require a coordinated approach. Ideally, there should be one common approach, one list of debarred suppliers, and one set of criteria on how convicted firms can regain their position as sufficiently trustworthy suppliers, at least for countries with a similar legislation, such as the EU.

Coordination across countries and institutions will imply a much clearer signal-effect against convicted suppliers, that inclination to criminal acts will not be tolerated, particularly if debarment in one country or by one organization implies debarment by others, regardless of where (or by which branch of the company) the crime was committed. (25) What we should keep in mind, however, is that the trustworthiness of different parts of a large international corporation may differ; the trustworthiness in one context and country may be different than in another. A further concern is debarment of *suspected* offenders. If trusted public procurement is the goal, why not debar a firm under investigation, which is now quite common – regardless of where in the world the investigation takes place? It is important to be aware of how coordination in debarment may have its own side-effects. It may, for instance, have to imply a reduced debarment period – since indeed, the reaction will strike harder. If, by trying to force suppliers to act with integrity, we eliminate them from the market place, we truly throw out the baby with the bathwater. Coordinated and globalized solutions on debarment will call for coordinated protection of markets as well.

International collaboration on regulatory nuances in debarment requires joint reasoning and learning. Debarment in public procurement is now applied across the globe – by governments, international organizations and the procurement units of firms – with many different administrative solutions and debarment criteria. A knowledge bank of lessons learned would help us draw on the experiences elsewhere and eventually strengthen our confidence in the solutions we end up choosing. (26)

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(25) Consider for instance the “cross-debarment” by development banks. On April 10 2010, several Multilateral Development Banks (MDBs) signed the “Agreement on Mutual Enforcement of Debarment Decisions” on 9 April 2010, see <http://lnadbg4.adb.org/oi001p.nsf/>.

(26) During the fall of 2013 the World Bank conducted a comprehensive review process of its sanctions system and experiences where the views of governments, the private sector, civil society and research were brought in; see their law, justice and development websites at [www.worldbank.org](http://www.worldbank.org). Such exercises might benefit

## 6. Conclusion

Debarment from public procurement has become an important weapon in the fight against corruption and other forms of business-related crime. While EU Member States are obliged to implement such rules, it is up to each state to consider nuances, enforcement, and how to avoid “unnecessary” harmful consequences.

While debarment is supposed to promote trust in public procurement, there are trade-offs associated with this trust. Our initiatives to fight crime must match our attempts to protect competition. Governments are not only trusted to react against crime, but also to secure ‘value for money’ in their allocations.

Even suppliers that have been found guilty in the listed offences are market players, often large employers too, and they should not be excluded from public procurement longer than what is deemed “necessary” for them to regain trust. For these reasons, we have to develop clearer ideas of what is required for these players to regain trustworthiness. The most important suppliers are organizations with owners, a management and administration; rarely individuals with uncorrectable integrity flaws. Under external monitoring, these organizations can make convincing and monitored steps which force them to act honestly and responsibly.

The revised PPD addresses firms’ opportunity to avoid or reduce debarment through self-cleaning initiatives. However, there are no official policy principles for the relationship between such initiatives and the debarment period, and hardly any literature exists on how these rules can incentivize compliance with the law.

In an attempt to get us somewhat further along the path to addressing these challenges, this chapter has discussed how we can align different goals behind procurement rules in the use of debarment and self-cleaning. We have sketchily suggested principles and mechanisms and outlined the policy space for legal improvements.

In this chapter we call for international collaboration and coordinated solutions. If this is not politically achievable, it is at least possible for governments to improve their rules.

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the process towards a well-functioning and harmonized system within the EU region and internationally.

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## CHAPTER 5

### Brief notes on bid rigging and price fixing in Poland

BY

Anna GORCZYNSKA

Assistant Professor, Univeristy of Lodz

#### 1. Introduction

Bid rigging (also called collusive tendering) is the most common form of distortion of competition, especially in the context of public spending. Bid rigging occurs when companies which are expected to compete instead cooperate to offer lower quality goods or services to the purchaser, or fix prices which do not correspond to the market value of the offered goods. Thus, illegal agreements replace the competitive marketplace.

The importance of bid rigging is proved by the fact that it decreases the effectiveness of the public investment. It must be emphasized that the main goal of the bidding procedure is to achieve better value for money. Lower prices, better quality, and innovation can be achieved only if companies compete honestly. Bid rigging can distort competition in the procurement process by undermining the benefits which should be achieved in a genuine tendering procedure.

The economists argue that the frequent occurrence of this type of cartel is due to the characteristics of the tendering procedure which facilitate conspiracy, for example inelastic and stable demand or small numbers of companies involved in the tendering procedure. The principle of transparency in the award procedure should theoretically facilitate detection of cheating in public spending. (1) However, the detection of bid rigging is difficult due to the many actors involved in the manipulation of the award of public contracts. (2)

The aim of this Chapter is to discuss bid rigging and its most common form, that is, price-fixing, as the most harmful form of abuse of competition rules by

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(1) M. MACI, *Bid rigging in the EU public procurement markets: Some history and developments*, in *European Competition Law Review*, 2011, 406; see also: S. DAVIES – A. MAJUMBAR, *The development of targets for consumer savings arising from competition policy*, in OFT Economic Discussion Paper, 2002, 52-53.

(2) S. WEISHAAR, *Cartels, Competition and Public Procurement. Law and Economics Approaches to Bid Rigging*, Elgar Publishing, 2013, 65.

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companies, which results in limiting the efficiency of public spending. Some examples of Polish regulations and jurisdiction on bid rigging are also given. A helpful tool for combating bid rigging is the OECD publication “Guidelines for Fighting Bid Rigging in Public Procurement” (2012), which not only enumerates the most common forms of bid rigging, but also offers a checklist for designing the procurement process to reduce this risk.<sup>(3)</sup> The latest report of the European Commission’s “Public Procurement: costs we pay for corruption” (2013) also presents an opinion that bid rigging can be considered for the most dangerous factor of corruption increase in all tendering procedures.<sup>(4)</sup>

## 2. Competition rules in EU law

The most important rules of the European Union competition law are set forth in Articles 101 and 102 of the Treaty on Functioning of the European Union (TFEU).<sup>(5)</sup> Infringement of this EU law may result in fines of up to 10% of the global turnover of the collusive companies. Moreover, in many countries infringement of competition rules constitutes a criminal offence and entails personal liability. Article 101 TFEU contains provisions concerning collusion also known as cartel activity. It is stated that all agreements between enterprises which have as their object or effect the prevention, restriction, or distortion of competition in the EU are prohibited. Infringement of Article 101 is committed when all of the following elements are present cumulatively. Article 101 TFEU states that all types of agreements of anticompetitive nature fall under the scope of EU regulations. It should be noted that such agreements can be concluded both in the written and oral form, and may even be executed in the form of concerted practices between companies or organisations of companies. The significant element in such agreements is distortion of competition, no matter whether this would be the object or effect of collusive behaviour. Thus, collusion mentioned in Article 101 TFEU directly refers to public procurement and constitutes a common form of abuse of competition. Article 102 TFEU prohibits abuse of a dominant position by a company or companies, although European law does not prohibit a dominant position as such. A company is said to hold a dominant position if it controls 40% or more of a particular market. Such a situation is bound to occur rarely due to the high threshold of market dominance. However, it can be observed in the case of rare

(3) *OECD Guidelines for Fighting Bid Rigging in Public Procurement 2012*, 2012, in [www.oecd.org](http://www.oecd.org).

(4) EU Commission, *Public Procurement: Costs we pay for corruption*, October 2013, available at [www.ec.europa.eu/anti\\_fraud/documents/fraud/pwc\\_olaf\\_study\\_en.pdf](http://www.ec.europa.eu/anti_fraud/documents/fraud/pwc_olaf_study_en.pdf).

(5) G. HIRSCH – F. MONTAG – F.J. SÄCKER, *Competition Law: European Community Practice and procedure*, London Sweet and Maxwell, 2008; D. CHALMERS – G. DAVIES – G. MONTI, *European Union Law*, Cambridge, 2010, 973; C. MUNRO, *Competition law and public procurement: two sides of the same coin?*, in *PPLR*, 2006, 352-361.

goods and services, e.g., in the IT sector, or the supply of natural resources. There are relatively few cases of bid rigging cartels in public procurement in the EU law.<sup>(6)</sup> Among the main factors which explain this situation are the level of opening of the public procurement markets in the European Union, and the enforcement of EU competition law against the anti-competitive practices in public markets.<sup>(7)</sup> Additionally, bid rigging is often associated with corruption of contracting authorities officials who are in charge of public procurement and who are not interested in the investigation of illegal awards of contracts.<sup>(8)</sup> On the other hand, in recent years, at both the European<sup>(9)</sup> and national levels,<sup>(10)</sup> we can observe an increase in cases which directly refer to bid-rigging. It is a sign of European-wide consideration of bid rigging as the most harmful form of cartels in terms of efficiency in public expenditures.

### 3. Definition of bid rigging

The legal definition of bid rigging is not included to the legislation of the European Union but it can be derived from the rules of competition and main rules of public procurement system: equal treatment and non-discriminatory treatment of the participants of tendering procedure.<sup>(11)</sup> The definitions are formulated on the level of case law and national legislation<sup>(12)</sup> as well as in the doctrine of competition law.<sup>(13)</sup> European law does not criminalise cartels or

(6) *Vereniging van Samenwerkende Prijsregelende Organisaties in de Bouwnijverheid v. Commission of the European Communities (SPO)*, in T-29/92 [1995] E.C.R. II-289, upheld in appeal in case C-137/95 [1996] E.C.R.

I-1611; *HFB Holding für Fernwärmetechnik Beteiligungsgesellschaft mbH & Co KG v. Commission of the European Communities* (T-9/00) [1999] E.C.R. II-2429.

(7) M. MACI, *Bid rigging in the EU public procurement markets: some history and developments*, cit., 408.

(8) A. LAMBERT-MOGILIANSKY – K. SONIN, *Collusive market-sharing and corruption in procurement*, in *Journal of Economics & Management Strategy*, 2006, 883; OECD, *Fighting corruption and promoting integrity in public procurement*, 2005.

(9) ECJ, 15 May 2008, *SECAO SpA I Santorso Soc.COOP. arl v. Comune di Torino*, in Case C-147/06, E.C.R. I-3565; ECJ, 19 May 2009, *Assitur Srl v. Camera di Commercio, Industria, Artigianato e Agricoltura di Milano*, in Case C-538/07, E.C.R. I-4219; *Koninklijke Wegenbouw Stevin BV v. European Commission*, in T-357/06; *Fuji Electric CoLtd v. European Commission*, in T-132/07, E.C.R. II 4091-4218; *Areva v. European Commission*, in T-117/07, E.C.R. 633-788; *Siemens AG Österreich v. European Commission*, in T-122/07, E.C.R./II 793-898; *Fifa v. European Commission*, in T-385/07, E.C.R. II-205-268; ECJ, 11 July 2013, *European Commission v. Stichting Administratiekantoor portielje i Gosselin Group NV*, in Case C-440/11, not yet published; ECJ, 23 August 2013, *Schindler Holding v. European Commission*, in Case C-501/11 P, not yet published.

(10) Number of bid rigging cases in Poland in the rulings of National Appeals Chamber (KIO): 2013 - 19 cases; 2012 - 15 cases, 2011 - 21 cases e.g. KIO 2694/13, KIO 1703/13, KIO 1441/13, 1400/13, KIO 1353/13, KIO 1282/13, KIO 149/13, KIO 2276/12, KIO 1287/12, KIO 1243/12, KIO 896/11, KIO 1444/11, KIO 1866/11.

(11) See also S. ARROWSMITH, *The Law of Public and Utilities Procurement*, Sweet and Maxwell, 2005, 62-72; C. BOVIS, *The Liberalization of Public Procurement and its Effect on the Common Market*, Ashgate, 1998.

(12) See footnote No. 8 and 9.

(13) A. SANCHEZ GRAELLES, *Public Procurement and EU Competition Rules*, Oxford 2011.

bid-rigging but allows the Commission to impose administrative penalties on collusive companies.(14)

Bid rigging involves illegal agreements concluded between the participants of a tendering procedure as well as concerted practices between companies aiming at restricting competition. The most common types are:

1. Collusion between companies which participate in a tendering procedure, in respect of the offers submitted and to all activities which restrict competition (vertical and horizontal collusion);
2. Collusion between the contracting authority and a company/companies.

In Poland the general rule forbidding all forms of illegal collusion can be derived from the Act of 29 January 2004 – Public Procurement Law,(15) which sets forth the rules of public procurement. In the Polish legal system, bid rigging is prohibited by the Act of 16 February 2007 on Protection of Competition and Consumers,(16) which states that any agreements concluded by companies participating in tendering procedures and agreements concluded between a bidding company and the contracting authority are forbidden. The law prohibits collusion in respect of the terms and conditions of the submitted bids, especially as regards price and scope of work. The general prohibition of bid rigging is addressed both to the procedures conducted pursuant to the Public Procurement Law and the Act of 23 April 1964 – the Civil Code.(17) Thus, cartels in tendering procedures constitute the most serious anticompetitive conduct. Bid rigging cannot be permissible, and even *de minimis* safe harbour rules are not applicable.(18)

#### 4. Forms of bid rigging

Bid rigging is concluded in various forms, but all of them impede the efforts of public purchasers to obtain goods and services at the lowest possible price.(19) Moreover, bid-rigging cartels lead to the restriction of competition.

In the doctrine,(20) several types of bid rigging are distinguished, which *may also occur jointly*:

(14) P. ARDEN, *Legal regulation of multi-provider framework agreements and the potential for bid rigging: a perspective from the UK local government construction sector*, in *PPLR*, 2013, 165-182, see examples given in the article: Pre-Insulated Pipe Cartel [1999] OJ L 24/1; Lifts and Escalators [2008] OJ C75/19.

(15) Dz.U. of 2004 No. 19 item 177 as amended, Article 7-8.

(16) Dz.U. of 2007 No. 50 item 31 as amended, Article 6 par. 7.

(17) Dz.U. of 1964 No. 16 item 93 as amended.

(18) A *de minimis* rule constitutes the possibility of exemption from the general ban on abuse of competition due to the minimal market position of a company and its *minimal influence on competition*.

(19) OECD, *OECD Guidelines for Fighting Bid Rigging in Public Procurement*, cit., 1.

(20) OECD, *OECD Guidelines for Fighting Bid Rigging in Public Procurement 2012*, cit.; C. KENNEDY-LOEST – M. FARLEY, *Competition Law vs Private Enforcement in the Public Procurement Field: Bid-rigging*, Public Procurement: Global Revolution V, Copenhagen 2010, conference papers, 3-5; A.

#### 4.1. Bid-rigging cartels between companies – the most common form is price fixing

4.1.1. Cover bidding, also called complementary, symbolic, or token bidding, is the most popular form. It occurs mainly in the following situations:

- I. a bidder agrees to submit a bid that is higher than the bid of the designated winner,
- II. a bidder submits a bid that is known to be too high to be accepted, or
- III. a bidder submits a bid that contains special terms that are known to be unacceptable to the contracting authority.

An agreement between companies aims to make the participants resign from a procedure or withdraw their offer. Thus, companies set up the winner of the bid in advance and submit their offers only to provide the appearance of genuine competition.

Price fixing is the main form of cover bidding. It involves collusive behaviour or any type of agreement where the bidders submit artificially high and overestimated tenders to enable the other bidder to win the contract. This behaviour gives a misleading impression that the contracting authority is offered competitive bids.

In a time of economic crisis, this particular tendency has been observed in the market of public procurement. Entities submit abnormally low bids, which could be eliminated by existing legal regulations both on the European and national levels, but in practice in many countries this occurs quite rarely. For example, in Poland there have been numerous instances not only of low bids, but of abnormally low bids in public road construction. Enterprises decide to participate in public contracts to continue their business activity even at very low profits or no profits at all. In that context, price fixing does not automatically mean only fixing the highest prices that are normally available in the market, but fixing the lowest prices to eliminate possible competition and just to survive as an economic operator. The position of the contracting authority is the most favourable and the requirement of assuring the efficiency of public spending is very often wrongly understood as a pursuit of the lowest prices as the only award criterion. Unfortunately, this can often lead to poor quality public services and public works and, ultimately, to a waste of public money.

4.1.2. Bid suppression refers to agreements between companies in which one or more companies agree to refrain from bidding or to withdraw a previously submitted bid. Thus, only the designated winner's bid will be accepted. Bid

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GÓRCZYŃSKA, *Wpływ umowy przetargowej na ograniczanie praw konsumenta*, in M.Królikowska-Olczak – B. Pachuca (eds. by), *Ochrona konsumenta w prawie polskim i w Unii Europejskiej*, Beck, Warszawa, 2013, 347.

suppression occurs when a company does not submit a bid for final consideration. Another form of abuse occurs when bidders submit bids which must be rejected due to formal errors. This type of collusion can be used in tendering procedures which require the participation of a defined number of bidders.

4.1.3. Bid rotation means collusive behaviour or agreement of firms which continue to bid but agree to take turns being the winning bidder. Furthermore, they allocate a certain amount of money as a benefit from the tendering procedure to the others.

The collusive companies set down the conditions of benefit allocation, e.g., equal profit for each company or profit which corresponds to the size of each company. Illegal agreements can also involve a scheme of cooperation in the execution of a contract, e.g., all (or selected) competitors work as subcontractors.

4.1.4. Market allocation occurs when companies divide the market and decide not to compete with each other for particular geographical areas or consumers. Thus, two main types of market allocation can be distinguished, namely geographical market allocation and sectoral market allocation.

4.1.5. Concerted rejection of concluding a contract – here the winner of the procedure refuses to conclude a contract and the contracting authority is allowed to choose the second best bid. However, the second best bid is not the most advantageous due to, e.g., higher costs or inferior performance. A collusive agreement can also assume that the former winner would cooperate as a subcontractor.

4.1.6. Relationships within a group of companies (a holding company) – a Polish example

The latest amendment of the Polish Public Procurement Law was aimed to combat bid rigging, amongst other things.<sup>(21)</sup> To this end, new regulations were introduced in respect of business entities belonging to one group of companies (also known as a holding company or a capital group).

According to the Polish Public Procurement Law, two or more business entities which belong to the same group of companies but which submit separate bids or applications for participation in a bidding procedure must be excluded from that bidding procedure unless they prove that the links between them do not lead to violation of fair competition between contractors.

In accordance with the Public Procurement Law, if different enterprises within one group of companies decide to participate in a bidding procedure, then they are obligated to submit proof that the relationships between them do not infringe the principles of fair competition. The contracting authority shall

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(21) Dz.U. of 2012 item 1271 as amended.

have the right to demand explanations concerning such relationships, and if such explanations are not provided, the contracting authority shall have the right to exclude the bidder from the procedure. The term “group of companies” encompasses all business entities which are directly or indirectly controlled by one parent company, including that company.

In light of the doctrine of competition law, it is certainly true that concluding an agreement within the group in principle excludes its anticompetitiveness as the business entities constituting it are treated as a single economic unit.<sup>(22)</sup> Referring to the “single economic unit” doctrine of the Tribunal of Justice, it is necessary to conduct a test for independence or dependence of business entities each time to assess the decision-making independence of the members of a group. In principle, the conclusion of anticompetitive agreements does not concern the members of a group – such transactions are treated as a form of allocation of tasks and responsibilities between entities which comprise a single economic unit.

There are exemptions from that general rule, and the Polish Office of Competition and Consumer Protection assumes that anticompetitive agreements may be concluded only by separate and autonomic economic entities and investigates the scope of implication of the group’s cooperation for the economic relations and competition inside the group of companies.<sup>(23)</sup>

#### 4.2. Bid-rigging agreements concluded between the contracting authority and one or more companies

The contracting authority can also infringe on the general ban on collusive agreements. This occurs mainly when the specifications or qualification criteria favour a particular provider.

Price fixing is a common form of collusive practice and refers to the fixing of prices or other contract conditions. The negative impact of collusion between the public and private sector is very harmful to the economy. It eliminates entities which do not participate in illegal agreements from the market of suppliers and providers, and hinders competition between economic operators. Bid rigging between the contracting authority and firms can be conducted by manipulating the specifications of a contract, which may be provided to the collusive companies in advance or in a more detailed version as compared to others. Specifications could also be prepared through illegal cooperation between the public and private sector and thus be especially

(22) T. SKOCZNY – A. JURKOWSKA – D. MIĄSIK, *Ustawa o Ochronie Konkurencji i Konsumentów. Komentarz*, Beck, Warszawa 2009; A. ZAWŁOCKA-TURNO, *Zmowa przetargowa czy działanie zgodne z prawem?*, IKAR, 2012, 56.

(23) Office of Competition and Consumer Protection, Decision of 14 March 2007 (DOK-34/07).

designed for a particular company. To eliminate competitors, the contracting authority may introduce some qualification criteria precluding other companies. For example, one of the criteria for submitting a bid could be some technical capacity or ability, and the collusion could occur in the formulation and disclosure of the criteria and methodology for assessing this technical capacity/ability. A practical problem appears in the requirement to prove experience in conducting a particular type of works or supplying services, which does not assure best value for money, but only leads to elimination of other entities. For example, the requirement to present experience in the construction of theatres in a contract concerning the modernisation of a conference centre does not represent real public interest, but leads to elimination of a number of providers.

Collusive agreements usually result in discrimination against entities which fall outside the scope of bid rigging. However, this discrimination may be remedied based on the provisions of EU law as well as regulations of all national public procurement systems. It is treated as a serious abuse of the fundamental market freedoms, as the non-discrimination and equal treatment principles constitute the foundation of the competitive tendering procedure.

### ***5. Factors conducive to bid rigging***

The OECD Guidelines for Fighting Bid Rigging in Public Procurement distinguish some factors which are most conducive to the commitment of bid rigging. (24) Thus, bid rigging could appear in the following situations:

*Small number of companies* – bid rigging often occurs when the number of bidders is small and they can communicate easily with each other in order to, e.g., share the market geographically or according to sectors or access to know-how;

*Specific market conditions* – constant and predictable demand from the public sector increases the risk of collusion, e.g., in the construction industry. Additionally, also the economic crisis, which destabilises economic relations, contributes to many collusions. There are also some particular sectors where the risk of bid rigging is increased, e.g., the construction, defence, IT, or pharmaceutical industries.

*Problems with entering a market* – in a market limited due to licence requirements or high entry costs, companies conclude agreements to minimize the risk of new entrants.

*Trade and business associations and organisations* – although trade and business organisations and sectoral associations play a very positive role, they can

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(24) OECD, *OECD Guidelines for Fighting Bid Rigging in Public Procurement 2012*, cit.

also be used as a forum for promoting special treatment only for the members of such a group and support illegal anticompetitive behaviour.

*Repetitive bidding and identical orders* – predictable and frequent tendering procedures enhance the risk of bid rigging because economic operators want to allocate contracts among themselves.

*Lack of innovation or substitutes* – little or even no innovation in the product or services or a lack of substitutes also create conditions favourable to collusion due to a lack of alternatives.

## 6. Sanctions

Infringement of Articles 101 or 102 TFEU results in the possibility of incurring severe sanctions. The Commission can impose fines of up to 10% of a group of companies' global turnover.<sup>(25)</sup>

In Poland, fines for bid rigging can be imposed by the Office of Competition and Consumer Protection (UOKIK). In 2012, only 3 decisions on bid rigging were passed (in comparison to 40 cases of distorting competition in the form of bid rigging). In 2013 only 2 anticompetitive and 14 explanatory proceedings were initiated. UOKIK can investigate price fixing, but only if it is linked to laws concerning competition and consumers. The detectability of price fixing could be increased if the National Appeals Chamber informed UOKIK about cases of suspected price fixing, as UOKIK has the authority to conduct evidentiary proceedings.

The Polish Public Procurement Law, however, does not provide for such regulations, which should be postulated *de lege ferenda* in order to enhance the effectiveness of law.

On the other hand, bid rigging on the part of the contracting authority is punishable by fines imposed by the President of the Public Procurement Office. Being a form of abuse of non-discrimination and equal treatment, it can also fall into the scope of the general remedy system. In Poland, the system of public procurement remedies consists of a two-step litigation procedure involving an arbitration court (the National Appeals Chamber) and a civil court. The National Appeals Chamber, operating within the structure of the Polish Public Procurement Office, was set up as an administrative body responsible for the award and execution of public procurement contracts. The National Appeals Chamber was established for the examination of appeals lodged in relation to contract award procedures. The Chamber does not execute judicial power; it

(25) A. RILEY, *The modernization of EU anti-cartel enforcement: will the Commission grasp the opportunity?* in *ECLR*, 2010, 165-182; A. RILEY, *Modernizing cartel sanctions: effective sanctions for price fixing in the European Union*, in *ECLR*, 2011, 551-563.

operates as an arbitration court. The parties and participants of an appeal procedure may lodge a complaint with a court against the Chamber's ruling. The subsequent stage of litigation takes place in civil courts. The National Appeals Chamber plays an important role in developing public procurement law by applying and interpreting procurement legislation. (26)

The Act on Public Procurement Law stipulates sanctions, e.g., the sanctions for abuse of a tendering procedure include: (27) annulment of the contract, imposing a financial penalty, liability for breach of the public finance discipline, and financial corrections in contracts financed with EU funds. (28)

In many Member States, bid rigging also constitutes a criminal offence and entails personal liability. In Poland it is penalised by the Act of 6<sup>th</sup> June 1997 – the Criminal Code, which states that persons involved in obstruction or undermining of a public bidding procedure or engaged in concerted action with a person acting to the detriment of the contracting authority, if the objective of such an action is financial gain, shall be liable to imprisonment of up to three years. (29)

## 7. Conclusions

Bid rigging is a serious form of abuse of competition rules. It limits market access based on competitive conditions, and restrains quality and know-how development. Price fixing constitutes the most common form of bid rigging and consists of manipulating the prices of the subject matter of contracts. Instead of best value for money, the contracting authority is offered goods and services whose value, scope, and technical merit are regulated by collusive agreements of economic operators.

In Poland the risk of bid rigging is especially high in the construction industry, railway, pharmaceutical industry, defence sector and IT sector. As the main beneficiary of the EU structure funds, Poland should award public procurement contracts in the most efficient, competitive and non-discriminatory proceeding.

Bid rigging is difficult to prove due to the shared economic interests of the colluding companies and market fluctuation. The leniency programme is

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(26) Act on Public Procurement Law, Artt. 172-203.

(27) *Guidelines on the conditions of conducting public contract award by negotiated procedure with a notice, competitive dialogue, negotiated procedure without a notice, single-source procurement and request-for-quotes*. Public Procurement Office 2010, 3.

(28) *Guidelines of the European Commission of November 27, 2007 on financial corrections in the breach of public procurement rules for expenditures co-financed from the Structural Funds and Cohesion Fund and finance corrections assessment for the breach of public procurement law related to realization of projects co-financed from the Structural Funds*.

(29) Dz.U of 1997 No 88 item 553 with amendments, Art. 305, par. 1.

a legal measure to encourage business entities to cooperate with competition offices in situations of existing collusion, but its role should not be overestimated as it plays only an auxiliary role in the anticompetitive procedures.

Generally speaking, the legal measures adopted both on the European and national levels seem to be sufficient. Problems concern the enforcement of legal provisions and long-lasting investigations to discover collusive behaviour. Otherwise, awareness of the sanctions and their imposition should lead to a higher level of lawfulness on the part of economic partners.

Thus, the leading role in restraining bid rigging will be played by contracting authorities which should be aware of the forms and measures of combating the anticompetitive behaviour in question. The risk of bid rigging can be minimised by varied measures, for example by dividing contracts into lots, encouraging sub-contracting, use of effective monitoring of public procurement procedures and clear communication of the consequences of the abuse of competition. The public sector should always pursue best value for money to increase the effectiveness of public spending in the public interest.



## **PART IV**

# **Contract Modifications and Corruption in the Execution Phase**

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**CHAPTER 1**  
**Material changes in contract management as symptoms  
of corruption: a comparison between EU and U.S.  
procurement systems**

BY

Gabriella M. RACCA

Professor of Administrative Law, University of Turin

Roberto CAVALLO PERIN

Professor of Administrative Law, University of Turin

***1. Fair competition in the selection  
and fair execution of the promised performance***

Fair competition during the award procedure is a requirement for any procurement system. To avoid value for money remaining an abstract concept, the contractor's actual performance must coincide with what was promised at the competitive stage. However, the EU Directives mainly concern the awarding phase of the contracts, rather than their execution,<sup>(1)</sup> which is left up to the rules of the 28 Member States. Nonetheless, the question of the limits of possible changes during the execution stage has also arisen in the EU, first before the EU Court of Justice and then in the new Directive.<sup>(2)</sup>

In the EU, once a contract notice has set a call for tenders, any interested economic operator can submit a binding offer, in accordance with the requirements set out in the contract documents. The tender is binding for a limited time<sup>(3)</sup> and cannot be withdrawn. Normally, the selection of the winning

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(1) Directive 2014/24/EU on *public procurement and repealing Directive 2004/18/EC*, 26 February 2014, Wh. 107.

(2) ECJ, 19 June 2008, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* in Case C-454/06, ECR I-4401; ECJ, 29 April 2004, *Commission v CAS Succhi di frutta*, in Case C-496/99 P; Directive 2014/24/EU, Art. 72; G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the Execution Phase of Public Procurement*, in *PCLJ*, 2011, 89; R. NOGUELLOU, *La Cour de justice prend une position de principe restrictive sur les cessions de marchés, puisqu'elle admet que celles-ci constituent, sauf si elles ont été prévues dans le marché initial, un changement de l'un des termes essentiels du marché, appelant par là une mise en concurrence*, in *Droit Administratif*, 2008. ID., *France*, in R. Noguellou & U. Stelkens (eds.) *Droit comparé des contrats publics*, Bruylant, Bruxelles, 2010, 689 et seq. M. TRYBUS – R. CARANTA – G. EDELSTAM (eds. by), *EU Public contract Law. Public Procurement and Beyond*, Bruylant, Bruxelles, 2014.

(3) 180 days in Italy. Art. 11(6) of Italian Legislative Decree No 163 of 12 April 2006, see also Art. 75(5).

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tenderer has to be carried out in two stages. (4) The contracting authority verifies the candidate requirements and excludes any tenderers that do not comply with the qualitative selection criteria. (5) In the EU, the contracting entities normally pre-qualify every participant. (6) At a later stage, in application of the award criteria, the procuring entities will accept the best offer, and must withdraw from negotiations with the other competing tenderers. (7) This withdrawal is fair inasmuch as it complies with the award criteria. (8) Particularly in Europe, the required objective evaluation of the tenders involves establishing a precise ranking of the tenderers according to the scores received.

If losing bidders find any fault or contradiction, they are entitled to file claims and complaints, requesting that the procuring entity review its final decision. (9) The EU Remedies Directives (10) are directed at facilitating the correction of the award procedure before the signing of the contract in order to assign the execution of the contract to the highest-ranking tenderer, instead of awarding it to an economic operator chosen unfairly or as a result of a faulty application of the award criteria. (11) The Directive permits procuring entities to correct the award procedure without having to pay for both the costs of the awarded contract and the award of damages to the successful protesting tenderer. (12) For this purpose,

(4) ECJ, 20 September 1988, *Beentjes* in Case C-31/87, paras. 15-19; ECJ, 24 January 2008, *Lianakis*, in Case C-532/06, para. 30; and 12 November 2009, *Commission v Greece*, in Case C-199/07, par. 51 to 55.

(5) This is done on the basis of exclusion criteria and criteria of economic and financial standing, professional and technical knowledge and ability.

(6) M. STEINICKE, *Qualification and Shortlisting*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public contract Law. Public Procurement and Beyond*, cit., 105.

(7) For the awarding criteria see: Directive 2004/18/EC, Art. 53. For Italian Public Contract Code see: Legislative Decree No. 163 of 12 April 2006, Artt. 81, 82 and 83.

(8) M. FRANCH – M. GRAU, *Contract Award Criteria*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public contract Law. Public Procurement and Beyond*, cit., 131-135 and 155 – 161.

(9) Directive 2007/66/EC, Wh. No. 17, “A review procedure should be available at least to any person having or having had an interest in obtaining a particular contract and who has been or risks being harmed by an alleged infringement”. See generally: *Remedies Mechanisms*, available at [http://europa.eu/legislation\\_summaries/internal\\_market/businesses/public\\_procurement/l22006b\\_en.htm](http://europa.eu/legislation_summaries/internal_market/businesses/public_procurement/l22006b_en.htm).

(10) Directive 2007/66/EC of the European Parliament and of the Council of 11 December 2007 (amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts), OJ L 335, implemented by Legislative Decree March 20<sup>th</sup>, 2010, No. 53 and Legislative Decree No. 104 of 2010. See: C. NICHOLAS, *Remedies for breaches of procurement rules and the UNCITRAL model law in procurement*, in *PPLR*, 2009, NA151. For an EU Directives analysis, see: J. GOLDING – P. HENTY, *The new remedies directive of the EC: standstill and ineffectiveness*, in *PPLR*, 2008, 146. For an interesting French perspective: J. ARNOULD, *Ineffectiveness of contracts under the new Remedies Directive in the UK and in the EC*, speech on *Public Procurement: Global Revolution IV* (Copenhagen, September 8<sup>th</sup>, 2010). For a UK law perspective: P. HENTY, *U.K.: public procurement remedies directive – an update on the implementation process*, in *PPLR*, 2010, NA17, and P. HENTY, *Remedies directive implemented into UK law*, in *PPLR*, 2010, NA115.

(11) C. H. BOVIS, *Legal Redress in Public Procurement Contracts*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public contract Law. Public Procurement and Beyond*, cit., 365 and 368-371.

(12) Directive 2007/66/EC, Art. 1, Amendments to Directive 89/665/EEC, Art. 2, *Requirements for review procedures* provides the possibility to “(a) take, at the earliest opportunity and by way of interlocutory procedures, interim measures with the aim of correcting the alleged infringement or preventing

the European Remedies Directive introduced a standstill period of at least ten days between the award and the signing of the contract, so as to prevent the consequences of an unlawful award from becoming irreversible.(13)

Moreover, the European Remedies Directive has resulted in increased litigation with regard to contracts awarded without competitive procedures. The EU remedies system, with its highly formalized and detailed implementation in many Member States, provides notice that any award procedure could be challenged or suspended and makes it possible to obtain the award of damages.

The gain attained by the unsuccessful tenderers could overcome that of the winning tenderer, who has to be able to cover performance risks.(14) Such deviation has recently been forbidden,(15) but excessive litigation is still present and often favours illicit agreements among suppliers or with the procurement official.

Problems related to modification of a contract during its execution arise in the U.S. as well and the conditions set out in the contract subsequent to a competitive procedure can be just as distorted as in the EU.(16) Nonetheless, from a U.S. perspective, unsuccessful tenderers take a different attitude to the litigation as they have no chance of receiving damages.(17)

## **2. Material changes in the EU and the U.S. Procurement system**

The problem of changes during the execution of a contract is common to any procurement system and it seems worthwhile to compare the solutions and risks that may occur.

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further damage to the interests concerned, including measures to suspend or to ensure the suspension of the procedure for the award of a public contract or the implementation of any decision taken by the contracting authority; (b) either set aside or ensure the setting aside of decisions taken unlawfully, including the removal of discriminatory technical, economic or financial specifications in the invitation to tender, the contract documents or in any other document relating to the contract award procedure; (c) award damages to persons harmed by an infringement". S. TREUMER – F. LICHÈRE (eds.), *Enforcement of EU Public Procurement Rules*, Copenhagen, 2011.

(13) Directive 2007/66/EC, 2a (2). C. H. BOVIS, *Legal Redress in Public Procurement Contracts*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public Contract Law. Public Procurement and Beyond*, cit., 387.

(14) S. L. SCHOONER – D. I. GORDON – J. L. CLARK, *Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations*, in *The George Washington University Law School – Working Paper*, 2008, 13-14.

(15) Legislative Decree No. 104 of 2010, Italian Code of Administrative Process, Artt. 120-125.

(16) OECD, *Integrity in Public Procurement. Good Practice from A to Z*, 2007, in <http://www.oecd.org/>, 25; United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, 2013, 23.

(17) D. I. GORDON, *Bid Protests: The Costs are Real, But the Benefits Outweigh Them*, in *GW Legal Studies Research Paper No. 2013/41*, 2013, 11 et seq.; ID., *Constructing a Bid Protest Process: The Choices That Every Procurement Challenge System Must Make*, in *PCLJ*, 2006, 427 et seq.

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The award of a public contract normally gives rise to a sort of (bilateral) “exclusive right”, whereby the public entity is “locked in” with the winner bidder.<sup>(18)</sup> In Europe, once in place any contract is considered “sacred”, thus excluding all sorts of interferences from third parties (e.g. unsuccessful tenderers). For example, in some EU Member States, such as Italy and Germany, the jurisdictional competence in the awarding phase differs from the one in the execution phase.<sup>(19)</sup>

Nonetheless, contracts resulting from a competitive tendering procedure seem to be different from common contracts, even during the execution phase. Similar questions have arisen in both the EU and the U.S., as the problem relates to the fact that a contract that is signed subsequent to a competitive bidding procedure cannot be modified in the manner of a common private contract, even if the parties agree.

The U.S. Federal Government has the duty to procure goods, services and works through a competitive process, similar to the European Directives. U.S. agencies have to “obtain full and open competition through the use of competitive procedures”.<sup>(20)</sup>

Unlike in the EU Directives, in the U.S. there is a strong attention on the whole procurement process cycle, and particularly on the contract management. The “delivered” quality should, in principle, coincide with what has been promised.

In both systems, the problems are not minimal changes, but rather significant changes during the management of the contract, as they can affect the competition principle in the selection and fair treatment of unsuccessful tenderers and also of other economic operators who might have been interested in the contract.

Until recently, EU Directives did not deal with this issue, as contract management was left up to the 28 national legal systems.<sup>(21)</sup> Nonetheless, in order to safeguard the principles of non-discrimination, transparency and competition, the EU Court of Justice limited the possibility of changing the terms of a

(18) R. D. ANDERSON – W. E. KOVACIC, *Competition policy and international trade liberalisation: essential complements to ensure good performance in public procurement markets*, in *PPLR*, 2009, 67; C. YUKINS, *Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting*, in *PCLJ* 2008, 545.

(19) For Italian jurisdictional competence see: A. MASSERA – M. SIMONCINI, *Basics of Public contracts in Italy*, in *Ius-Publicum Network Review*, February 2011, available at [http://www.ius-publicum.com/repository/uploads/21\\_02\\_2011\\_14\\_41\\_Massera%20inglese.pdf](http://www.ius-publicum.com/repository/uploads/21_02_2011_14_41_Massera%20inglese.pdf), 2 et seq.; G. M. RACCA, *Public contracts*, in *Ius-Publicum Network Review*, November 2010, available at [http://www.ius-publicum.com/repository/uploads/06\\_12\\_2010\\_10\\_17\\_Raccaeng.pdf](http://www.ius-publicum.com/repository/uploads/06_12_2010_10_17_Raccaeng.pdf), 19 et seq. For German Jurisdictional competence see: U. STELKENS, *Allemagne/Germany*, in R. Noguellou & U. Stelkens (eds.) in R. Noguellou & U. Stelkens (eds.) *Droit comparé des contrats publics*, Bruylant, Bruxelles, 2010, 332 et seq.; M. BURGI, *Enforcement of EU Public Procurement Rules – A Report about the German Remedies System*, S. Treumer & F. Lichère (eds.), *Enforcement of EU Public Procurement Rules*, Copenhagen, 2011.

(20) Competition in Contracting Act of 1984 – CICA, 10 U.S.C. § 2304(a)(1)(A).

(21) M. TRYBUS, *Public contracts in European Union internal market law: foundations and requirements*, in R. Noguellou – U. Stelkens (eds. by) *Droit compare des Contrats Publics – Comparative Law on Public Contracts*, Bruxelles, 2010, 81-82.

contract after the award.(22) The ECJ maintained that material amendments are those modifications beyond the scope of the awarded contract that bidders could not have reasonably anticipated at the time of the original award when they joined the competition. Such material amendments to the subject matter of the contract might have led to a different participation (different set of bidders) and, possibly, to a different award (different winning bidder).(23) According to ECJ case law, material amendments to a contract during its currency are equivalent to the illegal direct award of a public contract, without a contract notice. This allows the ECJ to examine the performance of a public procurement process as amended (which would otherwise fall outside of EU competence) and to declare it ineffective in an endeavor “to restore competition and to create new business opportunities for those economic operators which have been deprived illegally of their opportunity to compete.”(24)

The EU Court of Justice thus preserves the right of any economic operator – particularly of unsuccessful tenderers in the specific award procedure – to fair competition during the selection phase and, consequently, during the execution of the contract. This principle of fair competition is considered as having been violated in the event of a significant (material) unforeseeable amendment to the contract terms during the execution phase.

U.S. public contract regulations seem to be more flexible regarding possible subsequent modifications: even when a contract has been signed, not only the Court but also some other authorities can step in and undo it, and normally no damages are provided.(25)

Material or cardinal changes should, in principle, not be admitted.(26) The contract contains the “changes clause”(27) that permits unilateral

(22) ECJ, 19 June 2008, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* in Case C-454/06, ECR I-4401. A. BROWN, *When Do Changes to an Existing Public Contract Amount to the Award of a New Contract for the Purposes of the EU Procurement Rules? Guidance at Last in Pressetext Nachrichtenagentur GmbH (Case C-454/06)*, in PPLR, NA253, NA 255 (2008). See: P. CRAIG, *Specific Powers of Public Contractors*, in R. Noguellou – U. Stelkens (eds. by) *Droit compare des Contrats Publics – Comparative Law on Public Contracts, cit.*, 173 et seq.

(23) It was used the “counterfactual argument” that is normally used in antitrust cases. ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich*, cit. See also ECJ, 29 April 2004, *Commission v CAS Succhi di frutta*, in Case C-496/99 P; ECJ, 29 April 2010, *Commission v Federal Republic of Germany* in Case C-160/08; ECJ, 13 April 2010, *Wall AG v Stadt Frankfurt am Main* in Case C-91/08; ECJ, 25 March 2010, *Helmut Muller* in Case C-451/08; ECJ, 4 June 2009, *Commission v Greece* in Case C-250/07; ECJ, 15 October 2009, *Acoseit* in Case C-196/08.

(24) Directive 2007/66/EC, Wh. No. 14.

(25) See FAR 33.102.

(26) 41 U.S.C. § 601 et seq. Prior to the Contract Disputes Act of 1978, a claim arising from such a change could not be brought to the various boards of contract appeals.

(27) F. T. VOM BAUR, *The Origin of the Changes Clause in Naval Procurement*, in PCLJ, 1976, 175. The Changes clause was first used in defense contracts where it was taken to be essential in time of war for the government to include new technologies without halting work to renegotiate the contract. Changes clauses are in almost all categories of government contracts.

changes as long as the modifications fall “within the general scope of the contract”.(28) The contractor can only request adequate compensation for this, and if an agreement is not reached on this matter, the main interest is considered to go on and obtain the execution with the required modifications. The U.S. perspective considers that the need often arises to modify the terms of a contract after it has been signed. In such cases, the U.S. system follows the most efficient options from an economic standpoint: the modification of the contract.(29) The level of discretion of the contracting officer appears to be quite high and has been considered to admit a “presumption of allowance” of such modifications.(30)

The lack of transparency and broad discretion of the procurement official might sometimes favour malicious agreements, as sometimes occurs in the EU.

The corrupt agreement can take place even before the award has been made, and favours attractive tenders getting the contract with an intent to improve the terms afterwards, to the benefit of the contractor in return for compensation for the procurement official.

In the EU, where there is often a lack of control of contract management, the agreement can be on a lower level of quality than promised, which is accepted by the contracting official in contrast with the contract provisions.

The symptoms of a lack of integrity emerge especially when the modifications are eagerly accepted by the contractor, as they are favourable.(31) The favour can also simply be that of obtaining a contract without competition at the proper conditions, or even at particularly favourable conditions.(32)

In such cases, the former unsuccessful tenderers and other potentially interested economic operators may challenge the contracting authority on the basis that a “full and open competition” had not been assured.

(28) Market Facts, Inc., Comp. Gen. B-210226: May 28, 1985, available at <http://www.gao.gov/assets/470/464184.pdf>. GAO does not approve payment of a claim for extra compensation under the changes clause of a contract performed for a defunct federal agency where there is no written evidence that the alleged extra work performed was authorized, and the contracting officer of the defunct agency contends that such work was not authorized. Under the circumstances, the claimant has not met its burden of proving entitlement to payment.

(29) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, in *PCLJ*, 2009, 405 et seq.

(30) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, *cit.*, 405 et seq.

(31) J. CIBINIC – R. NASH – J. NAGLE, *Administration of government contracts*, 4th ed 2006, 382.

(32) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, *cit.*, 23. “Due to an understanding between the contractor and a corrupt public official, deviations from what has been agreed to between the parties, such as poor quality or defective performance, may not result in any negative consequences. The same is true for unjustified change orders, that is, orders which increase the scope of goods or services and, at the same time, the costs of the contract, often through highly uncompetitive prices”.

The U.S. federal procurement system assures equal treatment of bidders, although this is not the letter of the law.<sup>(33)</sup> It is explicit that, while all “contractors and prospective contractors shall be treated fairly and impartially”, they “need not be treated the same.”<sup>(34)</sup> In fact, many of the critical issues in U.S. procurement law – whether bidders with very low rankings, for example, should have the right to challenge an award – flow from the core problem that bidders are not equally treated.

This is an important issue that allows for a useful comparison with the EU principle of equal treatment in the award phase, which allows any tenderer to challenge the award decision. In the EU, some legal systems, such as in Italy, provide for the possibility of scrolling the ranking to the fifth position in the event of serious infringements, to replace the former winner. Such a rule seems to make it legitimate for the ranked tenderer to challenge, in the case of *inertia* on the part of the contract officer in terminating the contract following serious infringements during its execution.

The U.S. Federal Government identifies the party authorized to modify the terms of a contract between the agency and awardee as being the contracting officer.<sup>(35)</sup> The regulations set out the procedure by which the contracting officer may act (the documents that must be completed, etc.)<sup>(36)</sup> but provide poor guidance as to the circumstances under which such modifications are to be deemed legitimate. From the U.S. perspective, the question is defined by the so-called “cardinal change doctrine,” whereby an authority is not permitted to compel a contractor to perform work constituting a cardinal or material change to a contract. A cardinal or material change is construed to occur “when the government effects an alteration in the work so drastic that it effectively requires the contractor to perform duties materially different from those originally bargained for”.<sup>(37)</sup>

The issue of “cardinal change” has been applied for many years by the U.S. courts.<sup>(38)</sup> While they refer to it using different denominations (“*essential*”;<sup>(39)</sup>

(33) C. R. YUKINS, *Editor’s Note: a Response to Omer Dekel’s “Legal Theory of Competitive Bidding*, in *PCLJ*, 2008.

(34) FAR, Section 1.102-2.

(35) FAR 43.102(a). “Only contracting officers acting within the scope of their authority are empowered to execute contract modifications on behalf of the Government.”

(36) FAR 43.101(a)(1).

(37) *AT&T Commc’ns, Inc. v. Witel, Inc.*, 1 F.3d 1201, 1205 (Fed. Cl. 1993) (quoting *Allied Materials & Equip. v. United States*, 569 F.2d 562, 563–64 (Ct. Cl. 1978)); see also *Mgmt. Solutions & Sys., Inc. v. United States*, 75 Fed. Cl. 820, 830 (2007); *Gen. Dynamics Corp. v. United States*, 585 F.2d 457, 462 (Ct. Cl. 1978); *Powell*, supra note 38, at 378.

(38) *Emergent BioSolutions Inc.*, B-402576, June 8, 2010; *Lasmer Industries, Inc.* B-400866.2, B-400916.2, B-401046, March 30, 2009; *Blackwater Lodge & Training ctr. Inc.*, B-311000.2, November 10, 2008; *Atlantic Coast Contracting, Inc.* B-288969.4, June 21, 2002; *Engineering & professional Services, Inc.*, B-289331, Jan. 28, 2002; *MCI Telecomms. Corp.*, B-276659.2, Sept. 29, 1997.

(39) *Atlantic Coast Contracting, Inc.* B-288969.4, June 21st, 2002.

“material”;<sup>(40)</sup> “beyond-the-scope”<sup>(41)</sup>), they always address the same keypoint, that a modification which has substantially changed the original nature and purpose of a public contract requires a new award of the contract in order to avoid infringing competition among the bidders.

Nonetheless, the effective nature of a cardinal change is still debated: the contracting authority aims to adopt a narrow definition of the concept, in order to not be compelled to set a new award, while the losing bidders usually claim that any modification that has occurred has effectively modified the public contract and that a new award is therefore needed.

In determining whether or not a modification constitutes a “cardinal change” that triggers the competition, it is necessary to evaluate the material difference between the modified contract and the original one, examining any changes in the type of work, performance period, and costs between the contract as awarded<sup>(42)</sup> and as modified.<sup>(43)</sup> It is also necessary to consider whether the solicitation for the original contract adequately advised potential tenderers as to the type of change created by the modification, and thus whether the modification could have changed the field of competition.<sup>(44)</sup>

The timing of the change must also be taken into consideration. The more time that has elapsed since the signing of the contract, the stronger the case for allowing a modification.<sup>(45)</sup> When a request to change the terms of a contract is made close to the signing of the contract, there could be the suspicion that a corrupt agreement has been entered into.

Good practice includes the setting-up of an effective monitoring system regarding the verification of compliant contract performance, for both contract terms and specifications. Contract changes should be allowed only if this possibility is provided for in the contract or the law (e.g. by a clear and pre-established monetary cap on the contract’s value), or if those changes do not substantially change the essence of the contract.<sup>(46)</sup>

With the same purpose, the introduction of a kind of “presumption of impermissibility” that could be rebutted only when the changes are necessary to

(40) *Lasmer Industries, Inc.* B-400866.2, B-400916.2, B-401046, March 30th, 2009.

(41) *Armed Forces Hospitality, LLC*, B-298978.2, October 1st, 2009.

(42) *MCI Telecomms. Corp.*, B-276659.2, Sept. 29, 1997, 97-2 CPD 90, 7.

(43) *Atlantic Coast Contracting, Inc.*, B-288969.4, June 21, 2002, 2002 CPD 104 at 4.

(44) *DOR Biodefense, Inc.; Emergent BioSolutions*, B-296358.3; B-298358.4, Jan. 31, 2006, 2006 CPD.

(45) The Comptroller General has also criticized changes made immediately after the solicitation process has concluded. See *United Tel. Co. of the Nw.*, Comp. Gen. B-246977, Apr. 20, 1992, 92-1 CPD 374, at 7-8; *Midland Maint., Inc.*, Comp. Gen. B-184247, Aug. 5, 1976, 76-2 CPD 127, at 3-4; *A & J Mfg. Co.*, Comp. Gen. B-178163, May 10, 1974, 74-1 CPD 240 at 3.

(46) *United Nations Office on Drug and Crime (UNODC), Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption, cit.*, 23.

the successful implementation of the contract, has also been proposed.<sup>(47)</sup> The contracting entity should justify the exception to the presumption of impermissibility on a case-by-case basis.

### ***3. The limits to admitted changes and the respect of fair competition***

Following ECJ case law in this regard, the reform of the current procurement Directives raised the question of the limits to the material amendments that can be admitted during the execution of the contract.<sup>(48)</sup> The New Directive<sup>(49)</sup> describes five different circumstances under which the contracts or framework agreements may be modified without a new award procedure.

From a U.S. point of view, the question always relates to the limits of changes “within the scope of the contract” provided in the public interest and at proper conditions. The fundamental issue is whether or not a modification of the contract, or the issuance of a task or delivery order under a framework agreement, circumvents the general statutory requirement that agencies obtain a full and open competition through the use of competitive procedures when procuring their requirements.<sup>(50)</sup>

The new Directive includes a provision on material changes to contracts – what U.S. courts have traditionally called “cardinal” changes – that provides a somewhat formalistic structure around a very economically-based decision of the EU Court of Justice. When new conditions introduce new terms which would have brought other bidders into the original competition, the amendments to the original contract are material, and should trigger a new competition.<sup>(51)</sup> Courts also play pivotal roles in shaping procurement rules,<sup>(52)</sup> as the new directive points out.

3.1. A new award procedure is not required where the modifications “have been provided for in the initial procurement documents in clear, precise and unequivocal review clauses”. Contracting authorities have to clarify such

(47) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, cit., 405 et seq.

(48) Directive 2014/24/EU, Art. 72.

(49) Directive 2014/24/EU, Art. 72.

(50) See 10 U.S.C. § 2304(a)(1)(A); *Lasmer Indus., Inc.*, Comp. Gen. B-401046 et al., 2009 CPD 77 (2009).

(51) C. R. YUKINS, *The European Procurement Directives and the Transatlantic Trade & Investment Partnership (T-TIP): Advancing U.S. – European Trade And Cooperation in Procurement*, forthcoming.

(52) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06) cit. An amendment to a public contract during its currency may be regarded as being material when it introduces conditions which, had they been part of the initial award procedure, would have allowed for the admission of tenderers other than those initially admitted. G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the Execution Phase of Public Procurement*, in *PCLJ*, 2011, 89.

clauses in the procurement documents and state the scope and nature of any possible modifications or options, as well as the conditions under which they may be used. The procurement documents “may include price revision clauses or options”.<sup>(53)</sup> An extension of the contract, as a consequence of an objectively evaluated high quality performance, whenever provided, might be possible.<sup>(54)</sup> It should be noted that the choice of applying such a revision clause could also be induced by an improper advantage being given to the procurement official in charge of the decision.<sup>(55)</sup> The Directive admits such modifications of the original contract, “irrespective of their monetary value”. Nonetheless, the contract documents must set out the maximum value of the contract in order to enable the economic operators to know the possible value of the contract in advance. The discretionary power to modify the value and terms of the contract is limited by the exclusion of the alteration to the overall nature of the contract or the framework agreement.<sup>(56)</sup>

As mentioned above, from a U.S. perspective, the contract itself is a source that empowers the procuring official to make modifications because the procurement regulations require that a government contract contain a

<sup>(53)</sup> Directive 2014/24/EU, Art. 72(1)(a) also states that “Such clauses shall state the scope and nature of possible modifications or options as well as the conditions under which they may be used”.

<sup>(54)</sup> K. HARTLEV – M. WAHL LILJENBØL, *Changes to Existing Contracts Under the EU Public Procurement Rules and the Drafting of Review clauses to Avoid the Need for a New Tender*, in *PPLR*, 2013, 58 - 67, concerning the use of the review clause for a change: in the nature and scope of the subject of the contract, in price, of the duration of the contract, of contractual partner and replacement of subcontractor. S. T. POULSEN, *The possibilities of amending a public contract without a new competitive tendering procedure under EU law*, in *PPLR*, 2012, 179.

<sup>(55)</sup> United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, *cit.*, 23.

<sup>(56)</sup> ECJ, 29 April 2004, *EC Commission v CAS Succhi di Frutta SpA* in Case C-496/99 P, para. 118. The ECJ state that “the contracting authority wish, for specific reasons, to be able to amend some conditions of the invitation to tender, after the successful tenderer has been selected, it is required expressly to provide for that possibility, as well as for the relevant detailed rules, in the notice of invitation to tender which has been drawn up by the authority itself and defines the framework within which the procedure must be carried out, so that all the undertakings interested in taking part in the procurement procedure are aware of that possibility from the outset and are therefore on an equal footing when formulating their respective tenders”. ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), *cit.*, para. 57. The *Pressetext* case law state that “the changeover to the euro, an existing contract is changed in the sense that the prices initially expressed in national currency are converted into euros, it is not a material contractual amendment but only an adjustment of the contract, provided that the amounts in euros are rounded off in accordance with the provisions in force, including those of Council Regulation (EC) No. 1103/97 of 17 June 1997 on certain provisions relating to the introduction of the euro”. According to ECJ “Where the rounding off of the prices converted into euros exceeds the amount authorised by the relevant provisions, that is an amendment to the intrinsic amount of the prices provided for in the initial contract”. “Nevertheless, the conversion of contract prices into euros during the course of the contract may be accompanied by an adjustment of their intrinsic amount without giving rise to a new award of a contract, provided the adjustment is minimal and objectively justified; this is so where it tends to facilitate the performance of the contract, for example, by simplifying billing procedures”. ECJ, April 22th, 2010, *EU Commission v Kingdom of Spain*, in Case C-423/07, concerning the extension of the subject matter of a works concession for the construction, maintenance and operation of a motorway.

“changes clause” (57) granting the discretion to introduce unilateral changes, as long as the modification falls “within the general scope of the contract”. (58)

The text of this clause provides that if the contractor objects to the nature of the modification, it must perform the changed work and may only request proper compensation for the change that has been made. Whenever the monetary demand exceeds the appropriate amount, as evaluated by the procuring official, and the parties are unsuccessful in resolving this issue, the dispute resolution mechanism, as laid down in the contract, will govern its resolution. The contractor is obliged to implement the modification requested by the agency even if the parties disagree on the price owed to the contractor for the modification. (59) The “changes clause” does not contain any instructions as to when a modification of a contract is legitimate and proper and when it is not. (60)

In U.S. case law, contractual modifications that fall “within the scope of the contract” are exempted from competition requirements, as are exercises of options that were evaluated under the original competition, and can be exercised at prices “specified in or reasonably determinable from the terms of the basic contract”. (61) An increase in the price of a public contract in the U.S. is not considered to be a substantial modification since it does not alter the

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(57) *Jamsar, Inc.*, GSBCE 4396, 76-2 BCA 12053, the board refused to insert the Changes clause in a building services contract. Under the FAR, the Changes clause is a mandatory clause for almost all types of contracts.

(58) See the general guidelines set forth in FAR 43.205 and the language of the clauses that must be included in the contract between the authority and the contractor in FAR subsections 52.243-1 through 52.243-6. For reference to this as a Changes clause, see *AT&T Communications, Inc. v. Witel, Inc.*, 1 F.3d 1201, 1205 (Fed. Cir. 1993).

(59) FAR 52.243-1(e). The Federal Court reverses a decision of the General Services Administration Board of Contract Appeals. See *AT & T Communications, Inc. v. Witel, Inc.*, 1 F.3d 1201 (Fed. Cir. 1992); *Witel, Inc. v. General Services Administration*, GSBCE No. 11857-P, Aug. 4, 1992, 93-1 BCA 25,314. The GSBCE held that a modification adding dedicated telecommunication services was outside the scope of the original competition, and was therefore a new service requiring a new competition. The Federal Circuit held that the GSBCE had erred in its reading of the Services Improvements clause, and that the this clause allowed the contractors to offer “any service advantage”. The GSBCE had looked to a long line of General Accounting Office (GAO) decisions to decide whether T3 service was outside the scope of the original competition. While the GSBCE recognized that the FTS2000 contracts include a “Service Improvements” clause allowing the contractors to propose improvements to offered services or features, the GSBCE concluded that T3 service was a new or additional service, and not an improvement. The Federal Circuit recognizes that the Competition in Contracting Act of 1984 offers no guidance to decide when a modification of a contract requires a new competition, else falls within the scope of the original competitive procurement. The Federal Circuit looked to a previous GSBCE decision on modifications within the scope of the FTS2000 contracts, *MCI Telecommunications Corp.*, GSBCE No. 10450-P, Feb. 28, 1990, 90-2 BCA 22,735, and noting the GSBCE’s conclusion there that “all of the offerors believed that the successful vendors would provide virtually all commercially available attercity telecommunications services,” held that the GSBCE should have similarly concluded in *Witel* that the offerors would also have believed T3 service to be within the scope of the contract.

(60) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, *cit.*, 414.

(61) FAR 17.207(f).

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original scope of the contract: a substantial price increase alone – as long as it refers to additional services carried out by the same contractor and in relation to the original contract – does not establish that the modification is beyond the scope of the contract.

This is more evident when the contractor's price for the additional services requested, which are the cause for the price increase, was lower than the losing bidder's price for performing the same services.(62)

Considering the time extension of a public contract, the question arose in the U.S. in relation to Research and Development contracts that may involve uncertainty. A time extension, even if it was significant, was therefore not considered to be a cardinal change of the public contract awarded, since there was no material difference between the modification and the original public contract.(63)

3.2. An “impossible change of contractor” occurs whenever additional works, services or supplies must be provided for “economic or technical reasons”,(64) or whenever such a change “would cause significant inconvenience or substantial duplication of costs”.(65) This provision defines cases in which it could be possible to use the negotiated procedure without prior publication. The proposal provides a quantification of the admitted contract modifications. Any increase in price may not be higher than 50% of the value of the original contract.(66) The Directive clarifies that “for the purpose of the calculation of the price (...) the updated price shall be the reference value when the contract includes an indexation clause”.(67) Consecutive modifications are admitted, always according to the same principle.(68)

In the case of several successive modifications, the limitations attached to the increase in price shall apply to “each modification”. Obviously, any modification, and in particular subsequent modifications, shall not be aimed at circumventing the Directive.

As previously noted, from a U.S. perspective, there are situations where adjusting the terms of a contract to meet actual circumstances is considered

(62) *Atlantic Coast Contracting Inc.*, B-288969.4, June 21, 2002, 2.

(63) An important decision has been stated with regard to public contracts, awarded through a request for proposal, in the field of Research and Development “*A 5 year extension of vaccine development effort was not an out-of-scope change of the original 10-year contract*” has been significantly stated in *Emergent BioSolutions Inc.*, B-402576, June 8, 2010, 14.

(64) Directive 2014/24/EU, Art. 72(1)(b)(i).

(65) Directive 2014/24/EU, Art. 72(1)(b)(ii).

(66) Directive 2014/24/EU, Art. 72(1)(b).

(67) Directive 2014/24/EU, Art. 72(3).

(68) The envisaged provisions are the result of intense negotiations resulting in substantial amendments to the original text of December 2011. The Commission Proposal originally referred the quantification to the total amount of the modifications. Limitations to the amount of modifications were suppressed in final provision of a fix maximum amount of the possible increase in price was generally considered inappropriate.

to be more efficient than a new solicitation of tenders or continuing to follow the original terms of the contract. This can occur when: the requested change does not entail a heavy financial burden; the modification is due to changed circumstances; a new competitive bidding procedure would produce a predictable result; the change clearly improves the Government's position as a party to the contract; or when the contract is complicated and a delay would entail serious penalties.(69) The U.S. regulations provide that the incurrence of losses by a contractor in carrying out a contract is not a sufficient reason to allow for a modification of the contract, and that discretion in this matter is given to the contracting authority in accordance with the facts of the situation.(70) Modifications are considered to be legitimate if related to a situation in which the failure to modify a contract will cause the contractor to suffer such heavy losses as to be unable to complete the project or supply the product, with the result that national security may be threatened.(71) A situation in which the contractor suffers a loss as a result of an act committed by the administrative body itself can permit the required amendments.(72)

3.3. "Unpredictable circumstances" can justify contract amendments whenever they could not have been foreseen by a diligent contracting authority, provided that they do not "alter the overall nature of the contract".(73) Moreover, the limit of 50% of the price of the contract must be respected for each modification, always ensuring that the directive is not circumvented.

From a U.S. perspective, when modifications are motivated by unforeseeable circumstances, the tendency is to admit them. Significant new technological developments could require revisions to an agreement in the midst of a long-term project awarded to a contractor after a competitive bidding procedure. The need for modifications may arise during the performance of a long-term contract for health, educational, or social services, where the needs change. The unexpected discovery of an archaeological site or a mineral quarry in the middle of paving a new highway could also justify modifications.(74) The contracts should be amended in order to accommodate a new set of circumstances, as continuing the implementation of the original contract would not only be highly impractical but also clearly harmful to the public interest. Contracts for construction or demolition may contain a clause addressing "differing site conditions", (75) which provides a remedy for two types of

(69) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, cit., 407.

(70) FAR 50.301.

(71) FAR 50.302-1(a).

(72) FAR 50.302-1(b). FAR 50.302-2.

(73) As provided in Directive 2014/24/EU, Art. 72(1)(c)(ii).

(74) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, cit., 405-406.

(75) FAR 52.236-2.

condition changes: “subsurface or latent physical conditions at the site which differ materially from those indicated in the contract” and “unknown physical conditions (...) which differ materially from those ordinarily encountered” in this type of work and in the geographical area where the project is located. If the requirements contained in this FAR clause are satisfied, the contracting officer may equitably adjust the contract price and duration.

The foreseeability test also applies to bidders, and is one of the main criteria that courts apply to decide upon the legitimacy of a modification.(76)

Integrity issues could arise whenever the need to amend a contract derives not from circumstances that were unforeseeable or outside the procuring agency’s control, but from faulty assessments made by the contracting agency: erroneous design estimates discovered in the middle of a construction project that necessitate more excavation than the amount specified in the contract, or a long-term contract for the supply of computerization work that fails to provide for changes in technology that were foreseeable at the time at which the bid was solicited.(77) The question could relate to whether or not the faulty assessment was due only to incompetence or to corruption. Nonetheless, modifications in such cases require a higher degree of inquiry on the part of the authorizing body to ensure that the modification resulted from an unintended error and not from an ulterior motive. There is the risk that allowing the modification could send the wrong message that “negligence pays”.(78)

A step forward toward integrity in Europe can be seen in the provision that, within the EU, the “impossibility of changing the contractor” and the “unpredictable circumstances” require the publication of a notice in the OJEU.(79) The aim of this publicity is to assure external control over respect of the provided limits by the other economic operators who participated in the original tender and by all the economic operators of the relevant sector, as well as by associations, citizens and any stakeholder of the procurement system. In such situations, transparency can promote integrity, by preventing possible abuses.

**3.4.** A modification may also concern a change of contractor by which a new supplier replaces the original awardee.(80) In ECJ case law,(81) a change of

(76) *Makro Janitorial Servs., Inc.*, Comp Gen. B-282690, Aug. 18, 1999, 99-2 CPD 39, at 3; *MCI Telecomms. Corp.*, Comp. Gen. B-276659, Sept. 29, 1997, 97-2 CPD 90, at 8 Am. Air Filter Co., Comp. Gen. B-188408, June 19, 1978, 78-1 CPD 443, at 9–10.

(77) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, *cit.*, 406.

(78) O. DEKEL, *Modification of a government contract awarded following a competitive procedure*, *cit.*, 406.

(79) Directive 2014/24/EU, Art.72 (1).

(80) Directive 2014/24/EU, Art.72(1)(d).

(81) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), *cit.*

contractor was considered as a substantial amendment to an essential contractual term, unless this replacement is permitted by the initial contract. This decision raised some concerns as the case is not infrequent, especially in work procurement.<sup>(82)</sup> As a rule, “the substitution of a new contractual partner for the one to which the contracting authority had initially awarded the contract must be regarded as constituting a change to one of the essential terms of the public contract in question, unless that substitution was provided for in the terms of the initial contract, such as, by way of example, provision for sub-contracting”.<sup>(83)</sup> In that case, the ECJ distinguished a simple internal reorganisation of an economic operator<sup>(84)</sup> from cases where a transfer of shares during the currency of the contract<sup>(85)</sup> is made, or where the “transfer of shares in the subsidiary to a third party was already provided for at the time of transfer of the activities to the subsidiary”.<sup>(86)</sup> The ECJ stated that, in these cases, it “would be liable to constitute a new award of contract”. Public contracts are regularly awarded to legal persons. If a legal person is established as a public company listed on a stock exchange, it follows from its very nature that the composition of its shareholders is liable to change at any time, without affecting the validity of the award of a public contract to such a company. Yet, this validity might be affected when “there are practices intended to circumvent Community rules governing public contracts”.<sup>(87)</sup> Similar considerations “apply in the case of public contracts awarded to legal persons established not as publicly-listed companies but as limited liability registered cooperatives. Any changes to the composition of the shareholders in such a cooperative will not, as a rule, result in a material contractual amendment”.<sup>(88)</sup>

(82) R. NOGUELLOU, *La Cour de justice prend une position de principe restrictive sur les cessions de marchés, puisqu'elle admet que celles-ci constituent, sauf si elles ont été prévues dans le marché initial, un changement de l'un des termes essentiels du marché, appelant par là une mise en concurrence*, cit. ID., France, in R. Noguellou & U. Stelkens (eds.) *Droit comparé des contrats publics*, cit., 689 et seq.

(83) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), cit., para. 43. “However, some of the specific characteristics of the transfer of the activity in question permit the conclusion that such amendments, made in a situation such as that at issue in the main proceedings, do not constitute a change to an essential term of the contract”.

(84) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), cit., para. 45 “an internal reorganisation of the contractual partner, which does not modify in any fundamental manner the terms of the initial contract”.

(85) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), cit., para. 47 “If the shares in APA-OTS were transferred to a third party during the currency of the contract at issue in the main proceedings, this would no longer be an internal reorganisation of the initial contractual partner, but an actual change of contractual partner, which would, as a rule, be an amendment to an essential term of the contract. within the meaning of Directive 92/50”.

(86) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), cit., par. 48.

(87) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), cit., par. 51.

(88) “The terms ‘awarding’ and ‘awarded’ (...) must be interpreted as not covering a situation, such as, where services supplied to the contracting authority by the initial service provider are transferred to another service provider established as a limited liability company, the sole shareholder of which is the initial service provider, controlling the new service provider and giving it instructions, provided that the initial service provider continues to assume responsibility for compliance with the contractual

A change of subcontractor, even if the possibility of a change is provided for in the contract, may in exceptional cases constitute a material amendment to one of the essential provisions of a concession contract, where the use of one subcontractor, rather than another was, in view of the particular characteristics of the services concerned, a “decisive factor in concluding the contract, which is in any event for the referring court to ascertain”.<sup>(89)</sup>

According to the new Directive, a modification of the contractor is permitted whenever it is provided by a review clause or option in the procurement documents or in case of “corporate reconstruction, merger, acquisition or insolvency”.<sup>(90)</sup> Obviously, the new contractor has to fulfil all the qualitative criteria provided in the initial award procedure.

A change of contractor is also possible “in the event that the contracting authority itself assumes the main contractor’s obligations towards its subcontractors where this possibility is provided for under national legislation”.<sup>(91)</sup> Such a provision seems to recall provisions in French law that admit the extension to the awarding authority of liability towards subcontractors, for the contractual relationships among the contractor and its subcontractors.<sup>(92)</sup>

3.5. A final rule considers any other modification to be non-substantial and thus admitted, irrespective of value, insofar as it does not fall within the scope of the cases listed in the subsequent paragraph.<sup>(93)</sup> The listing of the cases of material amendment that make the contract modification ineffective clarifies the limits set to the discretion of the contracting authorities for the benefit of transparency and competition among economic operators. A further specification concerns modifications below the amount of the EU thresholds and that do not exceed 15% of the initial contract value for works contracts and 10% for service and supply contracts.<sup>(94)</sup> The risk to be prevented is the illicit fragmentation of the contract value in the initial award procedure and its increase with successive modifications.

obligations”. See also: ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), *cit.*, para. 52.

<sup>(89)</sup> ECJ, 13 April 2010, *Wall AG v Stadt Frankfurt am Main* in Case C-91/08, para. 39.

<sup>(90)</sup> Directive No. 2014/24/EU, Art. 72 (1)(d)(ii).

<sup>(91)</sup> Directive No. 2014/24/EU, Art. 72(1)(d)(iii).

<sup>(92)</sup> R. NOGUELLOU, *France, cit.*, 691.

<sup>(93)</sup> Directive No. 2014/24/EU, Art. 72(1)(e).

<sup>(94)</sup> Directive No. 2014/24/EU, Art. 72(2). A. GIANNELLI, *Performance and renegotiation of public contracts*, in *Ius Publicum Network Review*, 2013, available at [www.ius-publicum.com/pagina.php?lang=en&pag=report&id=44](http://www.ius-publicum.com/pagina.php?lang=en&pag=report&id=44). See also Law No. 127 dated 8 February 1995, Art. 8, establishing that any proposed amendment to a public contract involving a price increase of at least 5% of the original price should be subjected to a mandatory but non-binding opinion by the tender commission who had decreed the assignment.

#### ***4. Substantial modifications that require a new award procedure***

Amendments to the contract shall be considered to be substantial and thus ineffective whenever the contract or the framework agreement is “materially different in character from the one initially concluded”.<sup>(95)</sup> The EU Directive draws on the ECJ case law regarding the definition of forbidden “substantial modifications” of the contract.

The principle of transparency is essentially intended to preclude any risk of conflicts of interest, favoritism or arbitrariness on the part of the contracting authority.<sup>(96)</sup> It implies that all the conditions and detailed rules of the award procedure must be drawn up in a clear, precise and unequivocal manner in the notice or contract documents. This is to ensure that, firstly, all reasonably informed tenderers exercising ordinary care can understand their exact significance and interpret them in the same way and, secondly, the contracting authority is able to ascertain whether the tenders submitted satisfy the criteria applying to the relevant contract.<sup>(97)</sup>

Therefore, although any tender which does not comply with the specified conditions must obviously be rejected, “the contracting authority nevertheless may not alter the general scheme of the invitation to tender by subsequently proceeding unilaterally to amend one of the essential conditions for the award, in particular if it is a condition which, had it been included in the notice of invitation to tender, would have made it possible for tenderers to submit a substantially different tender”.<sup>(98)</sup>

The ECJ case law stated that “the terms governing the award of the contract, as originally laid down, would be distorted” in case of modifications of the conditions of the tender “when the contract was being performed”. Such modifications constitute a violation of transparency but also of fair

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(95) Directive No. 2014/24/EU, Art. 72(4). This substantial change is also present whenever the modification: (a) introduces conditions which, had they been part of the initial procurement procedure, would have allowed for the admission of other candidates than those initially selected or for the acceptance of an offer other than that originally accepted or would have attracted additional participants in the procurement procedure; (b) changes the economic balance of the contract or the framework agreement in favour of the contractor in a manner which was not provided for in the initial contract or framework agreement; (c) extends the scope of the contract or framework agreement considerably; and (d) where a new contractor replaces the one to which the contracting authority had initially awarded the contract in other cases than those provided for under point d) of paragraph 1.

(96) S. ROSE-ACKERMAN, *Corruption and conflicts of interest*, in J.-B. Auby – E. Breen – T. Perroud (eds. by), *Corruption And Conflicts Of Interest. A Comparative Law Approach*, Edward Elgar Publishing, 2014, 4 et seq.

(97) ECJ, 29 April 2004, *Commission v CAS Succhi di Frutta SpA* in Case C-496/99 P, paras. 111 and 115.

(98) ECJ, 29 April 2004, *Commission v CAS Succhi di Frutta SpA* in Case C-496/99 P, paras. 111 and 115.

competition among participants to the tender, damaging other economic operators that might have been interested in participating. Moreover, such a modification may favour the contractor and be accepted or solicited by corrupt behaviour.

The recent provision qualifies as substantial a modification that “changes the economic balance of the contract or the framework agreement in favour of the contractor in a manner which was not provided for in the initial contract or framework agreement”. This change would undermine fair competition, as the award is decided through the evaluation of the tenders and, in the EU, through a precise ranking subsequent to an objective evaluation. Significantly changing the economic balance means that the winner is favoured and the previous competitive selection is thwarted.<sup>(99)</sup>

Even when the award procedure has been carried out in strict respect of the principles of fairness and transparency, the contractor’s infringements or non-compliance with contractual clauses might modify the economic balance and, thereby distorting bids ranking *a posteriori*, thwart the competitive selection process.<sup>(100)</sup> In such cases, opportunism in the contract execution has a retrospective impact on competition at the award stage. Consequently, losing tenderers should have legal means to act at the execution stage as they can file claims and complaints. Indeed, throughout the award phase, and by extension during the execution of the contract, unsuccessful tenderers enjoy a « right to fairness and competition » according to European and national rules. These rights are mandatory and their infringement can lead to the ineffectiveness of the contract at stake.<sup>(101)</sup> Similarly, material amendments outside the scope

<sup>(99)</sup> ECJ, *EU Commission v Federal Republic of Germany* in Case C-160/08, cit., paras. 98-99-100 e 101. The amounts of the extension of the contract was quantified in € 673 719.92. This case law concern the award of contracts for public ambulance services where it has been considered substantial the extension of the subject matter of the contract to a “district association” non indicated in the contract.

<sup>(100)</sup> Concerning the principle of Transparency see: C. H. BOVIS, *EU Public Procurement Law*, Cheltenham, 2007, 67. See also: Id., *Regulatory Trends in Public Procurement at the EU Level*, in *EPPPL*, 2012, 225-226.

<sup>(101)</sup> Directive No. 2007/66/EC, Art. 1, *Amendments to Directive 89/665/EEC*, Art. 2(d), Ineffectiveness: “1. Member States shall ensure that a contract is considered ineffective by a review body independent of the contracting authority or that its ineffectiveness is the result of a decision of such a review body in any of the following cases: (a) if the contracting authority has awarded a contract without prior publication of a contract notice in the Official Journal of the European Union without this being permissible in accordance with Directive 2004/18/EC; (b) in case of an infringement of Article 1(5), Article 2(3) or Article 2a(2) of this Directive, if this infringement has deprived the tenderer applying for review of the possibility to pursue pre-contractual remedies where such an infringement is combined with an infringement of Directive 2004/18/EC, if that infringement has affected the chances of the tenderer applying for a review to obtain the contract; (c) in the cases referred to in the second subparagraph of Article 2b(c) of this Directive, if Member States have invoked the derogation from the standstill period for contracts based on a framework agreement and a dynamic purchasing system”. For the Italian System see the Administrative process code: Legislative Decree July 2, 2010, No. 104, Art. 121.

of the contract preclude other undertakings from taking part in competitions for the award of a new, different contract. In accordance with the Remedies Directive,(102) in such cases the contract becomes ineffective and void.

Oversight on the part of third parties in relation to contract performance could prevent corruptive pacts between the contractor and the procurement agent which undermine the ability to provide quality goods and services to the citizens.

The competition principle must be safeguarded until the end of the performance so that “promised quality” (as identified in the competitive award) does in fact coincide with “delivered quality”.(103) This is important with respect to the competition principle but also for the integrity of the system as the main cases of corruption recently reported in the EU occurred during the execution phase.(104) As the correction of the award for the benefit of the best tenderer is provided, there should also be the possibility to assure a correct execution for the benefit of citizens.

As previously noted, in the U.S. federal procurement system, the main goal is to obtain successful completion of contract performance. Moreover, unlike in Europe, when the award is subsequent to a competitive negotiation there is no precise ranking of the tenderers and so there may not be a second best with an interest in replacing the defaulting winner.

Restricting the power of the Government to make changes to a contract awarded after competitive bidding may cause frustration and dissatisfaction among procurement officials. The competitive bidding mechanism could be considered too rigid to act efficiently, and may lead to a distrust of the competitive procedure altogether. Due to the ambiguity of the regulations, the courts have developed case law(105) in an attempt to define the situations in which a modification of a procurement contract is legitimate.

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(102) Directive No. 2007/66/EC of (amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts) that was implemented by Italian Legislative Decree March 20, 2010, No. 53.

(103) G. M. RACCA – R. CAVALLO PERIN, *Material Amendments of Public Contracts during their Terms: From violations of Competitions to Symptoms of Corruption*, in *EPPPL*, 2013, 291-292. Some problems about the execution of the contracts are raised also in the recent Green Paper on the modernisation of EU public procurement policy Towards a more efficient European Procurement Market, *supra* note 12, § 2.5.

(104) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report*, COM(2014) 38 final, in [http://ec.europa.eu/dgs/home-affairs/what-we-do/policies/organized-crime-and-human-trafficking/corruption/anti-corruption-report/docs/2014\\_acr\\_france\\_chapter\\_en.pdf](http://ec.europa.eu/dgs/home-affairs/what-we-do/policies/organized-crime-and-human-trafficking/corruption/anti-corruption-report/docs/2014_acr_france_chapter_en.pdf), 27 et seq.

(105) The issue of legitimacy of a modification to a procurement contract was developed by rulings in two separate court systems. The first is the U.S. Court of Federal Claims, which is authorized, *inter alia*, to hear cases of infringement of the duty to hold a competitive bidding procedure established in CICA. The second is the Comptroller General, who acts by virtue of the Competition in Contracting Act.

The European tradition of a “sacred” contract which, after it is signed, becomes an exclusive matter between parties and national regulations is overcome by the provision of the European Court of Justice and the new Directive concerning limits to “material amendments”.(106) Whenever they occur during the execution phase, “material amendments” are in breach of EU law either if they are added to the original contract (extensions), or if they take the form of a worse-than-promised performance.(107) This encroachment into contract law is necessary to protect competitors against potential violations of the principle of transparency and fair competition in the award of the public procurement.

### 5. *The role of unsuccessful tenderers after the signing of the contract*

The failure to monitor the contractor’s performance and a lack of supervision over the quality and timing of the process is one of the principal risks in public contracts.(108) The monitoring of contract management assumes a strategic role to ensure the correct performance of public contracts.(109) The compliance between the signed terms of the contract and the performance is a strategic tool to verify the efficiency of the choices resulting from the award procedure. This is also a way to protect the integrity and correctness of the choices made by the contracting authority and to detect unlawful decisions or errors of assessment.

A rigorous oversight of contract implementation is therefore of paramount importance. In that regard, it seems increasingly necessary for unsuccessful tenderers to act as diligent “watchdogs”, verifying that the review process functions appropriately, and challenging infringements. This however requires a certain level of transparency in the management of the contract.(110) Unsuc-

(106) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich*, *cit.*, an amendment to the initial contract may be regarded as being material when it extends the scope of the contract considerably to encompass services not initially covered. This latter interpretation is confirmed in the provisions that impose restrictions on the extent to which contracting authorities may use the negotiated procedure for awarding services in addition to those covered by an initial contract. An amendment may also be regarded as being material when it changes the economic balance of the contract in favour of the contractor in a manner which was not provided for in the terms of the initial contract. The same principle is established in G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, *cit.*, 105.

(107) ECJ, *Pressetext Nachrichtenagentur GmbH v Republik Österreich* (C-454/06), *cit.*

(108) OECD, *Implementing the OECD Principles for Integrity in Public Procurement*, *cit.*, 81.

(109) OECD, *OECD Principles for Integrity in Public Procurement*, 2009, available at [www.oecd.org/gov/ethics/48994520.pdf](http://www.oecd.org/gov/ethics/48994520.pdf), 69 et seq.

(110) S. L. SCHOONER – D. I. GORDON – J. L. CLARK, *Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations*, *cit.*, 2008, 13-14; United Nations Commission on International Trade Law, United Nations Convention against Corruption: implementing procurement-related aspects (Second session, Nusa Dua, Indonesia, 28 January-1 February 2008), available at [www.uncitral.org/uncitral/en/index.html](http://www.uncitral.org/uncitral/en/index.html).

successful tenderers ought to be assured that they lost because the selected contractor not only submitted the best “promised” value for money (price-quality *ratio*), but has in fact delivered the best value-for-money performance. Otherwise, the main goal of the competitive mechanism would be undermined, thus distorting competition in the procurement market. Only fair behavior in contract management, namely overall compliance with the contract conditions set at the awarding stage, ensures a real and effective competition throughout the entire public procurement cycle. Since unsuccessful tenderers harmed by the unlawful award of a contract have access to remedies, they should also have access to remedies when they seek to provide evidence that the execution of the contract does not correspond to what was defined in the award.(111)

The recent EU provision on the publication of information relating to the modification of awarded contracts in the OJEU(112) might strengthen the monitoring of unsuccessful tenderers, other economic operators and civil society. In this perspective, associations, taxpayers or users may also be interested in surveying the modifications and any possible misconduct or failure that may occur in the performance of a public contract.

In Europe, regulations on public procurement set fairly strict and (presumed) objective criteria for the award of public contracts. Competing tenders are evaluated according to how many of the announced points(113) they score for (both technical and financial) criteria and sub-criteria.(114) Despite the fact that tenders have to be evaluated objectively, or perhaps for this reason, competition is frequently fierce. Tenderers tend to scrutinize each other and,

(111) M. TRYBUS, *Public contracts in European Union Internal Market Law*, in R. Noguellou & U. Stelkens (eds.) *Droit comparé des contrats publics*, 312. ECJ, 29 April 2004 *EU Commission v CAS Succhi di Frutta* in C-496/99.

(112) Directive No. 2014/24/EU, Art. 72 (1).

(113) Directive No. 2004/18/EC of Art. 23 for the technical specifications and Art. 53(1), for the awarding criteria, where is provided that “when the award is made to the tender most economically advantageous from the point of view of the contracting authority, various criteria linked to the subject-matter of the public contract in question, for example, quality, price, technical merit, aesthetic and functional characteristics, environmental characteristics, running costs, cost effectiveness, after sales service and technical assistance, delivery date and delivery period or period of completion”. The most recurrent scales are  $S_h = [0,100]$  and  $S_t = [0,1000]$ . For instance, if the adopted scale is  $S_h$  and quality has a weight of 60%, then up to 60 points are awarded to a tender’s technical specifications while up to 40 points are awarded to the price. It is worth mentioning though that public procurement regulations in the US moved away from a numerical comparison of tenders.

(114) Directive No. 2004/18/EC, Art. 53(2), where is provided that “Without prejudice to the provisions of the third subparagraph, in the case referred to in paragraph 1(a) the contracting authority shall specify in the contract notice or in the contract documents or, in the case of a competitive dialogue, in the descriptive document, the relative weighting which it gives to each of the criteria chosen to determine the most economically advantageous tender. Those weightings can be expressed by providing for a range with an appropriate maximum spread. Where, in the opinion of the contracting authority, weighting is not possible for demonstrable reasons, the contracting authority shall indicate in the contract notice or contract documents or, in the case of a competitive dialogue, in the descriptive document, the criteria in descending order of importance”. See: ECJ, June 14, 2007, *Medipac-Kazantzidis AE v Venizeleio-Pananeio* in Case C-6/05.

most importantly, control how the procuring entity makes use of those objective awarding criteria. Unsuccessful tenderers can file a claim<sup>(115)</sup> on the procuring entity's evaluation of another tenderer's offer even on the basis of minimum differences in the points assigned to an element of the tender. This can be a key factor for the award of the contract, thus overturning the result of the award itself. According to the European Directives, the ranking can be modified in favor of the protesting tenderer.<sup>(116)</sup>

The procuring entity's ability to evaluate tenders correctly and fairly is important not only for ensuring the public contract is correctly allocated, but also to guarantee its correct performance. However, in a close competition, a tenderer included in the ranking might assure the more effective contract oversight. If, for instance, the highest-ranked tender were to be ranked only slightly above the second-highest, then any lower-than-expected performance during the execution of the contract would result in the winning tender being (*ex post*) worse than the highest-ranked-loser. The contractor's opportunism at the execution stage ought to be considered *de facto* as a lower-quality tender at the competition stage. This is why, in Italy, it is also possible to provide that the second-highest tender has the right to replace the winner in the case of termination of the contract due to serious infringements.<sup>(117)</sup>

Since losing tenderers have the right to a fair competition throughout the *whole* cycle of the procurement process and therefore even during the execution phase, they are entitled to provide evidence on the infringement of the selection procedure rules and could also be active in the monitoring of the subsequent execution phase.<sup>(118)</sup>

(115) H. SCHRÖDER – U. STELKENS, *EU Public Contract Litigation*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public Contract Law Public Procurement and Beyond*, cit., 443 et seq.; B. MARCHETTI, *Il sistema di risoluzione delle bid disputes nel modello federale statunitense di public procurement*, in *Riv. Trim. Dir. Pubbl.*, 2009, 963.

(116) See generally: Directive No. 2007/66/EC, Wh. No. 13 and 14.

(117) Italian Legislative Decree No 163 of April 12, 2006, Art. 140, where is provided that Contracting authorities include in the contract notice that in the event of failure of the contractor or termination of a contract for breach of the same (in accordance with articles 135 and 136), will be progressively challenged the subjects who participated in the original tender, resulting from its ranking, in order to sign a new contract for the award of completion. It is possible to scroll the ranking and call the subject which has made the second best offer, until the fifth highest bidder, except the original contractor. In this case the award is concluded under the same conditions already proposed by the original contractor on his offer. G. M. RACCA, *Public Contracts – Annual Report 2012*, in *Ius Publicum Network Review*, 2012, available at [www.ius-publicum.com/repository/uploads/07\\_09\\_2012\\_11\\_04\\_RaccaEN.pdf](http://www.ius-publicum.com/repository/uploads/07_09_2012_11_04_RaccaEN.pdf), 32 seq.; L. FERTITTA, *La figura del secondo classificato nell'aggiudicazione degli appalti pubblici*, in *Rivista trimestrale degli appalti*, 2005, 442; V. PALMIERI, *Scorimento della graduatoria e tutela della concorrenza nell'esecuzione degli appalti pubblici*, *Foro amministrativo – C.d.S.*, 2208, 868. See also: A. MASSERA – M. SIMONCINI, *Basic of Public Contracts in Italy*, in *Ius Publicum Network Review*, 2011, available at [www.ius-publicum.com/pagina.php?lang=en&pag=report&id=43](http://www.ius-publicum.com/pagina.php?lang=en&pag=report&id=43), 8 et seq.

(118) The losing bidders' "active" role at the execution stage is logically consistent with a provision in the Italian Code of Public Contracts whereby, in case of serious infringement, contracting authorities can replace the selected contractor by "scrolling down" the initial ranking of bidders. See also: C.

Relying on non-winning tenderers to monitor winners' performance might be useful as the former have an in-depth knowledge of the subject matter of the contract and are endowed with the suitable professional skills to monitor the winner's performance. This might help alleviate the moral hazard problem arising at the execution stage in relation to the contracting authority.(119)

This monitoring task could be assigned to them by the procuring entity itself through precise clauses listed in the contract documents and could be linked to the provision of their right to substitute the winner in the event of a termination of the contract. Also, "integrity pacts" could be useful instruments for setting transparency and monitoring provisions.(120) Such provisions should be carefully defined in order to prevent colluding strategies resembling those that arise in a second-lowest bid competitive mechanism.(121) It would be necessary, for instance, to provide that the subsequent tenderer in the ranking must accept the same conditions as those set in the terminated contract.(122)

What is more, in the U.S. it is possible to find case law involving challenges to the administration of a contract that were filed by potential bidders or unsuccessful bidders. These bidders challenged the authority's decision to change the terms of the contract with the awardee, arguing that by making such changes, the contracting agency was infringing upon the duty imposed on it(123) to award procurement contracts through a full and open competition.

The decisions mainly confirm that a modification to the terms of a contract executed following a competitive bidding procedure was considered to be

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GINTER – N. PARREST – M. A. SIMOVART, *Access to the content of public procurement contracts: the case for a general EU-law duty of disclosure*, in *PPLR*, 2013, 156-164, where the Authors link the transparency and the non-discrimination principles to the relevance of considering the contract as a Public document. Concerning the disclosure of procurement documents they remind that "transparency and equal treatment are fundamental principles of procurement law and in fact inherent to exercise of public powers in general. These principles do not cease to apply after a procurement procedure ends".

(119) G. NAPOLITANO – M. ABRESCIA, *Analisi economica del diritto pubblico, cit.*, although the authors seem to consider almost exclusively the role of informational asymmetries on the subject matter of the contract.

(120) EU Commission, *Report from the Commission to the Council and the European Parliament, EU Anti-Corruption Report, cit.*, 31. Transparency International, *The integrity pact. The Concept, the Model and the Present Applications: a Status Report*, 31 December 2002, 12.

(121) A second-lowest bid is the buying equivalent of a Vickrey auction. Assuming that the procuring entity is interested in the financial dimension(s) only, the second-lowest bid mechanism awards the contract to the lowest bidder that will receive an amount of money equal to the second-lowest bid. When the number of bidders is small (only two) there exists a strong incentive to collude. One bidder will submit a very low price, while the second will submit a very high one. The former will get the contract at potentially extremely favorable conditions, and split the "collusive" payoff with the loser: G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement, cit.*, 105.

(122) EU Commission, note 2007/2309/C, January 30, 2008 containing observations on the Italian Legislative Decree April 12, 2006, No. 163, Art. 140.

(123) By CICA (Competition in contracting Act - 1984).

legitimate if it fell within the “scope of the contract” and was not considered to be legitimate if it departed from such scope. Thus, one could argue that if the modification falls outside the scope of the contract, a new bidding procedure is required, and that forcing the contractor to make the changes would constitute a breach of the contract.(124) As previously noted, the problem relates to determining whether or not a modification falls within the scope of the contract.(125) The OECD report on Federal Public Procurement in the U.S. suggested that the Government ensure a better integration among its e-procurement systems, so as to generate better quality data and promote performance analysis.(126)

The availability of clear and accurate data can also facilitate the monitoring of civil society, media, companies, NGOs and academia.(127) “Civil society, therefore, frequently generates pressure against corruption in public procurement, leading to the penalization of corrupt actors”.(128)

Correct and adequate monitoring activities can result in the availability of data on how economic operators run the performance. From such data, black-listing, debarment(129) and cross-debarment(130) forms may be created, both

(124) O. DEKEL, *Modification of a government contract awarded following a competitive procedure, cit.*, 2009, 414-415.

(125) *Lasmer Indus., Inc.*, Comp. Gen. B-401046 *et al.*, 2009 CPD 77

(126) OECD, *Public Procurement for Sustainable and Inclusive Growth. Enabling reform through evidence and peer review.* available at <http://www.oecd.org>, 15; OECD, *Implementing the OECD Principles for Integrity in Public Procurement, cit.*, 13. Gov't Accountability Office, GAO, *The National Flood Insurance Program: Progress Made on Contract Management but Monitoring and Reporting Could Be Improved*, January 15, 2014, suggest to improve monitoring and reporting of contractor performance, recommending that the Federal Emergency Management Agency FEMA (1) determine the extent to which quality assurance surveillance plans and CPARS assessments have not been prepared, (2) identify the reasons why, and (3) take steps, as needed, to address those reasons. FEMA concurred with GAO's recommendations

(127) OECD, *Implementing the OECD Principles for Integrity in Public Procurement, cit.*, 119, the principle No. 10 provide that “Member countries should empower civil society organisations, media and the wider public to scrutinise public procurement. Governments should disclose public information on the key terms of major contracts to civil society organisations, media and the wider public. The reports of oversight institutions should also be made widely available to enhance public scrutiny. To complement these traditional accountability mechanisms, governments should consider involving representatives from civil society organisations and the wider public in monitoring high-value or complex procurements that entail significant risks of mismanagement and corruption”. D. SORACE – A. TORRICELLI, *Monitoring and Guidance in the Administration of Public Contracts*, in R. Noguellou – U. Stelkens (eds. by) *Droit compare des Contrats Publics – Comparative Law on Public Contracts, cit.*, 205 - 208. In the same book see also: S. BOYRON – A. C. L. DAVIES, *Accountability and Public Contracts*, 221-225.

(128) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption, cit.*, 26-27.

(129) S. Gov't Accountability Office, GAO Report, *Suspension and Debarment*, September 2012, available at: [www.gao.gov/assets/650/648577.pdf](http://www.gao.gov/assets/650/648577.pdf). See also: S. L. SCHOONER – S. COLLINS – R. J. BEDNAR – S. A. SHAW – D. BRIAN – J. J. McCULLOUGH – J. S. PACTER – M. G. MADSEN – C. R. YUKINS – J. S. ZUCKER – A. J. PAFFORD, *Suspension and Debarment: Emerging Issues in Law and Policy*, in *PPLR*, 2004.

(130) C. R. YUKINS, *Cross-Debarment: A Stakeholder Analysis*, GW Law Faculty Publications, 2013.

as anti-corruption initiatives and so as to be able to evaluate the past performance of economic operators in the award procedure.

### 6. Material amendments and Integrity Issues

The level of quality promised in the contract that was signed after the competitive tendering process is often not delivered during the execution phase and the procuring entities may accept a different and worse-than-promised performance.<sup>(131)</sup> The infringement of the contract can lead to a material amendment, concerning a modification of the economic balance of the initial contract. Such a situation can be due to the incompetence of the procuring officials or can be considered to be the symptom of a lack of integrity, conflicts of interest, collusion or corruption.<sup>(132)</sup>

This situation may arise as a consequence of malice and corruption,<sup>(133)</sup> that is, offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence the action of a public official during the selection procedure or the contract execution. However, poor contractor performance may also be due to poorly drafted contract requirements that leave public officials unarmed when problems arise.<sup>(134)</sup>

(131) G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011; G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *The safeguard of competition in the execution phase of public procurement: framework agreements as flexible competitive tools*, in *Quaderni Consip*, VI (2010); R. CAVALLO PERIN – G. M. RACCA, *La concorrenza nell'esecuzione dei contratti pubblici*, in *Dir. amm.*, 2010, 325.

(132) R. Hernandez Garcia (ed. by) *International Public Procurement: A Guide to Best Practice*, London, 2009; T. M. ARNAIZ, *EU Directives as Anticorruption Measures: Excluding Corruption-Convicted Tenderers from Public Procurement Contracts*, in K. V. Thai (ed. by) *International Handbook of Public Procurement*, 105; E. AURIOL, *Corruption in procurement and public purchase*, in *International Journal of Industrial Organization*, 2006, 885; Transparency International, *Curbing Corruption in Public Procurement*, cit.; D. I. GORDON, *Protecting the integrity of the U.S. federal procurement system: Conflict of interest rules and aspects of the system that help reduce corruption*, in J.-B. Auby – E. Breen – T. Perroud, *Corruption And Conflicts Of Interest. A Comparative Law Approach*, cit., 46 - 52. See also: OECD, *Fighting Corruption and Promoting integrity in Public Procurement*, 2005, available at <http://browse.oecdbookshop.org/>.

(133) See C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, cit., 70; R. HERNANDEZ GARCIA, *Introduction: The Global Challenges of International Public Procurement*, in R. Hernandez Garcia (ed. by) *International Public Procurement: A Guide to Best Practice*, London, 2009, 11; T. MARIA ARNAIZ, *EU Directives as Anticorruption Measures: Excluding Corruption-Convicted Tenderers from Public Procurement Contracts*, in Khi V. Thai (Ed.) *International Handbook of Public Procurement*, 2008, 106; E. AURIOL, *Corruption in Procurement and Public Purchase*, in *Int. J. Indus. Org.*, 2006, 867; Transparency International, *Handbook for Curbing Corruption in Public Procurement*, 2006, 18-19, available at [www.transparency.org/content/download/12496/120034](http://www.transparency.org/content/download/12496/120034).

(134) In Italy both the theory and practice of public contracts have traditionally overlooked the relevance of contract management. The regulation of Italian Public Contract Code has introduced a specific “procurement execution director” in charge of the management and monitoring of the execution of goods and services procurement only recently. See Decreto Presidente della Repubblica, 5 October 2010, No. 207, Artt. 299, 300 and 301. For the aspects related to the contract execution see *Modernisation Green paper*, supra, note 6, at 24.

Integrity “beyond the selection of suppliers”(135) is required from the definition of needs to the contract administration phase as both the needs assessment and the contract management are “increasingly exposed to corruption”(136) and are neither duly addressed nor sufficiently monitored.

Adequate efforts in favour of competition, transparency and objective criteria in decision-making as fundamental principles and instruments to prevent corruption are necessary throughout the entire cycle of the public procurement process, from the beginning of the procedure to the conclusion of the performance phase. Otherwise, after the award, the procuring entity may have to accept a different and below cost, potentially subpar performance in violation of free competition and equal treatment principle.(137) This may be due to the lack of effective instruments for achieving the public interest as defined in the contract conditions (incompetence).(138) Moreover, the much debated phenomenon of “abnormally low bids” may occur because of tenderers’ decision to recover their additional « investment » (i.e. lower mark-ups).

An improper (malicious) agreement between one of the tenderers and the procurement officer allows the former to bid aggressively and win the contract as he/she already knows that he/she will not be obliged to perform properly.(139) By underperforming, the winner will obtain additional profits, to be shared with the procurement officer. If the delivered quality differs from the quality that was promised in the award, the whole equilibrium of the ranking of the tenders is undermined and the economic balance of the contract is modified in favour of the winner.

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(135) United Nations Comm’n on Int’l Trade Law, *United Nations Conventions Against Corruption: Implementing Procurement Related-Aspect*, 14. The procedures to be used by procuring entities in selecting the supplier or contractor with whom to enter into a given procurement contract”. Its Guide to Enactment states that the Model Law does not address the terms of contract for a procurement, the contract performance or implementation phase, including resolution of contract disputes, and by implication, the procurement planning phase. United Nations Comm’n on Int’l Trade Law, *UNCITRAL Model Law on Procurement of Goods, Construction and Services with Guide to Enactment*, 1994, available at [www.uncitral.org/pdf/english/texts/procurem/ml-procurement/ml-procure.pdf](http://www.uncitral.org/pdf/english/texts/procurem/ml-procurement/ml-procure.pdf).

(136) Transparency Int’l, *supra* note 7, at p. 20; see also C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model*, *cit.*, 83-88; United Nations Office on Drugs & Crime, *United Nations Convention against Corruption*, Art. 9(2), provides that a procurement system must ensure adequate internal control and risk management. Art. 9(2): “2. Each State Party shall, in accordance with the fundamental principles of its legal system, take appropriate measures to promote transparency and accountability in the management of public finances. Such measures shall encompass, *inter alia*: ... (d) Effective and efficient systems of risk management and internal control ...”. The regulation of non-selection phases of procurement may thus be addressed within the general governance system in a State party: for the reasons, it is vital that they are integrated into the procurement system itself.

(137) R. CAVALLO PERIN – G. M. RACCA, *La concorrenza nell’esecuzione dei contratti pubblici*, *cit.*, 325.

(138) O. BANDIERA – A. PRAT – T. VALLETTI, *Active and passive waste in government spending: Evidence from a policy experiment*, *cit.*, 1278.

(139) G. M. RACCA, *The safeguard of competition in the execution phase of public procurement*, Speech at the seminar *The New Public Law in a Global (Dis)Order A Perspective from Italy*, New York University School of Law, 19-20 September 2010. See also: G.M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, *cit.*, 105.

Cardinal changes or material amendments can be considered as a red flag of corruption and entail a risk of improper agreements being made between the contractor and the public official, or they may simply imply an incorrect decision that has been made as a consequence of a lack of adequate needs assessment, planning and budgeting. (140) Integrity is the basic prerequisite for achieving the “desiderata” of a procurement system and to obtain the correct reaction to the effective need for material amendments to awarded contracts.

### 7. Conclusions

The principles of transparency and competition play a key role in the awarding phase of a public procurement, but they seem to vanish during the contract management. This seems to be a prevailing feature of public contract regulation worldwide. (141) In this “black hole” of contract management, lack of transparency, incompetence, collusion and corruption might undermine the multiple objectives of public procurement systems.

The award and the execution of public contracts should not be affected by factors that harm the impartiality and the fairness of the decision (public officials’ incompatibilities and transparency rules are means to guarantee it). Avoiding the interference of political or external bodies would appear to constitute another key issue for preventing the distortion of the public contract market and favouring the implementation of best practices in the award of public contracts and in the subsequent monitoring of the performance phase.

Whenever delivered quality is shattered by opportunistic behaviour at the execution stage, the principles of transparency and non-discrimination are betrayed, since an incorrect execution undermines the competition principle put in place among competing bidders during the selection phase. In public contracts, unlike in private contracts, any amendment to the contractual conditions due to the contractor’s underperformance affects third parties, namely, but not exclusively, (142) unsuccessful tenderers. By having a substantive stake in the adherence of the contractor’s performance to that which was committed at the award stage, losing tenderers should be permitted to report infringements to challenge the contractor’s lower-than-promised performance as set forth in a contract they might have otherwise won. As a consequence,

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(140) OECD, *OECD Principles for Integrity in Public Procurement*, cit., 69, on the common risks to integrity in the post-tendering phase.

(141) United Nations Office on Drug and Crime (UNODC), *Good practices in ensuring compliance with article 9 of the United Nations Convention against Corruption*, cit., 20 et seq.

(142) H. SCHRÖDER – U. STELKENS, *EU Public Contract Litigation*, in M. Trybus – R. Caranta – G. Edelstam (eds. by), *EU Public Contract Law, Public Procurement and Beyond*, cit., 443 et seq.

they would exercise their right to fair competition and, if properly ranked, the subsequent bidder in the ranking could have the right to replace the winner.

The ability to collect and interpret information during the execution can make losing tenderers, together with the procuring authority, the most effective “supervisors” of the contractor’s compliance with contractual clauses. Since they are competitors in the same market, losing tenderers are in a potentially ideal situation for establishing which dimensions of performance are most vulnerable to opportunism. A precise evaluation of the limits for admitted “material amendments” during the execution phase is required in order to avoid thwarting competition. The idea of having losing tenderers that “cooperate” with the procuring authority might, in principle, be stretched to other crucial phases of the procurement process such as the evaluation of seemingly abnormally low tenders, especially in the case of somewhat complex public contracts where both quality and price matter. Allowing for such proactive initiatives by losing tenderers ought to be carefully defined by the procuring authority in order to fully exploit the potential benefits while limiting the risk of making the overall public procurement system even more adversarial or pro-collusive.

The monitoring of the performance of the contract by unsuccessful tenderers, and/or by third parties such as other economic operators, final users, NGOs and civil society, is a way of ensuring respect for EU principles or, in general, the competition principles that rule the award procedures. However, monitoring the correct implementation of the contract may be a useful tool to prevent potential illegal or collusive conduct among economic operators and better ensure competition throughout the entire public procurement cycle and in the procurement sector.

The U.S. experience brings to light a different perspective, wherein the lack of a precise ranking in the award of the contract after the “negotiation” stage limits the possibility of providing incentives for such monitoring activities. Ensuring respect for the principle of competition during the performance phase also seems to be a requirement for ensuring it is respected during the award phase. Any misconduct during the performance phase constitutes a distortion of competition and in the EU can result in the ineffectiveness of the contract. In any procurement system, only a deep and effective monitoring of the performance phase can stave off the risks of corruption and waste of taxpayers money.

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**CHAPTER 2**  
**The modification of public contracts:  
an obstacle to transparency and efficiency**

BY

Francisco J. VÁZQUEZ MATILLA

Ph. D. RESEARCHER, Public University of Navarra  
vocal of the administrative tribunal of public contracts  
of Navarre (Spain)

***1. Introduction***

Modifications may cause a significant impact in the execution of a contract to the extent that these changes may be considered a new contract. A contract that is repeatedly modified must be classified as inefficient. After many modifications it may no longer be known if the executor of the contract is the most advantageous to the contracting authority. In addition, numerous modifications raise questions about the integrity of the contract, and the possible existence of corruption or conflicts of interest in hiring. Modifications made by the contracting authority may be improper if they would not have been anticipated by the original tenderers who submitted tenders.

Modifying a contract is a standard practice rather than an exception. However, a modification is improper where it lacks justification or the changes would have directly affected the tendering process. In Spain, the Report and Conclusions of the Committee of Experts for the study and diagnosis of the status of procurement made in 2004, warned that the changes in the contract may undermine the competitive nature of the initial award to the extent that the contract is executed effectively, and their prices are not those by which they competed. The Report also noted the possibility of corruption in contract modifications generates moral hazard problems, since sometimes these changes are sought with the aim of creating a return on a contract for which, the tenderer had bid too low.

In conclusion, practices of this nature undermine the proper administration of the contract to be executed, and constitute a new contract that would be payable for a new tender dossier, and therefore the new advertising potential subjects interested in the award, in the light of the principles of equal treatment

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and the transparency that should govern the actions of the contracting authority. All in all, as indicated by Racca “*any violation, change, or worsening of the quality during the execution phase entails undue profit for the winner*”.<sup>(1)</sup>

This demonstrates the growing interest on the subject, with European case law recognizing that contract modifications are considered to be a new contract.

Particularly relevant are the Judgments of the CJEU, of 29 April 2004, *Commission v CAS Succhi di Frutta SpA*, 19 June 2008 *Pressetext Nachrichtenagentur GmbH v Republik Österreich* and others, or 13 April 2010, *Wall AG v the Frankfurt ville-sur-le-Main and Entsorgungs-und Frankfurter Service (FES) GmbH* and finally the 22 April 2010 *Commission v Kingdom of Spain* discussed here.

The Procurement Directives set out with the intention of integrating the jurisprudence of the CJEU. However, the legislative process resulted in a relaxation of this effort. However, the claim is appropriate to clarify the circumstances leading to amend the contract and treat it as an exception.

## ***2. The justification for limitations on the ius variandi or power to change the contract and the need for fair procurement***

The concept of will comes from the Latin term *voluntas-atris* and could be defined as “*a power to decide and manage their own behaviour*” “*free will or self-determination*” or “*choice made by the own opinion or taste, without respect or attention to another objection*”. Like a part of that content agreement, client and contractor express their autonomy to give or make a delivery, producing freely, covenants, terms and conditions which are suitable, provided they are not contrary to law, to the morality or to the public order. Pacts which therefore cannot be changed to the arbitrament of one of the contractors.<sup>(2)</sup>

The transcendent is that “*the agreed forces*” as stated in the well-known principle *pacta sunt servanda*. A Latin term, attributed to the jurist Ulpiano (addressed by him in his commentary on the title Edictal *De pactis conventis: Digesto 2.14.7.7*) that means that the agreements between parties must be fulfilled according to his tenor and the obligations that they are born from the contracts have force of law between the contracting parties and must be fulfilled to the tenor of the same ones. The amendment during the development of the contract by the parties is not allowed, and still less the imposition

(1) G. M. RACCA – R. CAVALLO PERIN, G. L. ALBANO, *Competition in the Execution Phase of Public Procurement*, in *PCLJ*, 2011, Vol. 41, 89.

(2) As expressly stated in Article 1256 of the Spanish Civil Code.

a modification from one to another. Through agreements that make up the contract creates a real obligatory force of significance similar to that of any rule of law may establish.

In the case of public contracts, after the establishment of the requirement, it is satisfied by the contracting authority as reflected in the specifications. It is the offer by the various tenderers and accepted by the first through the award of the contract, these sheets have “force of law”. In particular, procurement documents constitute a normative power *inter partes*, within a plane subject to the rules and principles of higher law.

But apart from the importance of the amendments from the contract to the contractor, may be more deserving of protection are the effects that they have between the tenderers and even entrepreneurs, who did not participate in the original tender. Perhaps, after the existence of some changes they might have been interested in it. In fact, this issue has been addressed in the European case-law regarding the need to resolve the existing contract and modify it, rather than resolve and award again. If this situation would have served to arrange a procedure for selecting the best bid, if the amendment cannot ensure, it will try the best to be obtained. Do not forget that except in the case of downward modifications of contracts, the contractor is generally the most interested in having his contract be amended to reduce the work load, particularly in the case of the low bid; which satisfies their desire to recover costs not covered by the low tender and set new prices, even when necessary and applying unlawfully and immorally known as “against low” (3) to determine the market price down. (4) The public interest should no longer be on contract but on market competition.

New Directive 2014/24/EU. These principles are the free movement of goods, freedom of establishment and freedom to provide service and the principles derived from these freedoms, such equal treatment, non-discrimination principle, mutual recognition, proportionality and the principle of transparency. (5)

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(3) The “against low” means that the new price will be applied first economic downturn made in the tender and then add that low again, and thus nullify the effect of the financial offer.

(4) R. CAVALLO PERIN – G. M. RACCA, *La concorrenza nell'esecuzione dei contratti pubblici*, in *Dir. Amm.*, 2010, 325, incorporating the issues discussed during the symposium *Consip e il sistema italiano di public procurement: concorrenza, regolazione e innovazione*, Bologna, 15 June, 2009, especially page 339, also available at <http://www.robertocavalloperin.it/repository/file/1-La%20concorrenza%20nell'esecuzione%20dei%20contratti%20pubblici.pdf>; see also G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *The Safeguard of Competition in the Execution Phase of Public Procurement: Framework Agreements as Flexible Competitive Tools*, Seminar on *The New Public Law in a Global (Dis) Order: A Perspective from Italy*, N.Y. Univ. School of Law, 19-20 September 2010, 17, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2180856](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2180856).

(5) J. A. MORENO MOLINA, *Principios generales de la contratación pública, procedimientos de adjudicación y recurso especial en la nueva Ley de Contratos del Sector Público*, in *Revista Jurídica de Navarra*. No. 45, Enero – junio 2008, 45 - 77. D. ORDOÑEZ SOLIS, *La contratación pública en Europa*, Editorial Aranzadi S.A., 2002, 36-51.

These principles will be known as general principles of public procurement. They have an overall theme, as it should guide all phases of a public contract, and therefore are applicable to contracts subject to the requirements of EU directives, such as those who by reason of the amount are not covered by the Directive.(6) We did not have this cross-cutting the amount of steps taken to award the contract are totally meaningless.

The principle of equal treatment is considered a fundamental principle to keep in mind in public procurement.(7) The principle requires that comparable situations must not be treated differently, and it is not in identical situations different.(8) It seeks to promote the development of a healthy and effective competition between the companies involved in public procurement, imposing that all tenderers have equal opportunities to formulate their tenders, and provides that the same conditions apply to all competitors.(9)

Linked to the principle of equality are the principles of publicity, transparency and competition. The principle of publicity consists of ensuring free movement of goods and persons. In short, they give rise to the recruitment of all contracting authorities of the European Union, promoting the concurrence of all stakeholders in the bid to get the best deal. Transparency is synonymous with the absence of ambiguity in the field of public procurement, which manifests itself in all phases of the process. El CJEU in the judgment of 7 December 2000, *Telaustria* C-324/98, argued that this principle implies not a right for the contracting, but an obligation of transparency which requires the contracting authority to insure that it has complied with such transparency obligations.(10) The SCJEU of 13 November 2005, *Parking Brixen*, C-458/03, affirmed that the obligation of transparency that relapses on the above mentioned authority, consists on guaranteeing, for the benefit of potential tenderers, a suitable advertising that promotes open competition the concession of services, and to ensure the impartiality of the procedures of adjudication. Meanwhile, in the *CAS Succhi di Frutta S.p.A.* SCJEU, held that this principle is essentially intended to minimize the risk of favoritism or arbitrariness on the part of the contracting authority, implying “*all the conditions and detailed rules of the award procedure must be drawn up in a clear, precise and unequivocal manner in the notice or contract documents so that, first, all reasonably informed tenderers exercising ordinary care can understand their exact significance and interpret*

(6) ECJ, 3 December 2001, *Bent Moustén Vestmgaard*, in Case C-59-00, par. 20.

(7) J. A. MORENO MOLINA, *Los principios generales de la contratación de las Administraciones Públicas*, Editorial Bomarzo, Albacete, 2006, 33 - 43.

(8) ECJ, 27 November 2001, *Lombardini v Mantovani*, in joined Case C-285/99 and C-286/99; ECJ, 19 June 2003, *Gesellschaft für Abfallentsorgungs-Technik GmbH (GAT)*, in Case C-315/01, and ECJ, 20 December 2005, *Comisión v. France*, in Case C-264/03.

(9) ECJ, 29 April 2004, *CAS Succhi di Frutta S.p. A. v. Comisión*, in Case C-496/99P, par. 110.

(10) ECJ 18 November 1999, *Unitron Scandinavia*, in Case C-275/98, par. 31.

*them in the same way and, secondly, the contracting authority is able to ascertain whether the tenders submitted satisfy the criteria applying to the relevant contract.”*

We have to give special emphasis to the limitation on actions of the contracting authorities concerned. Those who favor the contractor without cause. Those decisions taken, for example, to modify a contract, or act in a manner that enables the contractor to unjustly enrich itself.

However, nothing will change unless you address the entire structure. The study of European legislation so far shows that contractual changes occur now as they have in the past. Nothing changes. See for example “Vauban’s letter” of July 7, 1683. Sébastien Le Prestre, Marquis de Vauban (1633 - 1701) Military Engineer Marshal of France, addressed this letter to François Michel Le Tellier, Marquis de Louvois (1641 - 1691) – War minister of Louis XIV (1638 - 1715) and told:

*“There are some jobs in recent years who have not completed, and that will not be completed, and all that, Monsignor, the confusion caused by the frequent sales that are made in their works, what does not serve to attract more than as contractors to the miserable, crooks and ignorant, and drive away those who are able to lead a company. I say more, and they delayed and considerably more expensive works, because these reductions and economies as sought are imaginary, and what a contractor who loses makes is the same as a drowning drowning: hold on to everything, in the office of the contractor is unable to pay suppliers, to low-wage workers make worse, cheat on everything and always ask for mercy against this and that. And from there ... pretty Monsignor, to make him see the imperfection of such conduct; leave it entirely, then, and in the name of God, restore good faith works to commission a contractor to do his will always be the cheapest solution that you can find duty.”*

The same is happening today.

The above discussion highlights the importance of analyzing the judicial pronouncements that constitute a genuine European law on amendments to the contract and these should be used to interpret the events related to the execution of the contract in all member States, resolving any doubts that might exist in favour of the greater range of principles that should govern the contract modifications.

### ***3. The case-law of Court of Justice of the European Union as impacting the right of contract modifications***

#### **3.1. Introduction**

The impact of the the European rights regarding modifications of a contract can be seen when these produce a substantially different contract. We have what we might describe as extinctive novation of the contract (opposite to the modificative novation of the contract). It would be a question of modifications

so significant that they substantially alter the initial tender and contract formation, adversely impacting the efforts at nondiscrimination and the free movement of services.<sup>(11)</sup> This, in addition to the economic impact, are contract amendments. The question is whether the new guidelines will result in the disappearance of the principle of mutability of the contract. Predicting the future, the answer will likely be negative. In Spain there has been a substantial change in terms of contract amendments (in Spain modifications limit is 10%). The percentages have declined. But those who live not only in the theoretical world of recruitment note that this scenario is unrealistic. The changes are now masked in units of work that no proceedings shall be replaced by others without shaping it until the contractual settlement phase where all the problems resurface. When reaching a contractual settlement it seems that everything is perfect. However, when the contract is closed all the problems begin to emerge. The solution is to strictly apply the jurisprudence of the CJEU and meet the principles of integrity and transparency.

Four CJEU cases have had a decisive influence on the construction of these serious limitations on amendments to the contract, or more specifically to the indiscriminate use of it. The CJEU judgment of 29 April 2004, *Commission v Succhi di Frutta SpA*, 19 June 2008 *Presstext Nachrichtenagentur GmbH v Republik Österreich* and others, or 22 April 2010 *Commission v Kingdom of Spain*, among other (from 13 January 2005, *Commission v Spain*, 13 September 2007, *Commission v Italy*, of 15 October 2009 *Acoset* and of 29 April 2010 *Commission v Germany*). Also the judgment of the General Court of 31 January 2013 has served to bring together all the previous statements on the subject.

### 3.2. The Judgement of the CJEU 29 April 2004, *Commission v CAS Succhi di Frutta S.p.A.*

The judgment of the CJEU of 29 April 2004, *Commission v CAS Succhi di Frutta SpA* defined budgets amendments to contracts and generally concluded that modification of the payment would infringe the principles of equal treatment and transparency.<sup>(12)</sup>

The Commission organized a tender to buy fruit juices and jams for the people of Armenia and Azerbaijan. It was expected that the the contractors would be paid in kind, and more specifically, with two fruits (apples and

(11) ECJ, 11 January 2005, *Stadt Halle y*, in Case C-26/03, par. 44; ECJ, 18 November 1999, *Unitron Scandinavia*, in Case C-275/98, par. 31; ECJ 7 December 2000, *Telaustria*, in Case C-324/98, par. 60 - 61, and ECJ, 29 April 2004, *CAS Succhi di Frutta S.p.A. v. Comisión*, in Case C-496/99P, par. 108-109.

(12) See F. J. VÁZQUEZ MATILLA, *La modificación de los contratos administrativos: reflexiones en torno a la STJCE de 29 de abril de 2004 y la Ley de Contratos del Sector Público*, in *Revista Española de Derecho Administrativo*, Núm. 143, 2009, 529-564.

oranges). After formalizing the contract, the Commission said that the quantities of the products had been recalled so far, and they were insignificant in relation to the quantities needed, even though the recall had almost finished, so therefore they considered it necessary to satisfy tenderers who wish to accept the payment, instead of apples and oranges, other products such as nectarines and peaches, creating from scratch a percentage of the equivalence.

Therefore, the company *Succhi di Frutta*, an unsuccessful tenderer that did not appeal the award of the contract, brought an action for annulment of Decision for amendments in question at the court of first instance – henceforth CFI – arguing that the Commission had violated the principles of equal treatment and transparency, among others issues. In those proceedings the Commission argued that the appeal should be declared inadmissible or alternatively dismissed, by the double reason that the applicant was not directly and individually affected by the change to the contract and had no interest in obtaining its annulment. In addition, she argued that the replacement, after the award of the fruits to be obtained as payment is in no way a violation of the principles of equal treatment and transparency, since there is no influence on the development of the tender procedure, since that replacement of the fruits that are produced after the award, which it has no influence on the development of the operation.

The Judgement of CFI (Second Chamber) of 14 October 1999 (Joined Cases T-191/96 and T-10), *CAS Succhi di Frutta SpA / Comission*, estimates the resource. He declared that there had been a infringement of the principles referred. After that, the Commission appealed against the SCFI.

The CJEU confirmed the judgment, that annulled the contested decision based on the fact that “*when a contracting authority had laid down prescriptive requirements in the contract documents, observance of the principle of equal treatment of tenderers required that all the tenders must comply with them so as to ensure objective comparison of the tenders*”,<sup>(13)</sup> and also the procedure for comparing tenders has to comply at every stage with both the principle of the equal treatment of tenderers and the principle of transparency so as to afford equality of opportunity to all tenderers when formulating their tenders.<sup>(14)</sup>

In this way, as the notice did not foresee the replacement of apples or oranges for peaches in payment of supplies, or the establishment of equivalence between these fruits for the winners (*Trento Frutta* and *Loma*), this is an important amendment an essential condition of a contract notice, in particular the arrangements for payment of the products to be supplied, so that the amendment is contrary to law by violating the principles of equal treatment

(13) ECJ 22 June 1993, *Commission v Denmark*, in Case C-243/89 ECR I-3353, par. 37; ECJ 22 April 1994, *Commission v Belgium*, in Case C-87/94, ECR I-2043, par. 70.

(14) ECJ 22 April 1994, *Commission v Belgium*, in Case C-87/94, par. 54.

and transparency obligation due.<sup>(15)</sup> The Court emphasized in this regard that the Commission should respect the criteria she had established in the notice in the contract terms, not only during the tendering process itself, which concerns the evaluation of tenders and selection of contractor but also, more generally, until the completion of the execution phase of the contract in question.

In addition, the decision stated that although an offer that does not comply with the terms must be clearly ruled out, the contracting entity was not authorized to alter the overall system of the bid unilaterally modifying one of the essential conditions after the contract was formalized; including a provision that, had it been included in the notice, would have allowed for tenderers to submit an offer substantially different.

The Court concluded that the contracting authority could not, after the award of a contract and also, by a decision whose content repealing the stipulations of earlier regulations, amend a significant condition of the tender, such as that relating to the arrangements for payment of products to be supplied.

In regard to the setting of the doctrine to be used to interpret the mode of making such modifications, the decision confirmed that:

*“should the contracting authority wish, for specific reasons, to be able to amend some conditions of the invitation to tender, after the successful tenderer has been selected, it is required expressly to provide for that possibility, as well as for the relevant detailed rules, in the notice of invitation to tender which has been drawn up by the authority itself and defines the framework within which the procedure must be carried out, so that all the undertakings interested in taking part in the procurement procedure are aware of that possibility from the outset and are therefore on an equal footing when formulating their respective tenders.”*

Moreover, there are cases that do not expressly provide for the possibility noted above, but the contracting authority nevertheless intends to disengage from one of the essential procedures that are provided during the tender period. After the award of the contract, the authority cannot validly apply dissimilar conditions to those imposed initially. In these cases, I estimate that if the proper procedure was not followed for the award, the authority must offer a new period for submission of bids. Conversely, if it has been awarded, the contract would be resolved.

The Court stated that:

*“where there was no express authorisation to that effect in the relevant provisions, the contracting authority could not, once the contract had been awarded and, moreover, by a decision which derogates in its substance from the provisions of the*

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(15) Around the obligation of the contracting authority of transparency in the tendering and subsequent execution of the contract the Court referred to the ECJ 18 June 2002, *Hospital Ingenieure Krankenhausstechnik Planungs-Gesellschaft mbH (HI) v Stadt Wien*, in Case C-92/00, ECR I-5553, par. 45, and ECJ 11 December 2002, *Universale-Bau*, in Case C-470/99, ECR I-11617, par. 91.

*earlier regulations, amend a significant condition of the invitation to tender, such as the condition relating to the arrangements governing payment for the products to be supplied, without distorting the terms governing the award of the contract, as originally laid down. Furthermore, a practice of that kind would inevitably lead to infringement of the principles of transparency and equal treatment as between tenderers since the uniform application of the conditions of the invitation to tender and the objectivity of the procedure would no longer be guaranteed.”*

Also reiterated in the absence of express provision to that effect in the notice, the contracting authority is prohibited from modifying, at any stage of the procedure, conditions of tender, as this would undermine the principle of equal treatment among all tenderers as well as principle of transparency.

The doctrine proclaimed by this judgment was used by the European Commission to require Spain to bring its codes to what I call the European law of contract amendments. That became the enactment of Law 2/2011, of March 4, Sustainable Economy. This has resulted in the public procurement rules a title V dedicated exclusively to this institution, unrelated to the title on the contract. The reform is more stringent than has existed in Spain in this matter. In summary, the rule provides that only if there is express provision in the contract documents in a clear, precise and unambiguous contract, it can be modified. Also it is expected that in the absence of such a contract provision, a contract may be modified if certain circumstances exist, provided that the change results in no more than a 10% increase or decrease in the price of contract award.<sup>(16)</sup>

### 3.3. The Judgment of the CJEU of 19 June presstext Nachrichtenagentur GmbH v Republik Österreich, APA-OTS Originaltext – Service GmbH, APA Austria Presse Agentur registrierte Genossenschaft mit beschränkter Haftung

At the request of the Austrian Bundesvergabeamt, the Court clarified an extensive catalog of questions on the interpretation of various provisions of Community law on public procurement award concept. In particular, the Court clarified under which conditions the modification of an existing contract should be considered a new contract. The background of the preliminary ruling results from a bitter dispute over the provision of news agency services to the Austrian federal

(16) See F. J. VÁZQUEZ MATILLA, *Nuevo régimen jurídico para las modificaciones de los contratos públicos: proyecto de ley de economía sostenible*, in *Revista Aragonesa de Administración Pública*, 2010, Nº 37, 348 and following, and ID., *Transformación sustancial del régimen de modificación del contrato por la Ley de Economía Sostenible*, in *Contratación administrativa práctica: revista de la contratación administrativa y de los contratistas*, 2011, Nº. 114, 46-57. See too J. M. GIMENO FELIU, *Las reformas legales de la Ley 30/2007, de Contratos del Sector Público, Alcance y efectos prácticos*, Thomson Reuters, 2011, Cizur Menor (Navarra), 109. J. COLAS TENAS, *La reforma de la legislación de contratos del sector público en la ley de economía sostenible: el régimen de modificación de los contratos del sector público*, in *Boletín Derecho Local*, 1st June 2011.

authorities, where Nachrichtenagentur, took legal action against the traditional contractual relationships existing between the Republic of Austria and Austria Presse Agentur (APA). These were long-term relationships that were subject to amendment in 2000, 2001 and 2005. The dispute arose in part by the fact that in 1994 the Republik Österreich (Bund) entered into a contract with the APA, which provides for the provision of certain services in exchange for payment. Years later APA founded the limited company APA OTS, a subsidiary of which owns 100% of the shares. Both companies agreed to a of transfer income, existing control by APA, where APA received the annual profits of the new society, and also covered the losses. In addition, APA informed the contracting authority that it was jointly and severally liable with APA-OTS under the contract, and that nothing would change in service development. The Austrian authorities gave their consent for the OTS service provided by APA-OTS. In addition, the contract was subsequently amended upon introduction of the euro.

PN (a company operating in the same sector) asked the Bundesvergabeamt to review the contract, stating that the division of the framework contract following the restructuring of APA in 2000, resulted in unlawful “*de facto* awards”. In the alternative, it argued that the choice of various procedures for the award in question were illegal. In these circumstances, the Bundesvergabeamt decided to stay proceedings and refer the Court to seven questions, although the Tribunal considered only 4. Here we analyze only the first, which inquired whether “Is the term” award “in the sense that it includes cases where the contracting authority plans to get in the future performance of a company that takes the form of a capital company. If these services were previously provided by another supplier, on the one hand, the only company in the future could be the partner that provides services and, secondly, it controls through manual? And if in such a case, is it relevant legal contracting entity has no assurance that the shares in the company’s future lending are not transmitted in whole or in part to third parties during the entire validity period of the original contract and does not rest assured that the shareholding of the company providing the service, which originally took the form of cooperative, not transformed during the entire validity period of the contract?”

The Court stated that to ensure transparency of procedures and equal treatment of tenderers, amendments to the provisions of a public contract during its validity constitute a new award if they have characteristics which differ from those of the original contract. Therefore, the Court looked for evidence indicating the willingness of the parties to renegotiate the essential aspects of the contract.<sup>(17)</sup>

Similarly, the Opinion of Advocate General Juliane Kokott, March 13, 2008 to this issue argued in principle, that subsequent amendments to the

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(17) ECJ 5 October 2000, *Commission v France*, in Case C-337/98, par. 44 - 46.

contents of existing contracts *may* satisfy the elements for the award of a public contract, thus requiring a new award. However, she concluded that not all minor changes on public services require a prior adjudication. Specifically, she stated that only material changes to the contract, in particular those that distort competition in the market and give preference to domestic suppliers of services, warrant conducting a new procurement procedure. A fundamental change is presumed to exist when it would have impacted the original competition, such as deterring other service providers from bidding, or where the new contract terms may encourage new tenderers to participate in the tender process, or where a previously ineligible bidder could now participate.

In the same sense, the Court stated that the modification of an initial contract may be considered substantial if it extends the contract, including the addition of services not required initially; alluding to the possibility that a new award should be made when an authority seeks additional services not included in an initial contract. She also stressed that a change can also be considered substantial if it changes the economic balance of the contract in favour of the contractor in a manner that was not foreseen in the original contract terms.

The judgment is of great importance because the article of Directive 2014/24/EU 72.1.d.3 eliminates the possibility of transfer of the contract. We believe that the fundamental support of this contention lies precisely in this statement, as we conclude that:

*“In general, it should be noted that the introduction of a new contractor to replace the one to which the contracting authority had initially awarded the contract constitutes a change of one of the essential terms of the contract in question, unless this substitution was under the terms of the initial contract, for example, as a subcontractor.”* (18)

### 3.4. The judgement of 13 april 2010 Wall AG contra La ville de Francfort-sur-le-Main y Frankfurter Entsorgungs- und Service (FES) GmbH y Otros

On December 18, 2002 the municipality of Frankfurt made a call for submission of applications to participate in a tender for a concession contract for services relating to the operation, maintenance and cleaning of eleven

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(18) This is without prejudice to the specific case, as APA-OTS was a 100% subsidiary of APA, and the latter had a power of direction over APA-OTS and as there was between these two entities a transfer agreement losses and benefits, which assumes APA, and the fact of the existence of joint and several liability with APA-OTS and that nothing would change in the provision of existing set, changing the subject was not an essential modification of the contract as stated by the CJEU. However the Court stated bluntly that If the shares in APA-OTS were transferred to a third party during the term of the contract at issue in the present case, no longer would be an internal reorganization of the initial contract elsewhere but an effective exchange of contracting party, which would in principle the change of an essential term of contract. This could constitute a new award of the contract.

urban public lavatories over sixteen years. The tenderers included Wall and Frankfurter Entsorgungs- und Service GmbH (FES). The contract was awarded to FES, with Wall serving as a subcontractor to FES. A clause in contract provided that Wall was the subcontractor of FES for the advertising services covered by the concession. The clause further provided that a change of subcontractor was allowed only with the written consent of the City of Frankfurt.

During the execution of the contract FES sought offers for the advertising services under the concession contract. FES subsequently awarded the advertising services to Deutsche Städte Medien GmbH (DSM). FES then sought permission from the City of Frankfurt to change subcontractors, from Wall to DSM, so that those public lavatories could be supplied by companies other than Wall. Wall brought an action before the regional court in Frankfurt, seeking to prevent FES from entering a contract with DSM for the advertising services and to prevent it from entering any contract with a third party for the construction of the new public lavatories.

In the alternative, Wall sought an order for the city of Frankfurt and FES to, jointly and severally, pay it the amount of EUR 1,038,682.18, plus interest, which was the amount initially committed by FES.

The regional Court then stayed the proceedings and sought a preliminary ruling from the European Court on a series of questions, including whether the principles of equal treatment and non discrimination on grounds of nationality, as well as the obligation of transparency arising therefrom, require calling a new tender when the contract is amended by replacing a subcontractor.

After clarifying that service contracts are not governed by the directives referred to public authorities that hold such contracts they are obliged to respect the fundamental rules of the Treaty and the obligations of transparency derives from them, the same way as and determines that *“a change of subcontractor, even when doing so is contemplated in the contract may, in exceptional cases, such changes constitute one of the essential elements of the concession contract, given the characteristics of the benefit at concerned, the recourse to a subcontractor rather than another has been a key element of the contract, which, in any case for the national court.”* In making its assessment, the referring court inferred that if the proposed subcontractor was a decisive factor in the original award decision, a subsequent change in subcontractors may constitute a change in one of the essential elements of the concession contract. Therefore, to restore transparency to the contract, a new award procedure may be required. This provides further support for the elimination of the power to transfer the contract and the impossibility of replacing certain subcontractors.

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### 3.5. The SCJEU of 22 April 2010 Commission v Kingdom of Spain, among others

The Spanish Ministry of Public Works began a procedure to award a public works concession for the construction, maintenance and operation of the connections section of a toll motorway A-6 between the cities of Avila and Segovia. The work also included construction of the bypass around the town of Guadarrama, a municipality located in the stretch of toll highway A-6, and finally, the expansion of part of the free section of the A-6, specifically the section between Madrid and Villalba. This included construction of a fourth lane in each direction to increase the capacity of the A-6 in the section above.

This contract was never awarded but by order of 7 July 1999 a new tender similar to the first was issued without referencing the object of the initial concession for the construction of the Guadarrama bypass or enlargement of a portion of the section Free the A-6. Points 13 and 16 of Clause 5 of this tender, which included the same language from the first statement, provided:

*“Tenderers expressly manifest in their tenders the measures they intend to take in relation to the effects of the grant on overall network traffic, area attractions and assessment of monuments of historical or artistic, as well as those on conservation and landscape maintenance and defense of nature, all regardless of compliance with existing regulations in these matters. « and that » the tenderer shall describe the measures to be proposed by the administration to take adequate intercity traffic management area affected by the construction of roads to the award, including the meaning of the bidder agrees to carry out their charge. Creativity and feasibility of these considerations will be positively valued in the award of the competition, given the high level of congestion in areas where traffic will affect the way under the license.”*

The concession was awarded to Iberpistas who had proposed a number of improvements in addition to those works mentioned in the second tender statement (construction of a third lane in each direction on the stretch of toll highway a-6 located between Villalba and the Valley of the Fallen link, construction of a third reversible lane on the stretch of toll highway A-6 located between the Valley of the Fallen link and the town of San Rafael, including the construction of a new tunnel, and finally the construction of a fourth lane in each direction on the free section of toll motorway A-6, in the portion between Madrid and Villalba). The last work mentioned was quoted in the first specification (the one that was never awarded) but not in the second statement governing the award.

The Commission brought an appeal alleging the specifications of the concession as described in the notice and the contract documents, as well as the works actually awarded, must always match. Neither the statement nor the advertisement mentioned the additional works proposed by Iberpistas. The Commission thus

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objected to the subsequently expanded work under the concession contract awarded to Iberpistas. In particular, the Commission argued that the additional work proposed by Iberpistas had not been published in the tender and was located outside the geographical area covered by the object of the concession, as published. The Commission further stated that neither the change in the subject of the concession introduced in the second announcement nor the second statement would allow reasonably informed and diligent tenderers to expect that they could propose such a set of expanded work. In fact, if the authorities invited a tenderer to make proposals that would lead the performance of work as additional works, considering that if it were otherwise, it must be assumed that bidders could propose works on all roads in other provinces where traffic could be affected by the works under the license.

The Court of Justice confirmed the importance of advertisements and tender documents, stating that they “*must have a clear wording to all potential tenderers, experienced and well informed and reasonably diligent, have a chance to get a concrete idea of the works to be performed, and their location, and to make your offer accordingly*”. Thus, the notice must include both the main subject of the contract additional objects, including the description and location of the works of the grant, and the amount or scope thereof. This disclosure, because it facilitates a meaningful comparison of offers, guarantees the existence of an adequate level of concurrency. Concluding that the additional works were awarded to Iberpistas although they were not within the purpose of the grant in question, with appropriate publicity required of them as an expression of the principles of equal treatment and transparency.

### 3.6. The SCJEU of 31 January 2013 Commission v Kingdom of Spain

The Judgment of the General Court (Eighth Chamber) of 31 January 2013 (Case 235/11) addressed an appeal of the Kingdom of Spain seeking the annulment of Commission Decision C 20111-1023, February 18, 2011 that reduced the amount of assistance provided under the Cohesion Fund for various projects relating to the execution of certain high-speed railway lines in Spain. This dispute involved Directive 93/38, which Spain asserted, does not regulate the modification of contracts but, merely regulates the bidding and award phase. The Court notes that Article 20 of Directive 93/38 addresses the issue of additional deliveries and permits the use of a procedure without prior call for competition for works or additional works not included in the project initially awarded or in the contract first concluded that, due to unforeseen circumstances, become necessary for the performance of the contract, provided that award to the contractor or service provider executing the original contract

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is made. Such noncompetitive procedures are also permitted whenever such additional works or services can not be technically or economically separated from the main contract without serious inconvenience for the contracting entities; or when such additional works or services, although separable from the performance of the original contract, are strictly necessary for its completion.

The Commission found several irregularities affecting the projects supported a reduction in the funds originally provided. The Commission understood that the Directive applied to amendments of contracts the provision of the Directive on supplementary contracts. The Kingdom of Spain argued that no additional benefits were hired but only some elements of the contract were altered, and that no new features, different from those initially recruited, were included in the contract modifications. The Kingdom of Spain argued therefore that the rule does not apply “*to regulate exclusively the award phase of the contract, refers only to the hiring of additional benefits, but not to the modification of contracts*”. The Court emphasized that the principle of equal treatment is a primary objective of the directives in the award of public contracts and implies an obligation of transparency which ensures compliance.

The Court noted the Judgment of the Court of 29 April 2004, Commission/CAS Succhi di Frutta, which discussed the award of outstanding new work to the initial contractor. All this on the basis of the principle of equal treatment implies an obligation of transparency which ensures compliance; that aims to promote the development of healthy and effective competition between companies involved in public procurement, requiring that all bidders have equal opportunity in formulating the terms of their offers and it implies that they undergo the same conditions for all competitors under the scope of Article 20 of the Directive governing ancillary contracts.

However, the Court did not consider whether there is difference between a complementary contract and a contract amendment. Instead, the Court simply stated that additional works legislation applies to contractual changes, despite the argument put forth by the Kingdom of Spain. Work performed, is thus again clearly classified as a modification of a contractual agreement.

The Court restates, the discussion in STJUE of April 29, 2004, Commission/CAS Succhi di Frutta that “if the contractor was authorized to modify at will, during the execution of the contract, the very conditions of tender without the relevant provisions express authorization to that effect, the terms of the award of the contract, as originally stipulated, would be distorted”.

In the absence of directives that limits the contractual changes this institution is directly related to the awards without advertising as regulated by Directive 93/38 and in particular to additional works. This seems questionable, though, the truth is that what matters in particular precept is the need to justify the unpredictability of contract modifications.

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The Court criticized the Spanish legislation allowing modification by new needs ... “using a criterion on the assessment of the existence of new requirements allow the contractor to modify at will, during the execution of the contract, the very conditions of the tender”.

#### **4. Contractual modifications in the new public procurement directives**

The Green Paper on the modernization of public procurement policy of the EU towards a European market for more efficient public procurement (COM (2011) 15 final) was published on January 27, 2011. With it launched a broad public consultation on legislative changes that could be introduced to facilitate and streamline the procurement and enable better use of public procurement in support of other policies. It considered the issue of modifications “*particularly complex*” and relying entirely on the case-law on the subject of CJEU generalized to the fact that:

*“any amendment to the provisions of a contract during its validity requires a new award procedure, entering substantial differences with the original contract”.* Specifically questioned “*if necessary legal clarification at European Union level to establish the conditions under which the modification of a contract requires a new procedure for the award.*”

This clarification could also refer to the possible implications of the changes (for example, provide a simpler procurement process for tendering the contract modified).<sup>(19)</sup> Following the Green Paper came a Proposal for a Directive of

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(19) Questions 39 and 40. “39. Should public procurement directives regulate the issue of substantial modifications of a contract during its validity period? If so, what elements of clarification propose? 40. When you need to organize a new tender procedure following the modification of one or more essential terms, would you be justified in applying a more flexible? What procedure would be?”. Of particular interest are the contributions made by members of the research project researchers on New Scenarios procurement, quoted in this work, in addition to the advertising of the Commission were reproduced in J. M. GIMENO FELIU (Director) – M. A. BERNAL BLAY (Coordinator), *Procurement Observatory*, 2010, Editorial Aranzadi SA (Cizur Menor, Navarre), 2011, 461 to 515, in response to them had the opportunity to reiterate the need for the Directive regulates to amendments to a contract and that there are limits to it. In response to the same had the opportunity to reiterate the need for the Directive regulates to amendments to a contract and that there are limits to it. Affirming that should be pointed out that: “1. – You can modify a contract when unforeseen or unexpected circumstances for a contracting diligent, reasonable and sensible for the traffic sector of social life or qualified by the kind of activity to try and not affect the essential conditions. 2. – The amendments to the contract limit can not exceed 50% (current limit of Article 31 of Directive 2004/18). 3. – In the case that from the beginning it is known that the contract could be affected by various circumstances, must be established that the forecast to make changes to the contract and the conditions upon which may be held must be not generically but identified the assumptions accurately, clearly and unequivocally, integrating, where appropriate, the estimated contract value the amount of possible variations of the contract from the start. 4. – Should clarify whether it is possible that the contractor transfers the contract to a third party (ECJ, *Pressetext Nachrichtenagentur GMBH*, cit.). 5. – Must be specified that the amendments should respect the general principles of public procurement, so that their violation is considered unlawful award a new zero. 6. – It seems necessary to clarify in this Paragraph that despite the provision not in the terms and conditions of the possibility of modification in certain circumstances, as stated, provided that the amendment does not

the European Parliament and of the Council on public procurement {SEC(2011) 1585}{SEC(2011) 1586}, with Chapter IV devoted to the contract and in particular Article 72 dedicated to the regulation of contract modifications.

New directives and in particular Directive 2014/24/EU (the remaining two did not differ from the regulation of this new classic Directive) makes a complete system of contractual modifications. Under Title II of the Directive, entitled “Rules applicable to contracts” may find Chapter IV “performance of the contract”. This chapter consists of 4 items. Article 70 dedicated to the execution conditions of the contract, 71 outsourcing, Amendment 72 to the contract during its term and 73 to the termination of contracts.

Paragraph 1 of Article 72 is devoted to cases where the contract amendment is possible. It begins by stating that in any of these assumptions can be modified analyzing the contract and framework agreements without starting a new procurement procedure. The first one is constituted by the “modified under the original contract”. The first feature and novelty of this type is a modified Directive that allows their introduction regardless of their monetary value. This does not seem very appropriate. For more than specified in the contract a significant change from the quantitative point of view creates a separate contract. In defense of the rule it should be noted that a limit that affects the issue discussed is imposed. It is impossible to establish modifications or options that would alter the overall nature of the contract or framework agreement. The provision requires that modifications expected to be carried out by the provision be described in the specifications in a clear, precise and unambiguous language. What are generic terms will not fit. In short, it is probably not possible to include such language in the modified contract except when there is sufficient evidence to consider what may occur and what the parties do not have, it is necessary to specify the conditions under which they can be used. The provision gives the example of planned price changes, revisions and options.

The second situation is the additional contracts. In the proposed directive it had been removed. Please note that we are facing unique circumstances provided for in (the latest in Article 31 of Directive 2004/18) previous directives. For this reason many states felt that it was not necessary to make a new

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*affect any essential | important for the bidding and attend an unforeseeable modification is potentially viable if it does not affect an essential condition. (ECJ, CAS Succhi di Frutta Spa, cit.) 7. – It should be clarified in which cases (causes) a contract can be modified so that operators can identify them. For example, new requirements can not enable to modify a contract, but other circumstances arising out of the contract that affect it and determine impossible to continue with its execution in the manner prescribed, provided this is not attributable to the contracting authority, otherwise they could hide anti-competitive practices.”* My other contributions to the Green Paper consultation can be viewed on the website of the European Commission: [https://circabc.europa.eu/d/d/workspace/SpacesStore/8ecfbbd-7020-4a40-b5c4-06c9804fe796/vazquez\\_en.pdf](https://circabc.europa.eu/d/d/workspace/SpacesStore/8ecfbbd-7020-4a40-b5c4-06c9804fe796/vazquez_en.pdf).

regulation, contract modifications, and in the same direction, the General Court of the European Union, applied in its judgment of 31 January 2013 against the Kingdom of Spain. During the legislative process it was incorporated with the usual wording. While explicitly specifying the need is not feasible for a separate procurement and should not be a mere convenience, the limit of its use to 50% of the contract award value should be retained.

Most striking is the course which is relevant to unforeseen changes. While it is necessary to be able to modify the contract in such cases the legislation for the Kingdom of Spain include a surprising limitation of 10% (originally 20%) given that the Directive now allows unforeseen changes up to 50% for unpredictable circumstances and the global nature of the contract is not considered to be altered.

The provision requires to be published in the OJEU procurement complementary (works, services or additional supplies) and modifications “not provided”. This notice shall contain the information set out in Annex V, Part G of the Directive, and published in accordance with Article 51 thereof.

Another supposed modification is allowed on the replacement of the contractor, but with many restrictions. As we have already anticipated, we have a substantial alteration of the legal tradition where the assignment has been a rule. But remember that it is not new. Now only the changes from corporate reorganizations, in a situation of insolvency (bankruptcy) will be allowed, or a clause in the original tender will be allowed. Interestingly, also the approach that the Administration is subrogated to the position of the prime contractor to ensure the continuity of contracts with subcontractors.

This will host the premises of ECJ of 19 June 2008, *Pressetext Nachrichtenagentur GmbH*) claimed to remember:<sup>(20)</sup>

*“In general, it should be noted that the introduction of a new contracting party in place of that to which the contracting authority had initially awarded the contract constitutes a change of one of the essential terms of the contract in question, unless this substitution was provided in the terms of the initial contract, for example, as a subcontractor”* and concluded that *“If the share capital of APA-OTS were transferred to a third party during the term of the contract at issue in the present case, no longer would be an internal reorganization of the initial contract elsewhere, but an effective exchange of contracting party, which would in principle the change of an essential term of contract. This could constitute a new award of the contract.”*

No substantial changes are allowed without verifying whether the requirements are met regarding unpredictability to certain percentages. This seems totally inappropriate, considering to be transposed with nuances. The

<sup>(20)</sup> What's more the aforementioned safeguards appears to make reference to cases in which is possible substitution of subcontractors referred to the judgment of 13 April 2010 against *The Wall AG Frankfurt ville-sur-le-Main* and *Frankfurter Entsorgungs- und-Service (FES) GmbH*.

unpredictability should be required regardless of the nature or amount of the modification. The amendment must be below the thresholds that would subject the contract to the board and bottom, too, 10% of the initial value of the contract in the case of contracts for services or supplies, and 15% of the value of the initial contract the case of works contracts. All with the prohibition of alteration of the global nature of the contract or framework agreement, and taking into account that if they are successive, the value is calculated on the basis of the cumulative net value subsequent modifications.

Paragraph 4 of Article 72 determines when we are facing changes that involve a substantial alteration of the original contract. The first key to verify are the facts that the Directive considers for the amendment to result in a contract or agreement that is materially different from the originally held. This is what could be defined as alteration of the global nature of the contract. However, after this Directive the following generic description of various circumstances that are met individually or together constitute a substantial alteration of the contract:

- a) the modification introduces conditions which, had figured in the initial procurement procedure, would have allowed the selection of candidates other than those initially selected or accepting a different offer to the initially accepted or have attracted more participants in the process recruitment;
- b) the modification changes the economic balance of the contract or framework agreement to the contractor in a way that was not foreseen in the initial framework contract or agreement;
- c) the modification extends significantly the scope of the contract or framework agreement;
- d) the contractor awarded initially designated by the contracting authority is replaced by a new contractor in circumstances other than those provided for in paragraph 1, letter d). As can be seen, the Directive establishes, correctly, the doctrine of the ECJ as to the substantial alteration refers contemplating each of the cases we have studied in this chapter.

Moreover, there are some issues to keep in mind as the calculation of the hammer price for calculating the percentage that constitutes a substantial alteration. In this regard, Article 72.3 determines that it must take into account the updated price will be the reference value if the contract includes a clause indexing.

For any changes not authorized by the Directive, commencing a new procurement procedure in accordance with the Directive is required. This is what is intended to avoid putting the same contractor directly, requiring a new procedure with all the guarantees and with respect to the guiding principles of public procurement.

Indeed, Article 73 of the Directive addresses the termination of contracts, including as a first course, whether the contract has undergone a substantial change, which would have required a new procurement procedure under Article 72.

### **5. The contract modifications, a barrier to integrity and efficiency of public procurement**

Public procurement has been identified as one of the governmental activities most vulnerable to corruption.<sup>(21)</sup> A contract that is repeatedly amended is a contract lacking integrity due to the general public. The risk of favoritism to the contractor, who rarely questions a modification is not only a moral hazard. Total rupture of the tender which was the basis for choosing the best deal is patent. In this sense, as pointed out by Tina Søreide:

*“One explanation may be the incentives of the contractor to manipulate decisions regarding modifications or additions to the original project, as this kind of work usually increases the enterprise profits (also when rates for supplementary works are contractual). Hence, inadequacy among public officials in charge of the project can be misused by the executing enterprise. The enterprise ability to understand deficiencies of the initial project and to forecast the nature and dimension of the changes may thus become important to win public procurement contracts in general. Bribes are paid in this context to obtain promises of changes and additions of the work, so that the enterprise can win the bid with an inferior offer.”*<sup>(22)</sup>

Avoid in short, the free favoring of the contractor against the remaining bidders. Only then will the authority obtain an offer that is the most efficient. Otherwise, as we have said, such action will not help the bidding process, which will be totally distorted.

Prof. Racca considered in this respect that:

*“Fair and open competition must be assured to every bidder, to get the evaluation of his offer in accordance with the award criteria. This right does not end with the award procedure but must be safeguarded in the execution. Changing the award conditions When this does not happen, the competition principle is undermined because the awardee’s lower-than-promised performance makes it as if the procuring entity failed to choose the best tender. Such low quality performance can cover a corrupt agreement too. The role of the losing bidder can be fundamental in*

<sup>(21)</sup> See OECD, *Integrity in public procurement*, 2009, 3; Transparency International – the global coalition against corruption, *Handbook for Curbing Corruption in Public Procurement*, 2006, [www.transparency.org/global\\_priorities/public\\_contracting/tools\\_public\\_contracting](http://www.transparency.org/global_priorities/public_contracting/tools_public_contracting), 13.

<sup>(22)</sup> T. SØREIDE, *Corruption in public procurement Causes, consequences and cures*, Chr. Michelsen Institute Development Studies and Human Rights, Norway, 2002, 16. In the same sense see J. CIBINIC – R. C. NASH – J. F. NAGLE, *Administration of Government Contracts*, The George Washington University Law School, Washington, Wolters Kluwers, 2006, 298 – 310.

*preventing corruption because of their deep knowledge of the object of the contract and of the winning conditions.”* (23)

The problem, as we have come to see, is that the principles that are used for bidding must be present for the other modes. (24)

In different countries, and in the example here noted, in the Spanish case, corruption in contract modifications is patent. In particular, the Court of Accounts of Spain, 942 in its report devoted to “*Audit of recruitment held in 2008 by the State Public Sector Entities subject to the laws of the government contracts*” has shown the existence of a high degree of corruption in public procurement in different Spanish regions. As an example the Court calls “*strange economic downturns*” existing in many tenders, where even the price was valued, but instead there was a high level of modifications of the contract price under implementation.

If not for the existence of corruption it is not understood as the contracting authority can, too often, further amend the contract to the benefit of contractor. An everyday example is the modification of the proposed works (with or without translation into the contract dossier) to “*relieve*” or make things easier during implementation. In particular, we see modifications of the construction processes, the materials used, the quality of supplies – which are intentionally low but you pay the same or higher price initially agreed.

Therefore, contract law in different countries of the world must work to make a regulation that allows the existence of some alleged priced contract modification. In particular, a significant change should be avoided at all costs since in this case, it is likely that competing bidders could have made an offer radically different had they known that the contract was to have such major changes.

Especially to be avoided are actions against the interest related to the transparency or the integrity of the procurement process and with respect to the general principles of contracting where other interests prevail. In particular, the consequences should be relevant to the improper execution of contracts and extra-contractual modifications. (25) Thus, it is necessary to expressly

(23) Seminar “Integrity and efficiency in sustainable public contracts, Corruption, conflicts of interest, favoritism and inclusion of non-economic criteria in the award and execution of public contracts”, network “Public Contracts in Legal Globalization”, Turin, June 8, 2012.

(24) P. GHERSON, *Review of Civil Procurement in Central Government*, HM Treasury, 1999, available at <http://archive.treasury.gov.uk/docs/1999/pgfinalr.html>. National Audit Office, United Kingdom, available at [http://www.unodc.org/documents/treaties/UNCAC/Publications/Convention/04-56163\\_S.pdf](http://www.unodc.org/documents/treaties/UNCAC/Publications/Convention/04-56163_S.pdf). United Nations Convention against Corruption (UNCAC), New York, 2004, article 9 (2), provides that a procurement system must ensure adequate internal control and risk management. Article 9 (2): “2. Each State Party shall, in accordance with the fundamental principles of its legal system, take appropriate measures to promote transparency and accountability in the management of public finances. Such measures shall encompass, inter alia: (...) (d) Effective and efficient systems of risk management and internal control(...)”.

(25) See OECD, *Fighting Corruption and Promoting Integrity in Public Procurement*, 2005, 143.

contemplate the possibility that competing bidders or others will have an interest in the amended contract. This is highly relevant advertising that is offered them by the contracting authority. There is no doubt that secrecy breeds corruption. This makes it possible to reduce the risk of favoritism to the contractor.

Often to ensure the integrity of the actions of the contracting authorities are not enough to adopt such need. It is necessary to establish tools to incentivize good management of the procurement. Otherwise, the violation of the principle of transparency and equality will be apparent to the detriment of the main objectives of the procurement. In particular, it is necessary to find each year how many contracts have been awarded to one company, which has been the procurement budget, the budget award, the amount of variations to contracts, and other circumstances worthy of attention (degree of fulfillment of the criteria used to award the contract). Certainly the internal cost that will generate the required disclosures will be less than the gains or benefits in transparency to the public, to the public procurement market, and ultimately of transparency in the public and especially on effectiveness and efficiency of recruitment. I think that limiting the amount of changes in contracts generated after the initial disbelief, offers a more appropriate and proportionate to the contract and less variation in price, and therefore more appropriate to the financial commitments of contractors.

However, the rules are not enough. There must be created an ethical culture of “good procurement”. To do this, it is estimated that a measure might be to establish seals or awards for good quality public procurement institutions, demonstrating that their processes are transparent, equitable, and respectful of the obligation of public assembly. This kind of distinction encourages a culture of good recruitment and tends to eliminate the belief that problems are resolved at the policy level or through more rules which create an unwillingness to make commitments or voluntarily behave in an ethical manner.(26)

At the same time, it is necessary to train personnel of the contracting authorities. The most important thing is to professionalize public procurement. Why do we want a complex set of directives aimed at simplifying the process if managers do not know how to apply them? Substantial alteration of the title of *Gobernaza* provided in proposed directives has led to the belief that professionalization will suffer even more.(27) They are often economic reasons

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(26) See Integrity Awards granted by Transparency International. See too D. JOSÉ ZALAQUETT – W. ALEX MUÑOZ, *Transparencia y Probidad. Pública Estudios de Caso de América Latina*, Centro de Derechos Humanos, Chile, 2008, 145; and the Executive Order N°. 122. RO / 25 of 19 February 2003, *Anti-corruption system of Ecuador*, Article 6 especially dedicated to those known as “integrity pacts”.

(27) D. I. GORDON – G. M. RACCA, *Integrity Challenges in the EU and U.S. Procurement Systems*, in *Ius public network review*, N° 3, 2013, 43.

that justify the lack of training and lack of establishment of advisory bodies and reports on recruitment. However, it does not seem to reduce the problem of poorly awarded contracts on the basis of the economic crisis, as happened in Spain. It is also considered necessary to create committees to control recruitment, influencing, particularly in overseeing the bidding and award, but without losing sight of the execution of the contract, including contract modifications, which as I said, should be treated generally as new contracts.

Finally, severe sanctions should be imposed, and therefore personnel should be held accountable who spend public funds for improper contract modifications. These sanction could include coercive remedies to prevent corruption and inefficiency in the modification of contracts.

In conclusion, it should change the perception that transparency, integrity and perception of corruption generates low rates of attendance, resulting in better deals. If a contract is awarded improperly because it would be substantially modified to be transmitted the idea, the new tender will entail not only the duty to apply for a new procedure but result in better deals, and better prices.

### *6. An overview of the Spanish Legislation*

Since the approval of the Law 2/2011, of March 4, Sustainable Economy has been a strong limitation to contract amendments during its execution. This provision introduces a section devoted exclusively to changes in contracts in Spanish public procurement rules (now the Royal Decree 3/2011, of 14 November, approving the revised text of the Law of Contracts Public Sector).

This title contains a set of rules that apply to all entities subject to the law, ranging from traditional public administration to public companies, mutual accidents or even, in certain circumstances the citizens themselves. It is the first time this situation occurred before this rule because public authorities did have rules on contract modifications but any other entity that is not exactly the concept incardinate Civil was exempt from it, permitting unlimited modifications of the contract by mutual agreement. This is the most important issue as there were, until now, inefficient practices, designed to order certain benefits to other entities that do not have the status of public administration but which are acting as contracting authorities not subject to certain rules, among them. There has been, in short, a major expansion of the scope of the contractual limits.

Before this rule was breaking into our legal procedures it was frequently observed that contracts were awarded without advertising because of their size that experienced many extensions or were modified over and over again, far short of reflecting the real image observed after the initial award. Such

notoriety and was shown during the debate on the reform of Law 53/1999 of 28 December, which stated that:

*“as has been applying the rules of this matter at this time, we are all aware that the bidders can bid below the actual price on the conviction that after the award may obtain substantial changes in the price initially seen by means of the modified. This is a practice that leads to difficult budgetary control from the point of view of investment costs (...).”*(28)

Similarly the report and conclusions of the Committee of Experts for the Study and Diagnosis of the situation of public procurement, developed in 2004,(29) and noted that the changes in the contract may undermine the competitive nature of the initial award, to the extent that the contract is executed effectively and their prices are not those for which it competed. Now the legislature has indicated that the estimated value of contract shall include any amendments thereof.

In short, there are two types of contractual amendments in Spain, under the conditional (which should be reflected in the estimated value) and unforeseen.

With respect to the amendments provided for in the contract, the existing Article 106 of the consolidated text of the Law on Public Sector Contracts determines that a contract may be modified when:

*“in the specifications or in the invitation to tender has been expressly advised of this possibility and have detailed in a clear, precise and unambiguous conditions that may be using it, and the scope and limits of the modifications that can be agreed, specifying the percentage of the contract price which may affect maximum, and procedure to be followed for that.”*

Even claiming that *“the circumstances in which the contract may be amended to be defined with complete specification by reference to circumstances which can be objectively verified and conditions for possible changes should be specified in sufficient detail to enable bidders valuation for purpose of making its offer and be taken into account in regard to the requirement of eligibility conditions for tenderers and evaluation of tenders.”*

Meanwhile, the new Article 107 of the above standard, determines the possibility of modifying the contract even if there is specific provision in the conditions but only for very specific circumstances(30):

(28) Journal of Sessions Number 232, April 22, 1999.

(29) *Informe y conclusiones de la comisión de expertos para el estudio y diagnóstico de la situación de la contratación pública*, Ministerio de Economía y Hacienda, 2004, 15-118.

(30) The report 43/2008 of 28 July 2008 of the Advisory Board on Administrative Contracting State, called "Modifications of contracts, interpretation of Article 202 of the Law on Public Sector Contracts. Legal regime applicable to contracts which call for tenders had been a notice published prior to the entry into force of the Act and its award had occurred after "aptly summarizes and interprets the new legal regime for contract modifications provisions of the LCSP, referring directly to the ECJ CAS Succhi di Frutta Spa maintaining that "when he had not expected the change can be made only modifications that meet the following three requirements: a) that respond to changing needs of the public interest, b)

- a) *“Inadequacy of the contracted services to meet the needs they aim covered by the contract due to errors or omissions suffered in the drafting or technical specifications.*
- b) *Inadequacy of the project or the delivery specifications for objective reasons which determine its inadequacy, consisting of geological circumstances, water, archaeological, environmental, or similar, as observed after the award of the contract and not were predictable before applying all due diligence in accordance with good practice in the development of the project or in the drafting of the technical specifications.*
- c) *Force majeure that would make possible the completion of the transaction on the terms originally defined.*
- d) *The desirability of incorporating the provision technical advances that improve markedly if their availability in the market, according to the prior art, has occurred after the contract award.*
- e) *Need to adjust the provision to technical specifications, environmental, urban, safety or accessibility endorsed after contract award.”*

As can be seen, the Spanish legislature has opted for a closed list of reasons to try to define the concept of shelling or unforeseen circumstances.

In my opinion, that would have been much better. This shows up just to see the first two conditions (b). These are based on unforeseeable circumstances considered an error in the project and generate uncertainty of wondering if every error can justify the adoption of a modification. It can be concluded, in my opinion, that only if the error is not attributable to the performance of a diligent contracting activity can an admissible modification be made.<sup>(31)</sup> Conversely, when an unforeseen issue arises (all cases not covered by mistake or not is a surprise), a contract can not be modified. A possible clue to the severity of the error is to confront the effect it has had on the development of competing bids by bidders, so that if they met the error would have otherwise presented a substantially different modification to the contract will not fit even though there is this legal provision.

The wording of these two causes led to the intervention of the European Commission. This led to the Advisory Board on Administrative Contracting State to rule on the matter. So the resolution of 28 March 2012, the Directorate General of State Assets, which is published by the recommendation of the

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it is properly justified this need in the record, and c) that does not affect the essential conditions of the contract”. Similarly, L. RUIZ MELLADO, *El nuevo (y necesario) régimen de modificación de los contratos administrativos en el proyecto de Ley de Economía Sostenible*, in *Contratación administrativa práctica: Revista de la contratación administrativa y de los contratistas*, Núm. 99, 2010, 63. In this new regulation consolidating “double possibility of modification of administrative contracts”.

(31) C. BARRERO RODRIGUEZ, *La Resolución de los contratos administrativos por incumplimiento del contratista*, Editorial Lex Nova, 2007, 100.

Advisory Board on Administrative Contracting interpretation of the rules contained in Article 107 of the Consolidated Law Public Sector Contracts on modifications of contracts determines, in short, paragraph a) (design errors) must be interpreted as meaning that only modifications to the contract will correct those errors that were not anticipated prior to the award of contract, provided that any respected due diligence in accordance with good practice in the development of the project or in the drafting of the technical specifications.

Third circumstance (c) deserves no further mention than the distinction between the two concepts: force majeure and fortuitous event, meaning the first to the fact that you cannot prevent or predict, while in the second case we find a predictable event but inevitable. The fourth circumstance (d) is what justifies in progress or technical progress and should justify the effect that at the origin of the modified figure this cause,(32) under management contracts utility whose duration was often excessive occasion to incorporate technical advances they posed an improvement in its management. It is also common that specifications incorporate the “progress clause”(33) under which the contractor agrees to perform the tasks associated with the contract, pursuant to which, at the time, and according to the progress of science, has, for example, technical standards, environmental and safety resulting from application users.(34) Finally, the fifth circumstance (e) is the “*need to adjust the provision to technical specifications, environmental, urban, safety or accessibility adopted subsequent to the award of the contract*”, which is similar in some ways to the first two circumstances mentioned, since they make the project unfeasible as external issues from the drafting of the contract itself. The drawback is that it can generate the introduction of a variety of contract changes caused by these circumstances. It would be advisable to add the requirement that the amendment was strictly necessary, because if the new regulation does not require adaptation e.g., a concrete building constructed prior to its entry into force, it does not seem appropriate to make the adjustment required and therefore the contract amendment. Nevertheless foregoing, the provision is intended to also combine the concept of unpredictability with a limit on the modification to prevent an alteration of the essential conditions of the tender and award, claiming that the amended should be limited “*to introduce the changes needed*

(32) H. JORGE ESCOLA, *Tratado Integral de los contratos administrativos – Parte especial*, Ediciones Depalma, Buenos Aires, 1979, II, 83 which refers to the appearance of electric lighting that displaced the gas lighting with the implications for electric service in 1910 resulted in France.

(33) A. QUINTANA LOPEZ, *Algunas cuestiones sobre la cláusula de progreso en el contrato de concesión de obras públicas*, in Civitas. Revista española de derecho administrativo, Núm. 131, 2006, 421-444.

(34) In this regard, Article 230.4 of the LCSP obliges the licensee to maintain public works public works pursuant to which, at the time and according to the progress of science, provides technical standards, environmental, accessibility and removing barriers and security of users that is applicable, without prejudice to the foregoing, this concept should be restricted to the really unpredictable since otherwise we would be more to a new need, now outlawed by the Law of Contracts Public Sector.

to meet strict the objective reason that makes it necessary” to prevent the use of synonyms extenuating pleasing to the ear of the word “that” (because, since, ....) in which advantage under a given circumstance changes occur not enjoy the main feature of all modifications which must relate to the successful development of the contract.

When there is disruption of an essential term is necessary to make a new award procedure. This is due to the fact that the alteration involves a distortion of competition by giving preference to the contractor over other bidders. As noted by the Advocate General Kokott in her Opinion in *Pressetext*, asserted that:

*“there must be presumed whenever an essential modification can not be excluded that the original conditions, less favorable, have discouraged other service providers to participate in the bidding for a public contract, or, in view of the new contractual conditions may now be interested in bidding, or that new conditions could have been done with the contract a bidder who once did not get it”.*(35)

Moreover, the CJEU had the opportunity to clarify in its judgment *CAS Succhi di Frutta Spa* that if the contractor was authorized to modify at will during the execution of the contract the very conditions of tender without containing the relevant provisions express authorization to that effect, the terms of the award of the contract, as originally laid down, would be undermined, claiming that the amendments to the provisions of a public contract during its validity when a new allotment are materially different in character of the initial contract. In this regard, the ECJ judgment of 19 June 2008, C-454/06 *Pressetext Nachrichtenagentur*, maintains that the amendments to the provisions of a public contract during the currency of the award constitute a new “when materially different in character from the the original contract, and therefore highlight the willingness of the parties to renegotiate the essential aspects of the contract”.(36) Specifically, it was noted that the essential conditions must relate or at least understand, but not limited to, the subject of the tender, the selection and award criteria, and any other provision that had been included in the tender procedure would possible for tenderers tender substantially different or would have allowed the participation of other bidders other than those initially admitted.(37)

(35) Opinion of Advocate General Kokott Ms. March 13, 2008, par. 48 and 49.

(36) See ECJ 5 October 2000, *Commission v France*, in Case C-337/98, par. 44 - 46.

(37) The ECJ, 19 June 2008, *Pressetext Nachrichtenagentur*, in Case C-454/06, states that an amendment may be considered substantial if it changes the economic balance of the contract to the successful tenderer in a way that was not foreseen in the terms of the original contract or when greatly expand initially contracted services, and instead, it implies a duty to make a new contract when all services provided by the contractor are transferred to a capital company where he is the sole shareholder, or by conversion prices in euro initially expressed in national currency, or finally, where a contracting authority agrees with the contractor during the term of a contract concluded with it indefinitely extend for three years in a waiver clause to the resolution which has already expired on the date on which the new clause

The Sustainable Economy Act, sought to define the vague legal concept of essential condition of the contract by the following list provided by Article 92 quater.<sup>3</sup> Law on Public Sector Contracts, but in no case can be understood that in the case of *numerus clausus*.

- a) *“when the amendment the function varies markedly and essential characteristics of the initially contracted provision.*
- b) *if the amendment alters the relationship between the performance contracted and price as that relationship was defined by the conditions of the award.*
- c) *when to perform the required service changed professional qualification was different from that required for the initial contract or conditions substantially different solvency.*
- d) *when the contract changes equal or exceed, in more or less, 10 per 100 of the auction price of the contract, in the case of subsequent amendments, all of which may not exceed this limit.*
- e) *in any other case where it can be assumed that, having been previously known modification, had attended the award procedure other stakeholders, or that bidders who took part in it had submitted bids made substantially different.”*

It is clear that in cases a) and b), c) altering the order, the relationship between object and price or the basic qualities required of the contractor, we face a critical condition, in analogy to what prevented by the ECJ judgment of 19 June 2008, *Pressetext Nachrichtenagentur C-454/06*, cited, being the common denominator, as we have also said that all lead to the filing of a separate bid from bidders even than those initially concurrent that now would be interested in participating in the tender.

Notwithstanding all this, it should be noted that all modifications leading to an increase of more 10% of contract award will be considered *ex lege*, a substantial alteration. What at the time was justified because there was an increased percentage of measurements (less than 10% of the hammer price) that is normally the case in many of the works given the obvious difficulty of translating *ab initio* each accurate measurement into a document or when they

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is agreed and agreed with him to set higher rebates than originally anticipated for certain prices determined based on the amounts in a particular area. The State Council in its Opinion No. 44793 of December 2, 1982 said that “when you do not aspire to give a new way of being in the relationship between the parties, but to establish a different kind of relationship, overflowing the limits of the contract modification, being in fact a new covenant”, and opinion by May 19, 1983 held that “administrative contract amendment is, by its nature and by its peremptory norms, delimitation reasonable and consistent with its goals and approaches, as well as its subject, ranging from the very moment preparing projects and concatenate the object being defined in the award”. Also stated that the general principles of administrative require that the power variation of the projects that the Administration has in contracts concluded by it, to be exercised within a reasonable limit that does not denature the object of the contract. Similarly, the Supreme Court, in its judgment of 21 January 1994 stated that “*the unilateral modification of the contract by the administration may not affect the essential provisions*”. A prime example of qualitative material alteration is reported in the opinion of the Spanish State Council of 8 June 1967 it still plans to build a railway became the contract going to build a road.

go to the ground or reality,(38) now becomes a substantial alteration of the contract. That is why we think the less controversial this new circumstance, especially when the Draft Law on Sustainable Economy fixed this percentage by 20% of the auction price of the contract and the project fell to 10% the percentage of modifications. Perhaps the explanation may be founded on a matter unrelated to the problem but the execution of the contract and the reality is that if the consultations the Council of State had to be carried out when the contract is more than 20% of the price original contract, which will be equal to or greater than 6,000,000 euros – under Article 195.3.b), Law on Public Sector Contracts – now limited in the Draft 20% could ever know one modified by the Council of State, which now is also modified diction and that would inform the Council of State when the modification had increased « more than 10% of the original contract price, which will be equal to or greater than 6 million euros ». This is in fact the foundation of which is in the report of the Council of State to which we have been referring literally says otherwise “*taken away query is bound to this Advisory Body potentially conflicting cases*”. That is why it is questionable whether it would not have been enough consultation had been carried out when the modified increase of 15% – i.e. – and even if he had seen fit to reduce the amount of 6,000,000 euros for other minor figures to accommodate the important work of the Council.(39) Another justification can be given by the forecast that the ECJ judgment of 13 January 2005 made to condemn Spain for including in cases where the procedure could be applied to those unpublished negotiated open or restricted procedures remaining wilderness and were bidding again by the method mentioned by 10% raising its starting price. But it is true that, in my opinion, what is preached by the ECJ was that they used a course of negotiated procedure not covered by the Directive and therefore impossible to forecast, given the exceptional nature of this procedure. Nor would make sense, since it is covered by Directive 2004/18 that Article 155 of the Law on Public Sector Contracts allows negotiated procedure to award contracts without advertising works to the contractor up to an amount not exceeding 50% of primitive contract, perhaps the number or percentage that should be in place now at most.

Finally, the new precept warns that this is not a list of assumptions priced quite the opposite, so that in any other case where it can be assumed that, having been previously known modification, had attended the award

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(38) C. HORGUE BAENA, *La modificación del contrato administrativo de obras*, Marcial Pons, Madrid, 1997, 74-76.

(39) This was something I realized, without success, the parliamentary group that the amendment number 825 considered reasonable to maintain the rate of 20% for the issuance of the report of the State Council “*without profits can accurately understand derived to reduce that percentage to 10 percent. With this reduction, will not address the issue of changes to contracts, generating, in turn, further delay in the processing of case*”.

procedure other concerned, or that bidders who took part in it had submitted bids substantially different from those made, we face a substantial alteration of the contract, in line with what the judgment pointed in CAS Succhi di Frutta S.p.A. and therefore should be considered a resounding success, because contrary to what happens to define unforeseen circumstances is now sufficient evidence to define the concept of substantial alteration.

All this involves the introduction of a new cause for termination of the contract, as is “*the inability to enforce the provision in the terms initially agreed upon or the possibility of producing some serious injury to the public interest of providing continued running in those terms when it is not possible to modify the contract in accordance with the provisions of Title V of Book I*”-new article 206.h) Law on Public Sector Contracts – thus leading compensation to the contractor with 3% of the amount of the provision left to do except the cause is attributable to the contractor – new Article 208.6 Law on Public Sector Contracts.

In short, despite having improved drafting precepts governing amendments of contracts by contracting authorities subject to the Spanish public procurement rules, I believe that the regulation is closer to the future directive. There is a clear limitation to these actions. In this sense it would have been more fortunate to refer exclusively to the unpredictability concept coined by European jurisprudence rather than pretending dismember.

In practice this reform has meant greater control of the modifications. Although, they are beginning to address the first corruption. No amendments formalize, stop running issues under other contracts without any document recorded in additional contracts or call (with the limit of 50%) awarded to the main contractor which are modifications of contracts.

They are hiding evil practices – because these rarely come to light – which I believe require a “*police for public procurement.*” Some “agents” are needed to examine the contents of the contracts and verify that the result genuinely reflects the contracted agreement, and to impose sanctions on the perpetrators and those who allow such improper changes.

But there are also notable experiences in Spain since 2010 which operated a success rate around 50% in court of appeal involving public procurement, which are also resolved in a timely manner (between 10 and 20 days from the filing of the appeal the resolution) and could also see extended its jurisdiction to the changes.

Two regions have already completed. Aragon and Navarra. Regional Law 3/2013, of 25 February, amending Regional Law 6/2006 of 9 June, CPV modification required to publish and notify not only the winner but the tenderers admitted. It is very interesting to refer to the amendment of the Socialist Group under which incorporates the text of the standard is required. It was the

24 amendment which specifically mentioned the possibility of bringing special resource (called, in Navarra, claims on public procurement).

*“With this public release is the possibility given to initial bidders to appeal or even claim procurement deem if it is an illegal modification, as in fact occurred in the judgment of the Court cited the Explanatory Memorandum and the need arises to change the regime in Navarra modified.”*

## 7. Conclusions

The epoch in which the regulation of the contract was forgotten seems to have passed. It is necessary to avoid corruption and inefficiency in government procurement, and favoritism to contractors awarded the contract resulting from its financial offer the increases progressively with each change to the contract, to the detriment of the participants of the tender issued practiced and economic interests of citizens.

The ECJ planted the seeds for the birth of a standard European law for contract modifications. This is specified in the new directives that covers all contract modifications through the integration of the doctrine of the Court of Justice of the European Union, and therefore the effort to provide clarity to the appropriate regulation. Despite the excessive flexibility of the final text allowing excessive minimis threshold.

We emphasize from the definition of CAS Succhi di Frutta S.p.A. the principle of transparency as a key element to interpret everything that happens in the execution of the contract, including its amendments. So this sentence is satisfied with the contract that is not substantially altered where all terms and conditions of the tender procedure are formulated in a clear, precise and unambiguous terms in the contract notice or in the specifications. On the one hand, all bidders reasonably were informed and are normally diligent in understanding the precise scope of the conditions and interpret them in the same way. Moreover, the contracting authority can actually check that the tenders submitted by the bidders meet the criteria the contract in question. But, certainly “intriguing” is the possibility of determining this statement, *a priori* unpredictable, and clarified this statement in 2004 admitting the possibility of unanticipated changed in the conditions but always had its origin, not in “new needs”, but genuinely unpredictable circumstances, that are erratic for a diligent contracting legal transactions used to the contract. It is necessary to reform the way forward of the contracting authority in respect of certain practices. Specifically, the assignment of the contract which is generally a violation of the principle of competition, in which the contract is transferred to a separate subject and report directly to the contractor without leaving at least what the subject is concerned, without regard the award made, and dictates

the ECJ of 19 June 2008, *Pressetext Nachrichtenagentur GmbH*). Another anticompetitive practice is to introduce the concept consistent improvements as award criteria, under the same commission services outside the tender and have been known would give rise to different offers. As it has given rise to the judgment of 22 April 2010 *Commission v Kingdom of Spain* confirmed that advertisements and tender documents must have a clear wording to all potential tenderers, experienced and well informed and reasonably diligent, so they will have the opportunity to get a concrete idea of the work to be carried out and have a common basis for preparing offers, otherwise there is a risk that the principles of equal treatment and transparency are violated.

But above all, it is essential to take real measures to ensure sound and transparent execution of public contracts. In particular, the Internet publicizing each and every one of the modifications or additional contracts of whatever amount.<sup>(40)</sup> As far as making the directive, but not for the amendments provided in the conditioned.

Racca, Cavallo and Albano propose a measure of great interest that tends to determine the satisfaction of all concerned with public procurement, with surveys of opinion at the end of the acquisition process, including taxpayers.<sup>(41)</sup>

In conclusion, a contract, in its preparation, must be defined methodologically and deliberately so that modifications are not always necessary. It is best not to foresee changes in the contractual documents than to make it too generic.

Consequently, efforts should generate greater transparency in recruitment and avoid corruption. This is achieved, in part, by strictly interpreting the concept of unpredictability and scope of the necessary modifications. In addition, for this purpose it seems appropriate to require all contracting authorities to publish the figures to tender, awarding and especially of the contract liquidation.

Spanish legislation on contract modifications has greatly limited the use of these measures. Defined a list of assumptions priced contract modification, imposing different limits, noting the prohibition of not more than 10% variation on the award price. However, the « picaresque » exceeds the legislator and now it is necessary to effectively control it according to the contractual terms, it has been found that often no formalized contract modifications exist and change remain hidden in complex contractual documents (older measurements works nonexistent units, ...). Also there has been an increase in contract works or services performed and improperly treated as complementary rather than what is actually modified.

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(40) This measure has already been carried out by different regions in Spain, Extremadura, Balearic Islands, Aragón, and municipalities as Pamplona (Navarra).

(41) G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the Execution Phase of Public Procurement*, *cit.*, 92.

## CHAPTER 3

### Brief notes on modifications of public contracts in Italy

BY

Paolo LAZZARA

Associate Professor of Administrative Law, University Roma Tre

#### *1. Introduction*

This chapter analyses the modifications on the cost of public works and services, compared with the contract provisions. The relevance of the subject is better understood considering that the issue of variations aims to gather at best the conservation of the binding constraint and the need (or opportunity) to adapt the performance to the provisions or circumstances occurred, or changing them in a more satisfactory way for the public authority. It is not easy to provide an answer to this problem since the variations affect the fundamental element of the procurement contract. On one side there is the need of a strict application of the contract: the contractor does not want to pay unexpected expenses, and, on the other side, it wants to perform the contract for which its offer and enterprise have been organized. In reverse, the need to adapt the performances to unpredictable events as well as the need to adapt the work (of goods or services) to the evolution of the technology available and to the present state-of-art make the need of variations a recurrent issue. The statutory boundaries of the concept of variation mark also the limits within the modifications of the original object are still part of the performance, together with the rule of the invariability of the work, which prevents running variations not agreed. The public authority, according to the principles of good faith and sincere cooperation, must accept those variations which are essential to the best performance of the work as well as those ones which are necessary to protect the contractor from professional liability. As known, these practices are usually ordered to circumvent the EU rules; national legislation, on one side, tend to limit the area for discretionary decisions at any stage of the public procurement.

EU law, on the other side, aims to realize the open competition in the market. A ban or severe restrictions to the variations might conflict with the nature of the contract which typically include this possibility. It is also very difficult to monitor all the public contracts during their execution phase, mostly because the competitors have no longer any information about the correct fulfilment of the contract. On these issues it would be useful to analyse the best practices

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to prevent those changes in contract execution which may determine serious circumvention of the rules and may form great opportunity for collusive behaviours. Useful information comes from the statistics relating to the variations occurred during the execution of the contract and from the criminal law sector.(1)

## ***2. Italian regulation on modifications of public contracts between private autonomy and public interest***

The specific legislation on public contracts has always paid a particular attention to the modifications occurring during the public contract execution phase due to facts, conditions and events unforeseen or unforeseeable at the time of the award. The Italian Public Contracts Code, adopted by legislative decree No. 163/2006, confirms this general approach. The particular relevance of this issue comes from the fact that the execution phase of the public contract in the Italian legal framework is governed by private law contracts which does not consider the principle of supremacy of the public administration assigning to it just the prerogatives of the private law and consequently it is bound to civil obligations. Within the private law the issue of modifications to a contract during the course of its execution is central; therefore a balance between the principle of conservation of the obligation and the need to adapt the performances to incumbent new legal provisions, unforeseen circumstances or changing needs of the contracting authority is established. Private law thus makes it clear that modifications occurring during the execution of public contract are essential elements of tender contracts and may be used, if properly defined, to gather opposite needs all worthy of protection;(2) the interest to the strict application of the negotiated agreement which requires that the client shall not pay for unexpected or otherwise excessive expenses, and, on the other side, the right of the contractor to perform the services contractually agreed for which it has arranged its business; secondly there is no doubt that the contractor has an interest to obtain a payment commensurate with the additional works. However, the need to adapt the performances to supervening regulations or to unforeseeable events must be taken into account, as well as the need to adapt the work (good or services) to the evolution of technology and rules. The concept of alteration in private law tender contracts therefore marks the limits within the changes in the performances should be considered relevant to the subject matter of the original contract. In the case of public contracting, the contracting authority, under the principles of good

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(1) G. M. RACCA – R. CAVALLO PERIN, *Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption*, in *EPPPL*, 2013, 279-293.

(2) C. H. BOVIS, *EU Public Procurement Law*, 2007, 72 et seq.; S. L. SCHOONER, *Desiderata: objectives for a system of government contract law*, in *PPLR* 2002, 107.

faith and sincere cooperation, must accept the modifications essential to the execution of the work.<sup>(3)</sup>

On this regard the law on public works contracts of 1865 allowed the contracting authority to increase or decrease the amount of public works up to one fifth of the total amount of the contract; beyond this limit, the contractor could refuse the implementation of modifications this variation and was allowed to rescind the contract.<sup>(4)</sup> The so-called “*quinto d’obbligo*” (a sum up to one fifth of the total amount of the contract) was and a limit to the prerogative of public administration to change the contractual terms, beyond which the contractor could refuse the implementation of the modifications and even terminate the contract.

There was no concern at all that the agreed alteration, which substantially changed the terms of the original contract, could affect the previous tender process thus undermining the equal treatment for the tenders. Considering the absolute separation of the two phases there was no ground for stating that the execution of the public contract could affect somehow a procedure already closed. The latest regulations on this issue, however, are characterized by the progressive reduction of the private autonomy and the discretion of the public administration on the chance of making modifications during the course of public constructions as a guarantee of the requirements and principles of the Community economic order (market competition). This leads to a limitation of the modifications stricter than the one originally contained within Article 25, law No. 104/1994: the contracting authority had to terminate the contract for any alteration exceeding one fifth of the sum of the original contract. The current law, as further explained, regulates this issue with more flexibility while maintaining a disfavor for modifications during the course of execution. These restrictions are intended, primarily, to prevent the circumvention of the rules of public tenders, with consequent detriment for the equal treatment among competitors which have been called to present the best proposal in relation to the conditions settled in the notice; it is necessary to avoid that firms offer lower prices relying on subsequent modifications.

In this sense, the limitation of private autonomy of the contracting authority aims to ensure the effectiveness of the system of “market competition” as well as to avoid that the modifications occurring in the course of construction undermine the

(3) Cass., sec. I, 29 April 2006, No. 10052, in *Mass. Giur. It.*, 2006: “*Also in public works contracts (...) a duty can be attributed to the commissioning body, creditor of the opus, following from the express reference in Article 1206 of the Civil Code and, more generally, from the principles of fairness and good faith (...) to cooperate for the fulfillment of the contractor’s duty through the completion of those activities (...) necessary to enable the latter to achieve the result required by the contractual relationship. In this context, the development of modifications during the course of construction (...) can be seen as expression of a necessary cooperative intervention of the creditor: this happens when the alteration of the original project (in this case, construction of a school building) is made necessary by supervening mandatory legislative and regulatory provisions, on safety of installations, since, in this case, the work that was made according to the originally planned construction methods and technical instructions would expose the contractor to liability for harmful events for the life and personal integrity of others.*”

(4) Italian Law No. 2248 of 1865, Art. 344, annex F.

rules on competition in public contracts.(5) The legislative rigor then is affirmed to the need to prevent the uncontrolled growth of the cost of implementation; this hypothesis, in fact, is one of the most serious dysfunctions of public negotiations. Indeed, the public law regime implicitly assumes that public contracts usually offer occasion to collusive practices and that the modifications during the contract execution may cause effects more detrimental to the interest of public administration and public finance.(6) This perspective is confirmed by the provisions that focus on some situations, considered highly problematic and needed to specific supervision by the supervisory authority; among these a particular emphasis is always assigned to the use of the modifications during the execution of public contracts since it could hide serious irregularities.(7) Indeed, the use of modifications during the execution phase is one of the headings that the Supervisory Authority on public contracts has to explain in the annual report to Parliament and Government. Therefore, the consent of the contractors in the approval of the modifications compared to the requirements of public law is consequently reduced. Even if the modifications are approved “in the interest of administration” and “aimed at improving the work and its function” (improvement modifications) they must be justified by supervening circumstances and they are permitted only if they do not constitute substantial changes to the contract and, last, they do not exceed five percent of the total amount of the works;(8) any other “subjective” request of the contracting authority, although aimed at improving the work or service, cannot be met during the ongoing contractual relationship. The rigor of public law that characterizes the execution phase of public contract finds is due to the principles of European Union law and in particular into the principle of transparency and equal treatment, according to the principles of free movement of services and competition.(9) The ECJ case-law has set some parameters that allow the logical reconstruction of the EU principles on this issue. The boundary line follows the different qualification of the changes to the contractual terms: “substantial” changes are those that significantly extend the contract, that alter the economic balance originally fixed and demonstrate the willingness of the parties to renegotiate the terms of the relationship; the result is the prohibition of those modifications which, if originally planned, could affect the result of the competitive tender for the possible presence of other firms, or for the different content of the

(5) R. CAVALLO PERIN – G. M. RACCA, *La concorrenza nell'esecuzione dei contratti pubblici*, in *Dir. Amm.*, 2010, 325-354; C. FRANCHINI, *Pubblico e privato nei contratti delle amministrazioni*, in C. Frachini – F. Tedeschini (eds. by), *Una nuova pubblica amministrazione: aspetti problematici e prospettive di riforma dell'attività contrattuale*, Torino, 2009, 2 e ss.; G. MUSOLINO, *Varianti in corso d'opera*, in A. Carullo – R. Iudica (eds. by), *Commentario breve alla legislazione sugli appalti pubblici e privati*, Padova, 2009, 849.

(6) G. M. RACCA – R. CAVALLO PERIN – G. L. ALBANO, *Competition in the execution phase of public procurement*, in *PCLJ*, 2011, Vol. 41, 89 -108.

(7) Italian Code of administrative procedure, Art. 6.

(8) In this case the amount must be covered in the amount allocated for the execution of the works.

(9) P. TREPTE, *Regulating Procurement. Understanding the Ends and Means of Public Procurement Regulation*, Oxford, Oxford University Press, 2004.

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bids. The existence of a substantial changes of contractual terms – far from being as “modifications” in the strict sense – therefore implies the assignment (illegal) of a new contract. In the same logic, the notice constitutes the main regulatory tool to be taken into account during the execution of the contract and in relation to the acts involved in this phase; therefore the relevant requirements must strictly meet “the end of execution of the contract”. It should be noted that EU-laws aim to encourage innovative planning business by the firms, providing that the conditions of the competitive tender are transparent and predetermined. To this end, a broad spectrum of assessment is given to the contracting authority; it is here enough to recall the prohibition to impose by a regulatory framework the criterion of awarding contracts on the basis of the lowest price.<sup>(10)</sup>

### *3. Admitted modifications of the public contracts in the Italian legal framework*

To identify the type of allowed alteration, one must distinguish between the relevant typologies. The first important specification of the concept derives from the distinction between modifications in the course of construction and renegotiation of the contract; in this regard, the law excludes the chance to modify the contractual clauses in order to avoid dysfunctions in the competitors’ behaviors and at the same time substantial modifications of the equal treatment of the participants. This means that the modifications during the execution are prohibited insofar as they significantly affect the content of negotiations and lead to the creation of works or services substantially different from the ones published and awarded.

Articles 1659-1661 of the Italian Civil Code and the Italian Public Contracts Code offer other important information on this issue: the alteration must be justified by the need to adapt the work, service or supplies to conditions that were not predictable or knowable at the time of conclusion of the contract. This explains the prohibition of modifications aimed to correct defects and errors already present in

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(10) ECJ, sec. II, 7 October 2004, in C-247/2, *Sintesi spa*, in *Urb e App.*, 2004, 1267: “Article 30, No. 1 of Directive 93/37/EEC is against a national legislation which for the awarding of public works contracts imposes the contracting authority to use only the criterion of the lowest price. The establishment by the national legislature, in general and abstract terms, of one award criterion, deprives the contracting authorities, of the possibility of taking into account the special nature and particular characteristics of individual contracts and therefore does not allow to choose the system that appears most likely to ensure free competition in the specific case” since the administration must have a discretionary in assessing the most economically advantageous bid; or, again, the censorship placed on the national provisions which established the automatic exclusion of anomalous bids, negating any margin of appreciation of the possible justifications; ECJ, 15 May 2008, *Secap Spa*, in Cases C-147/06 and C-148/06, in *Giornale dir. amm.*, 2008, 1103: “The national legislation which excludes any possibility of assessing the solidity and reliability of abnormally low tenders does not put the contracting authority in the position to fulfill the obligation to respect the fundamental rules of the Treaty on free movement, and the general principle of non-discrimination. This condition prejudices the interest of the contracting authorities themselves to the extent that it is not possible to evaluate the bids presented under conditions of effective competition and to award the contract under the criteria, also established in the public interest, of the lowest price or the most economically advantageous bid”. Similarly, Trib. I g. EC, sec. V, May 21, 2008, n. T-409/05, *Belfass SPRL*, E.C.R. II-781.

the public procedure and that would have required the interruption of the award procedure.(11) It therefore seems necessary to clarify the content of the discipline on modifications in public contracts to assess the consequences arising from their approval. The most common hypothesis occurs when the contracting authority and the contractor introduce, by consensus, some changes to the performance, beyond the limits allowed by the law. According to the civil law, the hypothesis would be not problematic at all, since the initial negotiated agreement can be in any way and at any time integrated or replaced by the contractors' mutual consent.

The public law has a different perspective mainly because the contractors – even if by mutual agreement – cannot contradict the prohibitions and limitations imposed by the discipline of administrative law. It should be established, first of all, the administrative law conditions under which a modification is possible; then, the validity of the agreement between the parties, and finally, the conditions of the original contract. The administrative acts which authorize an alteration in absence of the conditions laid down or beyond the limits established by article 132, Code of Administrative Justice, are considered illegal.

It must be recalled, by analogy, the case-law which considers void the renegotiations agreed in violation of the rules of public procedures, and adopted beyond the limits of public law.(12)

It is hard to go further about this complex issue, considering that the doctrinal and jurisprudential debate has not yet come to a solution.(13) In any case, the acts authorizing those prohibited modifications are considered illegitimate – such as a direct award – and can be appealed by any company interested in the contract.

The implementation of the prohibited modifications, on the other hand, does not affect the original contractual bind; this conclusion derives from the provision imposing the termination of the contract and the setting of a new tender only in the case of modifications exceeding one fifth of the original total amount, that are needed to correct errors and omissions of the executive project and are likely to affect, in whole or in part, the execution and use of the work.(14) The other “objective” modifications, related to supervening

(11) T.A.R. Lazio, Rome, sec. III, January 7, 2007, No. 76, in *www.giustizia-amministrativa.it*: “the institution of alteration (...) cannot be used as a reserve instrument which serves to correct errors that had already emerged during the process of formation of the contract for a public tender, resulting in contradiction with the principle of good performance and efficiency that the administration proceeds to the award of the contract in the knowledge that the contractual relationship, that it is about to conclude with the winner of tender is unsuitable to allow to complete the realization of the planned work”. T.A.R. Lazio, Rome, sec. III, 3 August 2006, No. 6911, in *Urb. e app.*, 2006, 1230; T.A.R. Lazio, sec. III, 5 July 2006, No. 691, in *Riv. Giur. Edilizia*, 2007, No. 1 vol. 1, 386.

(12) The Presidency of the Council of Ministers, Department of Community Policies, affirms the ban of renegotiation, circular of 15 November 2001, No. 12727.

(13) The doctrine which most recently addressed the solution, has placed due emphasis to the new “tenders guideline” (2007/66/EC) and to the most important negations of the administrative courts and the Courts of Cassation. The recent Community innovations (Directive 2007/66/EC), along with some authoritative doctrinal positions, lead us to prefer the simple theory of nullity of the (new) contract assigned without a tender.

(14) Italian Code of administrative procedure, Art. 132, 1<sup>st</sup>. par. Letter e).

or unforeseeable events,<sup>(15)</sup> do not have limits of value and do not require the termination of the contract; however this can happen only without prejudice, of the general prohibition of “substantial” modifications which affect the settled economic equilibrium or that lead the parties to express a willingness to renegotiate the terms of the original contract.<sup>(16)</sup>

The boundary between modifications (legitimate) and contract modifications has no meaning in presence of conditions that allow the assignment of the “new contract” by private agreement (without competitive tender). Indeed, in presence of the conditions required, the administration may directly appoint the firm that has already dealt with the works, supplies or main services (as long as the new contract comply with the formalities laid down therein). From this point of view the distinctions between modifications during the contract execution and renegotiation has still a great importance. It must be consider, the hypothesis of extreme urgency that leads, not infrequently, to the integration of the contract; the “complementary” performances that cannot be separated, from a technical-economic point of view, from the initial contract; the “repetition” of similar services already entrusted by the contractor. Others examples may be added.<sup>(17)</sup> Thus the link between limitation to modifications and assignment to private negotiations appears really strong: the direct assignment is allowed by the legal framework with specific reference to performances that, even if implying substantial changes to the contract, are technically and economically deeply linked to it.

The above assumptions, therefore, work such as safety valve which, under the conditions specified, allows the administration to integrate the contract with new services assigned to the firm that has executed the works. As already mentioned, the general disfavor for modifications during the public contract execution does not exclude the possibility that the changes may be justified both for the peculiar characters of the tender contract and for the difficulty of predicting objective and subjective conditions and circumstances occurring after the conclusion of the contract. According to this measures concerning details, related to non-essential elements of the project and not exceeding the percentage specified by law (5 or 10% depending on the type of variation) are allowed. In this case the contracting authority can decide autonomously, without following the procedure provided for modifications *stricto sensu*.<sup>(18)</sup> The legal framework also admits modifications (so-called improvements) imposed in the interest of administration and designed to improve the

(15) *Ibid.*, Art. 132, par. 1 (a), (b), (c), (d).

(16) Cass. Sec. I, June 14, 2000 No. 8094, cit.; C State Sec. V, 15 December 2005, No. 7130, cit., “the negotiation of new terms for the execution of new works as a result of a special valuation of alterations is certain proof of a new and independent contract, but it cannot be excluded for the mere fact that the contractor has agreed to perform the new works to the same terms and conditions of the original contract”.

(17) Italian Code of administrative procedure, Art. 57.

(18) Italian Code of administrative procedure, Art. 132, par. 3, first sentence, and Italian Presidential Decree No. 207 of 2010, Art. 161, par. 5.

functionality to the work, as long as they do not form substantial changes to the project, they are motivated by the objective requirements arising from supervening and unforeseeable circumstances and they do not exceeding 5% of the original amount and find coverage in the amount originally invested.

Beyond these limits, the mutation or the extension of the performances gives rise to a new contract that can be awarded without a tender only under the conditions provided by the private law. It is easy now to understand the ground of the special rules concerning the modifications – exceeding one fifth – which become necessary because of errors in the project could affect, even in part, the implementation or use of the work or service. In this case, and only in this case, the contracting authority must cancel the contract and issue a new tender; there is therefore a presumption of inadequacy of the project to meet the public ends in relation to essential and non-modifiable elements. The hypothesis invokes on one side, the general power to « withdraw » under art. 134, Code of Administrative Justice: the administration which terminates the contract pays for the work already performed, the useful materials and ten per cent of the works not performed.(19) However, in case of modifications made due to design errors, the termination by the contracting authority is mandatory. The case of modifications imposed by objective and supervening events is different; indeed, the modifications for events not foreseeable at the time of conclusion of the contract (so called objective) are allowed with no restrictions. These cases regard, for example, new legal rules come into force after the award (*jus novorum*), events related to the nature and specificity of the assets on which the works are performed, geological causes unforeseen and unforeseeable during the design stage. With regard to the *jus novorum*, the requirements for safety of installations are especially at stake, since they can change quite rapidly and give rise to an obligation of adjustment.

The contractor, in this case, cannot refuse to collaborate in the implementation of the modifications needed, neither the administration, for its part, may oppose the fact that the new regulation is implemented in order to perform the work or service in a more proper way. Failure to predict the quantitative limits to the so-called objective modifications imposes particular rigor in assessing the conditions of their occurrence in order to not hide adjustments already present during the design or award stage.(20)

Therefore the decision should be specifically justified and it must clarify the causes, conditions and requirements of the alteration; in particular, it is up to those responsible for the procedure, on proposal of the director of works, to describe the situation and to clarify the circumstances not foreseeable at the time of preparation of the project or the delivery of work. A final hypothesis of alteration occurs

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(19) Art. 134, 1st par., Code of administrative procedure.

(20) Authority for the Supervision of Public Works, January 11, 2001 determination, n. 1.

in the case of using of materials, components and technologies which did not exist at the time of planning: in this case, the contract may be changed providing that there will be an improvement in the quality of the service with no additional cost, and providing that the original design approach is not affected.

#### ***4. Modifications in the execution of services and supplies public contracts***

Article 114 of the Italian Code of Administrative Justice refers to regulation for the cases in which modifications happen during the course of execution in supplies and services contracts (or in mixed contracts). The rules provided for modifications in public works (Art. 132) are applied as long as compatible.

Even in these contracts are thus permitted modifications during the execution of the contract in accordance with Art. 311, Presidential Decree 207/2011. The regulation in particular, tracing what was established for works contracts, admits modifications for some unexpected variations related to supervening laws and regulations; unforeseen and unforeseeable causes; intervened possibility of using materials, components or technologies not existing at the time when the public tender procedure began that can determine, with no costs increasing, significant improvement in the quality of the services performed; modifications related to events that concern the nature and specificity of the assets and sites of intervention, which occurred during execution of the contract. Adopting modifications, increasing or decreasing, aimed at the improvement or to the better functionality of the performances object of the contract are also permitted, as long as such modifications do not involve substantial changes and are motivated by the objective requirements arising from supervening circumstances unforeseeable at the moment of the stipulation of the contract. The increasing or decreasing amount cannot exceed five percent of the original amount of the contract and must be covered in the amount allocated for the execution of the service.

Even in the procurement of supplies and services, the contracting authority may request a change, therefore increasing or decreasing, up to the fifth of the total price of the contract, after signing an act of submission, containing the same terms, prices and conditions of the original contract, providing no compensation for the contractor except the due payment on the new services. If the modifications exceed this limit, the contracting authority shall stipulate an additional act of the main contract after acquiring the consent of the executing party.

The executing party – on the other hand – has an obligation to perform all those non-substantive changes deemed as appropriate by the contracting authority and those that the Director of execution of the contract has ordered, as long as they do not change substantially the nature of the activities covered by the contract or impose additional costs borne by the executing party.



## **PART V**

# **The Need for Professionalisation in the Procurement Market**

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**CHAPTER 1**  
**The importance of a professionally educated public  
procurement workforce: lessons learned  
from the U.S. experience**

BY

Peter T. McKEEN

Adjunct Faculty, University of Virginia

***1. Introduction***

Since the 1990s, the U.S., EU and other countries have introduced a wave of procurement reforms to improve the efficiency and effectiveness of the procurement system. Many of these reforms have resulted in benefits to the procurement process. However, in other cases, legislation is enacted and regulations are implemented without fully assessing whether agencies are equipped to implement them and with little regard for unintended consequences.(1) Thus, integrating and assessing these reforms has prompted governments to focus greater attention on how the capabilities of the procurement workforce impact the overall effectiveness of the procurement system and the efforts to improve it. These efforts offer useful insights on the relationship between the procurement workforce and broader efforts to promote an effective procurement system that maintains the public's trust. Focusing on the lessons learned from the U.S. experience, this chapter will argue that in assessing the effectiveness and integrity of a public procurement system, consideration must be given to the capabilities of the system's procurement workforce. A procurement system where the workforce is not adequately prepared to deal with increasingly sophisticated practices is at a higher risk for fraud waste and abuse. The chapter will further argue that a public procurement system's effectiveness and integrity can be enhanced by the creation of a professionally educated procurement workforce.(2)

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(1) The Professional Services Council Acquisition Policy Survey, *The Great Divide*, October 2010 at 7, available at: <http://www.pscouncil.org/>.

(2) The 2010 OECD *Roundtable on Collusion and Corruption in Public Procurement* notes that the education of public officials, business and civil society is an important element in the effort to improve the integrity of the public procurement process.

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## **2. The Public Procurement Workforce – A Pillar of the Procurement System**

The structure of each national procurement system is influenced by a variety of factors, including the economic, cultural, political and social elements of the country and therefore each procurement system has certain unique characteristics. Thai, nevertheless studies of public procurement systems, including those by the Government Accountability Office (“GAO”) and the Organization for Economic Cooperation and Development (“OECD”), have identified certain common elements of a public procurement system.<sup>(3)</sup> An OECD study found four “pillars” of a procurement system: legislative and regulatory framework, institutional framework and management capacity, procurement operations and market practices, and integrity and transparency of the public procurement system. In considering these studies, Professor Thai identified a useful framework consisting of four essential pillars of a public procurement system: Procurement organization; Procurement laws and regulations; Procurement workforce; and Procurement process and procedures.<sup>(4)</sup> Under Thai’s analysis, the procurement workforce can be described as an essential pillar of a public procurement system. Thai notes that under the four pillar framework, each of these elements needs to function properly for a procurement system to operate effectively. Professor Thai further observes that: “[a] public procurement system may be ineffective in a sound procurement environment and an effective governmental structure and leadership because all or one of its ‘pillars’ is not efficient”.<sup>(5)</sup> Thus, the “four pillars” framework can be useful in making assessments of a procurement system, and determining the types of reforms that may be required.

Consistent with Professor Thai’s findings, there is widespread agreement that to operate effectively, a public procurement system requires an educated and specially trained procurement workforce. Indeed, Professor Thai further notes that: “The procurement system may be ineffective because a procurement workforce may not be of the quality and quantity essential to good procurement administration”.<sup>(6)</sup> These conclusions are fully supported by other studies that have identified the increasingly central role played by the procurement workforce in the effectiveness and efficiency of a procurement

(3) For example, GAO identified four “cornerstones” to the procurement system, including human capital. See GAO, *Framework For Assessing The Acquisition Function At Federal Agencies*, GAO-05-218G, September 2005; K. V. THAI, *International Public Procurement: Concepts and Practices*, in K. V. Thai (ed. by) *International Handbook of Public Procurement*, CRC Press: London, 2009, 4.

(4) K. V. THAI, *International Public Procurement: Concepts and Practices*, in K. V. Thai (ed. by) *International Handbook of Public Procurement*, *cit.*, 4.

(5) K. V. THAI, *International Public Procurement: Concepts and Practices*, *cit.*, 20.

(6) K. V. THAI, *International Public Procurement: Concepts and Practices*, *cit.*, 20.

system's operation. For example, a 2008 report by the National Association of State Procurement Officials ("NASPO") observed that the traditional mission of a procurement official serving as a "provider" of goods and services is being transformed to being the "manager of the providers" of goods and services.(7) Thus, according to NASPO, public procurement has transitioned from purchase order processing to a more strategic role in government, and that while compliance with policies and procedures was at one time a primary focus, today's public procurement professionals encounter more complexity and a more central role in organizational performance.(8) The NASPO report adds that today's procurement professionals are more central to defining and implementing the procurement value proposition for the stakeholders.(9) Further, the key role of the procurement workforce has been recognized as the role of procurement in overall organizational effectiveness and efficiency becomes more recognized.(10)

The above NASPO findings are echoed in a 2007 report of the OECD, *Integrity in Public Procurement – Good Practice From A To Z*, which includes a discussion on "Enhancing Professionalism To Prevent Risks To Integrity In Public Procurement."(11) The OECD report notes the increasing professionalization of public procurement and the need for appropriate skills to meet the greater demands of the public procurement process.

Public procurement is increasingly recognised as a profession that plays a significant role in the successful management of public resources. In the last decade reform efforts have often occurred in cycles, as public procurement has gone through substantial changes in terms of priorities, needs and capacity.

Public officials need to be equipped with instruments, as well as a range of procurement, project and risk management skills to properly plan and manage procurement processes, in accordance with the budget.

The OECD report notes that to provide procurement personnel with current skills and qualifications to prevent mismanagement and corruption, countries are using certification requirements, such as in the U.S., and specialized training in new technologies or specific situations, such as emergency contracting, which, without proper guidance, is conducive to fraud, waste and

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(7) National Association of State Procurement Officials, *Responding to an Aging and Changing Workforce: Attracting, Retaining and Developing New Procurement Professionals*, Research Brief, March 2008 at 1.

(8) National Association of State Procurement Officials, *Responding to an Aging and Changing Workforce*, *cit.*, 7.

(9) National Association of State Procurement Officials, *Responding to an Aging and Changing Workforce*, *cit.*, 7.

(10) National Association of State Procurement Officials, *Responding to an Aging and Changing Workforce*, *cit.*, 7.

(11) OECD, *Integrity in Public Procurement – Good Practice From A To Z*, 2007, available at: <http://www.oecd.org/development/effectiveness/38588964.pdf>.

abuse.<sup>(12)</sup> The report also notes the effort to assist procurement officials has included the development of internal information systems to support officials in making informed decisions about procurements.<sup>(13)</sup>

The central role of the procurement workforce in the public procurement process can also be seen by examining the adverse impact on the U.S. federal procurement system resulting from its downsizing more than a decade ago. For example, Professor Steve Schooner has noted that the significant reductions to the federal procurement workforce occurring in the 1990s: “reduced the number of professionals available to plan for, negotiate and manage the government’s contracts”.<sup>(14)</sup> These reductions: “rendered succession planning impossible, increased future risks associated with the pending retirement bubble, and left the government unprepared for the recent period of dramatically increased purchasing.”<sup>(15)</sup> These challenges resulting from insufficiencies in the U.S. federal procurement workforce, bolster Thai’s observations that the effectiveness of a public procurement system can be compromised when one of its pillars is not efficient.

### 2.1. A growing appreciation for the central role of the procurement workforce

Developments over the past decade in U.S. public procurement have reinforced the key role of the acquisition workforce and prompted calls for addressing workforce shortages and gaps in capabilities. In 2003, due in part to the adverse impacts of the downsizing of the acquisition workforce, the U.S. Congress, commissioned an Acquisition Advisory Panel (“AAP”) to examine certain procurement practices and make recommendations for improving the procurement process. In its 2007 report, the Panel noted that its findings and recommendations for improvement “make clear how essential the acquisition workforce is to the effectiveness of these elements of the federal acquisition system”.<sup>(16)</sup>

The Panel’s key observations included the following:

The federal acquisition workforce is an essential key to success in achieving the government’s missions. Procurement is an increasingly central part of the government’s activities. Without a workforce that is qualitatively and

<sup>(12)</sup> OECD, *Integrity in Public Procurement – Good Practice From A To Z*, cit., 63.

<sup>(13)</sup> OECD, *Integrity in Public Procurement – Good Practice From A To Z*, cit., 67.

<sup>(14)</sup> S. SCHOONER, *Federal Contracting and Acquisition: Progress, Challenges and the Road Ahead*, in *The George Washington University Law School*, Legal Studies Research Paper No. 483, 30.

<sup>(15)</sup> S. SCHOONER, *Federal Contracting and Acquisition: Progress, Challenges and the Road Ahead*, cit., 30.

<sup>(16)</sup> *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress*, January 2007 (“AAP Report”), 327.

quantitatively adequate and adapted to its mission, the procurement reforms of the last decade cannot achieve their potential, and successful federal procurement cannot be achieved.(17)

The findings of the AAP highlight both the central role of the public procurement workforce, as well as the need for an appropriately qualified workforce to implement the policies and practices designed to improve the procurement process. Without a qualified procurement workforce, efforts at reforming a procurement system will likely fall short.

The reductions in the federal procurement workforce noted above, promoted an increased reliance on government contractors, particularly during the administration of George W. Bush, as agencies outsourced many functions traditionally carried out in-house by government personnel.(18) In examining the performance of the Department of Homeland Security, an agency heavily dependent on contractor personnel, the authors note that “outsourcing as a matter of necessity, rather than as a matter of policy, leads to suboptimal results”.(19) These suboptimal results included concerns that contractor personnel were performing “inherently governmental” functions.(20) Thus, in some cases, the lack of government personnel resulted in non-government, contractor employees performing duties that should only be performed by government employees, potentially compromising the essential functions of the government. The reliance on contractor personnel led not only to concerns regarding the performance of inherently governmental functions, but the lack of government personnel created a loss institutional knowledge within agencies. This, in turn, compromised an agency’s ability to function, while rendering it less able to provide oversight of those contractors on which it relies. The authors recommended that:

*“the government promptly and aggressively recruit a huge number of business-minded professionals, but also must train the new personnel and provide supplemental training to the existing workforce to enhance their competence and expertise. Further, the government needs to provide meaningful incentives for, and employ creative solutions to retain (or of course, to continually recruit and train) over time, the best, most experienced professionals.”*

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(17) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit.*, 330.

(18) See for example, S. L. SCHOONER – D. S. GREENSPAHN, *Too Dependent on Contractors? Minimum Standards for Responsible Governance*, in *Journal of Contract Management*, 2008, note 27.

(19) S. L. SCHOONER – D. S. GREENSPAHN, *Too Dependent on Contractors? Minimum Standards for Responsible Governance, cit.*, 9.

(20) The term “inherently governmental function” means a function that is so intimately related to the public interest as to require performance by Federal Government employees and includes functions that require either the exercise of discretion in applying Federal Government authority or the making of value judgments in making decisions for the Federal Government, including judgments relating to monetary transactions and entitlements. See Office of Federal Procurement Policy Letter 11-01, *Work Reserved for Performance by Federal Government Employees*, October 12, 2011.

The call for restoring and improving the acquisition has also been made by members of the Obama Administration and GAO. For example, Daniel Gordon, who recently stepped down as Administrator for the Office of Federal Procurement Policy, made the following observation in September 2010 before the U.S. Commission On Wartime Contracting:

*“From 2001 to 2008, contract spending more than doubled to over 500 billion dollars, while the size of the acquisition workforce – both civilian and defense – remained relatively flat. This inattention to the workforce resulted in increased use of high-risk contracting practices and insufficient focus on contract management, as well as the especially troubling phenomenon of agency dependence on contractors to support the acquisition function.”* (21)

In addition, a number of GAO reports in recent years have emphasized the importance of a procurement workforce capable of working in a more sophisticated acquisition environment.(22) These reports stress that the failure to maintain an adequate workforce increases the risk of poor outcomes and vulnerability to fraud, waste, and abuse. Thus, in recognition of the central role of the procurement workforce in the promoting the effectiveness of the U.S. procurement system, the Obama administration has worked to strengthen all components of the federal acquisition workforce, including investment in the growth and development of the entire acquisition workforce.(23)

(21) D. I. GORDON, *Statement of the Honorable Daniel I. Gordon, Administrator for Federal Procurement Policy (“OFPP”), Office of Management and Budget Before the Commission On Wartime Contracting*, September 16, 2010, available at: [http://www.whitehouse.gov/sites/default/files/omb/legislative/testimony/ofpp/2010-09-16\\_Gordon-OFPP.pdf](http://www.whitehouse.gov/sites/default/files/omb/legislative/testimony/ofpp/2010-09-16_Gordon-OFPP.pdf).

(22) See for example, U.S. Government Accountability Office (GAO), *Acquisition Workforce: Status of Agency Efforts to Address Future Needs*, GAO-03-55, December 2002 (Most acquisition professionals will need to acquire a new set of skills focusing on business management. Because of a more sophisticated acquisition environment, they can no longer be merely purchasers or process managers. Instead, they will also need to be adept at analyzing business problems and assisting with developing strategies in the early stages of the acquisition); *DOD Acquisition Workforce: Additional Actions and Data Are Needed to Effectively Manage and Oversee DOD’s Acquisition Workforce*, GAO-09-342, March 2009 (If it does not maintain an adequate workforce, DOD places its billion-dollar acquisitions at an increased risk of poor outcomes and vulnerability to fraud, waste, and abuse); *OMB Acquisition Workforce: The Office of Management and Budget’s Acquisition Workforce Development Strategic Plan for Civilian Agencies*, GAO-10-459R, April 23, 2010 (the government needs to ensure that it has the workforce needed to carry out robust and thorough management and oversight of contracts to achieve programmatic goals, avoid significant overcharges, and curb wasteful spending. However, the capacity and the capability of the federal government’s acquisition workforce to oversee and manage contracts have not kept pace with increased spending for increasingly complex purchases); *High Risk Series: An Update*, GAO-11-278, February 2011 (The shortage of trained acquisition personnel impedes the capacity and capability of agencies, such as the Department of Defense (DOD) and Homeland Security (DHS) to oversee and manage contracts that have become more expensive and increasingly complex. As a result, GAO work has found that the federal government is at risk for significant overcharges and wasteful spending of the hundreds of billions of contract dollars it spends for goods and services each year).

(23) See also President Obama’s Government Contracting Memorandum of March 4, 2009, wherein the President noted the government’s obligation to “perform its functions efficiently and effectively while ensuring that its actions result in the best value for the taxpayers.” *Id.* In conjunction with this effort, the memorandum stated the need to ensure that the federal acquisition workforce possesses the capacity to develop, manage, and oversee acquisitions appropriately in support of the effort to achieve

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In conjunction with the efforts of the OFPP, the Department of Defense (“DoD”) has also moved to restore its acquisition workforce. DoD describes the rebuilding the acquisition workforce as a strategic priority.<sup>(24)</sup> DoD plans to augment the capacity of the defense acquisition workforce by increasing its numbers by 20,000 employees over the next 5 years.<sup>(25)</sup> Moreover, according to Mr. Hutton, current budget and long-term fiscal pressures underscore the importance of a capable and well-functioning workforce.

The preceding discussion supports the argument that the procurement workforce is a “pillar” of the procurement system. There is broad recognition that current procurement practices have expanded the role of the procurement professional in the overall acquisition process. The U.S. experience also highlights the adverse impacts, such as an increased risk of fraud, waste and abuse, that can occur when the capacity and the capability of the acquisition workforce is not up to the challenge. Thus, the acquisition workforce plays a central role in the efficiency and effectiveness of the public procurement process.

### ***3. The Increasing Complexity of the Public Procurement Process Demands A Professionally Educated Workforce***

Related to the more central role played by the acquisition workforce, is the increasing complexity of the procurement process. Public procurement is inherently complex and requires interdisciplinary skills and knowledge, such as economics, political science, public administration, accounting, marketing, law, management and engineering among others.<sup>(26)</sup> As detailed below, the evolution of acquisition methods and practices, along with public agencies’ efforts to balance often competing goals, has altered the role of the procurement professional and added new layers of complexity to the procurement process. The various procurement reforms imposed on the U.S. federal procurement system since the 1990s have changed the way the federal government purchases goods and services, with a greater reliance on judgment and initiative rather than rigid rules to make purchasing decisions.<sup>(27)</sup>

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programmatic goals, avoid significant overcharges, and curb wasteful spending. *Government Contracting Memorandum*, Presidential Documents, 74 Fed. Reg. 9755 (Mar. 6, 2009).

(24) U.S. Government Accountability Office (GAO), Statement of John P. Hutton, Director Acquisition and Sourcing Management, *Acquisition Workforce: DOD’s Efforts to Rebuild Capacity Have Shown Some Progress*, GAO-12-232T, November 16, 2011, available at: <http://www.gao.gov/products/GAO-12-232T> at 1.

(25) U.S. Government Accountability Office (GAO), *Defense Acquisition Workforce: DOD’s Training Program Demonstrates Many Attributes of Effectiveness, but Improvement Is Needed*, GAO-11-22, October 2010.

(26) K. V. THAI, *Public Procurement Re-examined*, in *Journal of Public Procurement*, 2001, Vol. I, *cit.*, 39. M. K. GIBONEY – P. T. MCKEEN, *Capstone Course Topics In Federal Procurement*, SMG, 2011 at 16.

(27) U.S. Government Accountability Office (GAO), *Acquisition Workforce: Status of Agency Efforts to Address Future Needs*, GAO-03-55, December 2002, available at: <http://www.gao.gov/products/GAO-03-55>.

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In a report on the acquisition workforce, GAO noted the need for the procurement workforce to acquire new skills to adapt to a changing environment:

*“Industry and government experts alike recognize that a key to making a successful transformation toward a more sophisticated acquisition environment is having the right people with the right skills. Leading public organizations here in the United States and abroad have found that strategic human capital management must be the centerpiece of any serious change management initiative and efforts to transform the cultures of government agencies. Workforce planning provides managers with a strategic basis for making human resource decisions and allows organizations to address systematically the issues that are driving workforce change.”*

Most acquisition professionals will need to acquire a new set of skills focusing on business management. Because of a more sophisticated acquisition environment, they can no longer be merely purchasers or process managers. Instead, they will also need to be adept at analyzing business problems and assisting with developing strategies in the early stages of the acquisition.(28)

Therefore, the new role of the procurement professional demands a fundamental understanding of the concepts and principles associated with the procurement process. This understanding can promote good judgment, critical thinking and sound analysis, which contributes to better decision-making.

As noted above, integrating procurement reforms has prompted the U.S. federal government to focus greater attention on how the capabilities of the procurement workforce impact the overall effectiveness of the procurement system and the efforts to improve it. These efforts offer useful insights on the relationship between the procurement workforce and broader efforts to promote an effective and ethical procurement system.

The 2007 report issued by the congressionally-authorized Acquisition Advisory Panel, as noted above, was tasked with reviewing laws, regulations, and government-wide acquisition policies “regarding the use of commercial practices, performance-based contracting, the performance of acquisition functions across agency lines of responsibility, and the use of Government-wide contracts”.(29) The U.S. Congress requested the Panel to recommend changes necessary to: (A) “protect the best interests” of the government; (B) “ensure the continuing financial and ethical integrity of acquisitions by ”the government; and (C) “amend or eliminate any provisions in such laws, regulations, or policies that are unnecessary for the effective, efficient, and fair award and administration of contracts for the acquisition” by the government of

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(28) U.S. Government Accountability Office (GAO), *Acquisition Workforce: Status of Agency Efforts to Address Future Needs*, GAO-03-55, cit., 1.

(29) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress*, January 2007 at ix.

goods and services.(30) Thus, the Panel's efforts focused on protecting the government's interests while promoting the effectiveness, efficiency and integrity of the procurement process.

In its Report, the Panel noted that the federal acquisition workforce was not one of the topics assigned to it by Congress.(31) However, the Panel found that "there was a clear understanding from the beginning that we could not provide the insight and assistance that Congress sought without addressing the problems presented by the federal acquisition workforce".(32) The Panel found "a significant mismatch between the demands placed on the acquisition workforce and the personnel and skills available within that workforce to meet those demands".(33) Interestingly, in its Report, the Panel characterized the procurement workforce as separate from the major elements of the procurement system, stating: "we believed that there was a serious risk that problems stemming from the shortcomings of the acquisition workforce would be misunderstood as problems with the procurement system".(34) As noted above the Panel recognized that its investigation clearly identified the essential nature of the acquisition workforce to the effectiveness of these [various] elements of the federal acquisition system.(35) The link between the effectiveness of the procurement process and the acquisition workforce was reinforced by the Panel's conclusion that: "[u]ltimately, whether one focuses on the problem areas of the federal acquisition system, or on solutions designed to alleviate these problems for the future, the close link between the acquisition workforce and effective strategies for acquisition reform, is inescapable".(36)

Given the critical relationship between the Panel's proposed procurement reforms and the acquisition workforce, the Panel chose to devote an entire chapter to a discussion of recommended workforce improvements. The Panel suggested a bolstering of the U.S. acquisition workforce, recognizing that while "strengthening of the acquisition workforce will by no means be cost-free, continuing failure to invest in an appropriate sized and skilled

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(30) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit., ix.*

(31) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit., 327.*

(32) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit., ix.*

(33) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit., 327.*

(34) Despite the Panel's characterization of the procurement workforce as separate from the procurement process, as discussed above, the acquisition workforce is generally recognized as a critical element of a procurement system.

(35) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit., 327.*

(36) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit., 329.*

acquisition workforce will be far more expensive than making the required investment”.(37) Thus, investing in the creation of an educated and trained procurement workforce can not only benefit the procurement process, but also enhance the effectiveness of procurement reforms.

The Panel’s recommendations include an agency emphasis on a human capital management plan to ensure an agency’s procurement workforce needs are met:

In each agency, as part of the overall agency human capital management plan, the Chief Acquisition Officer should be responsible for creating and implementing a distinct acquisition workforce human capital strategic plan designed to assess and meet the agency’s needs for acquisition workforce.(38)

In addition, the Panel identified a set of issues to consider in assessing the role of the acquisition workforce in implementing reforms to the procurement system. Those noted below could be applied to any procurement system when introducing or assessing reforms:

- I. Is the existing acquisition workforce sufficient in numerical strength to perform the missions that it has been assigned in a manner that assures- to the extent reasonably practicable – the effective, efficient and lawful operation of the acquisition system?
- II. Is the existing workforce sufficiently qualified by background, aptitude, credentials, skills and training to perform the missions that it has been assigned in a manner that assures the effective, efficient and lawful operation of the federal procurement system?(39)

The Panel’s findings reinforce the close link between the quality of the procurement workforce and the ability to manage reform and make improvements to procurement processes. As noted by the Panel, the acquisition workforce must have the education and skills to meet the demands placed on it by the increasingly complex requirements of the procurement system.(40)

(37) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit.*, 329.

(38) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit.*, 373.

(39) *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress, cit.*, 351.

(40) Consistent with the AAP report, a DoD-sponsored report issued in May 2012 continues to note the importance of a skilled acquisition workforce. The authors of a U.S. Air Force sponsored report on reducing costs and increasing the efficiency of procurement spending make a number of recommendations, including building greater trust between agencies and contractors; an emphasis on performance-based contracting; focusing on best value; and retaining key people. T. R. CROOK – D. J. KETCHEN, JR. – J. G. COOMBS – J. D. PATTERSON, *Cutting Fat Without Cutting Substance*, in *Contract Management*, May 2012, 20. The authors note that people with “strong knowledge, skills, and abilities, are critical to an organization’s performance” and that “organizations that are able to identify and retain their best people are much more likely to be efficient and effective than those that do not”.

More recent studies and reports on the acquisition workforce add further support the Panel's findings with regard to the need for enhancing the capabilities of the procurement workforce. For example, a recent GAO report noted that building workforce skills and expertise is just as important as increasing the size of the acquisition workforce.<sup>(41)</sup> GAO further noted that agencies need to determine the specific occupations, skills, and competencies critical to achieving their missions and goals, and to identify any gaps between their current workforce and the workforce they will need in the future.<sup>(42)</sup> GAO concluded that by taking such steps, agencies would be in a better position to adjust to changes in technology, budget constraints, and other factors that alter the environment in which they operate.<sup>(43)</sup>

Along with the federal government, state procurement organizations in the U.S. also recognize the value of an educated, and specially trained procurement workforce. As noted earlier, in 2008, NASPO issued a research brief on developing a new generation of procurement professionals. Like the findings of the Panel, NASPO identified similar issues confronting the acquisition workforce at the state level. NASPO found that the increasing demands placed on state procurement officials under the various procurement reform efforts means that the traditional skill set is no longer sufficient:

*"To achieve administration goals of improving government efficiency at a lower cost of operation, procurement officers are being called upon more frequently to develop, negotiate and administer complex contracts for technology, data centers, telecommunications and other government services. These complex contracts, along with continuing privatization efforts and performance-based contracting trends, are piling increasingly intricate projects into the realm of procurement, leading to the conclusion that traditional skills and training for procurement officials will no longer be sufficient to meet the demanding objectives of a changing government."*

NASPO Research Brief 1. The NASPO Brief further noted the need for greater sophistication from the procurement workforce to award and administer these more complex procurements:

*"Procurement professionals now use more sophisticated sourcing tools, such as "best value" evaluation or selection methodologies that more closely approximate the value that contractors provide to government. More complex contracts,*

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(41) U.S. Government Accountability Office (GAO), Statement of John P. Hutton, Director Acquisition and Sourcing Management, *Acquisition Workforce: DOD's Efforts to Rebuild Capacity Have Shown Some Progress*, cit., 4.

(42) U.S. Government Accountability Office (GAO), Statement of John P. Hutton, Director Acquisition and Sourcing Management, *Acquisition Workforce: DOD's Efforts to Rebuild Capacity Have Shown Some Progress*, cit., 4.

(43) U.S. Government Accountability Office (GAO), Statement of John P. Hutton, Director Acquisition and Sourcing Management, *Acquisition Workforce: DOD's Efforts to Rebuild Capacity Have Shown Some Progress*, cit., 4.

*(including indefinite quantity or master contracts) better serve the entire state but require more sophistication from the procurement professionals who source, execute, and administer them.”(44)*

The NASPO report also notes that other procurement methods, such as contingency contracting, have become more of a strategic imperative for states, requiring different emphasis for procurement professionals and their roles. In general, as public organizations focus more on the strategic implications of performance management, procurement professionals find themselves in a continually evolving role.(45)

Consistent with NASPO’s findings, the state of California, which has the world’s 8<sup>th</sup> largest economy, has also recognized the need for a professional procurement workforce in light of the challenges of an advanced procurement system. A California Performance Review report entitled: *The State Needs to Professionalize its State Procurement Workforce*, summarized the findings as follows:

*“Generally, the skills associated with California’s procurement workforce are inadequate to meet the needs of a modernized procurement system. The modernization of the California procurement system will require professional procurement service providers skilled in the areas of, price and market analysis, negotiation, strategic sourcing, finance, acquisition planning, performance based contracting and contract administration. To develop such a workforce, the state will need to create new civil service classifications and develop and implement new training and skills development curricula.”(46)*

### 3.1. Conflicting Goals

Not only have public procurement methods increased in complexity, but other factors, add to the challenges that impact the procurement professional’s efforts in effectively implementing procurement practices and policies. These include the pursuit of sometimes conflicting goals. In 2002, Professor Steve Schooner, identified nine goals associated with government procurement systems: 1) competition; 2) integrity; 3) transparency; 4) efficiency; 5) customer satisfaction; 6) best value; 7) wealth distribution; 8) risk avoidance; and 9) uniformity.(47) Professor Schooner noted that no procurement system can

(44) *National Association of State Procurement Officials, Responding to an Aging and Changing Workforce, cit., 7.*

(45) *National Association of State Procurement Officials, Responding to an Aging and Changing Workforce, cit.,7.*

(46) *California Performance Review, Volume 4, Issues and Recommendations, Chapter 7: Statewide Operations: Section D: Procurement: SO61 The State Needs to Professionalize its State Procurement Workforce available at: [http://cpr.ca.gov/cpr\\_report/Issues\\_and\\_Recommendations/Chapter\\_7\\_Statewide\\_Operations/Procurement/SO61.html](http://cpr.ca.gov/cpr_report/Issues_and_Recommendations/Chapter_7_Statewide_Operations/Procurement/SO61.html).*

(47) S. L. SCHOONER, *Desiderata: Objectives For A System of Government Contract Law*, in *PPLR*, 2002, 103.

achieve all of the goals, and that determining which goals are most important “is a daunting, ever-evolving challenge”.(48) While there are “transactional, economic and social costs associated with maximizing transparency, integrity, and competition, Professor Schooner believes such costs are worthwhile.”(49)

Similarly, Professor Sue Arrowsmith has identified a related set of eight key objectives for a public procurement system: 1) Value for money (efficiency) in the acquisition of required goods and services; 2) Integrity – avoiding corruption and conflicts of interest; 3) Accountability; 4) Equal opportunities and equal treatment for providers; 5) Fair treatment of providers (offerors); 6) Efficient implementation of industrial, social and environmental objectives in procurement; 7) Opening up public markets to international trade; and 8) Efficiency in the procurement process.(50) Professor Arrowsmith notes that “some systems attach much more importance than others to the policies of fair and equal treatment of providers, to the use of procurement to promote social objectives or to accountability – with the result that the government may be willing to pay higher prices for goods or services or to accept greater process costs to implement these values”.(51)

Thus, as discussed by professors Schooner and Arrowsmith, public procurement systems seek to achieve a variety of goals/objectives in the acquisition of goods and services. Some of these goals complement each other, while others may pose conflicts. In the U.S., as elsewhere, the acquisition process is used as a means to implement sometimes unrelated, but important, policy goals, in addition to meeting agency requirements.(52) As discussed above, recent procurement reforms in the U.S., EU and elsewhere have promoted certain goals such as efficiency, transparency and best value. Both the U.S. and EU procurement systems also place great emphasis on promoting certain socioeconomic goals in the acquisition of goods and services, including small business participation, fair labor standards and policies to protect the environment. In many cases it is the procurement professional who must deal directly with these “conflicting values”, which often requires making two sets of decisions:

*“what makes sense economically and what is required from a policy standpoint. Their main goal is to buy the best product or service that will enable their team to meet its mission while adhering to an often complex and ever-changing set of policy guidance, law and regulation. They are the ones in whom we entrust, or upon*

(48) S. L. SCHOONER, *Desiderata: Objectives For A System of Government Contract Law*, cit., 103.

(49) S. L. SCHOONER, *Desiderata: Objectives For A System of Government Contract Law*, cit., 103.

(50) S. ARROWSMITH, *Public Procurement Regulation: An Introduction*, Asia Link, 2010, available at: <http://www.nottingham.ac.uk/pprg/documentsarchive/asialinkmaterials/publicprocurementregulationintroduction.pdf>, 4.

(51) S. ARROWSMITH, *Public Procurement Regulation: An Introduction*, cit., 5.

(52) M. GIBONEY – P. MCKEEN, *Capstone Course Topics In Federal Procurement*, cit., 16; *The Great Divide*, The Professional Services Council Acquisition Policy Survey, cit., 6.

*whom we impose, the responsibility for making reasoned business judgments that are in the best interests of the government.”*(53)

For example, awards to small businesses may result in higher costs but also promote the goals of wealth distribution and opportunities for those businesses that may not otherwise be able to compete for an award. Similarly, the requirement for certain wage requirements under a contract subject to the Service Contract Act may result in higher costs to the government, yet it promotes the goals of wealth distribution and the social objective of fair labor policies.

To effectively deal with these various policies and sometimes conflicting goals, the procurement professional must have a genuine understanding of the broader context in which the procurement system operates, including the overall goals of the procurement system. With that broader understanding, the procurement professional is better equipped to make sound judgments and decisions that balance the multiple goals and objectives of a public procurement system. This broader understanding can be best obtained through professional education. For example, the author discusses the concept of conflicting goals/values in his procurement courses, with good effect, to place the daily challenges of the procurement professional in a broader context.

The increasing complexity and conflicting goals also results from the globalization of the procurement process, which adds a additional layer to the procurement process that the procurement professional must sort through in awarding and administering contracts. For example, in the U.S., even at the state level, procurement officials must implement treaty obligations, such as those under the Agreement on Government Procurement (“GPA”) and the World Trade Organization (“WTO”).(54)

As discussed above, recent procurement reforms in the U.S., EU and elsewhere have pursued certain goals such as efficiency, transparency and best value. Both the U.S. and EU procurement systems also place great emphasis on promoting certain socioeconomic goals in the acquisition of goods and services, including small business participation, fair labor standards and policies to protect the environment. The imposition of a increasing number of goals on the procurement system inevitably leads to what can be referred to as “conflicting values”. As a result, a procurement professional may be faced with a situation where promoting small business participation artificially limits competition, or the imposition of certain employee wage requirements results in higher costs. Effectively managing these conflicting values requires a genuine understanding of the overall goals of a procure-

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(53) *The Great Divide*, The Professional Services Council Acquisition Policy Survey, *cit.*, 6.

(54) *National Association of State Procurement Officials, Responding to an Aging and Changing Workforce*, *cit.*, 9.

ment system which should be obtained through professional education. Thus, as noted above, the increasingly complex nature of the procurement process highlights the link between an educated and qualified procurement workforce and effective strategies for procurement reform.

#### ***4. Establishing A Professional Public Procurement Workforce***

The preceding discussion has argued that 1) the public procurement workforce is a critical element of a public procurement system; 2) the procurement process is inherently complex and has been made more so by continuing reforms and the adoption of new procurement policies and practices; and 3) promoting the effectiveness and integrity of a modern, complex procurement system demands a professionally educated workforce. The next question is then, how best to pursue the goal of a more educated workforce? Again, the lessons learned from the U.S. experience provide useful guidance.

We can begin by examining the current state of efforts to educate and train the procurement workforce in the U.S. While the reports and studies noted above emphasize the current need for a professional procurement workforce, Congress has sought to address this issue since the early 1990s. The Defense Acquisition Workforce Improvement Act (10 U.S.C. § 1744-46) and section 4307(a) of the Clinger Cohen Act established education, training and experience requirements for entry and advancement in the procurement field for DoD and civilian agencies. In 2005, pursuant to this legislation, the OFPP issued Policy Letter 05-01, *Developing and Managing the Acquisition Workforce*, to establish a framework for creating “a federal acquisition workforce with the skills necessary to deliver best value supplies and services, find the best business solutions, and provide strategic business advice to accomplish agency missions”. The Policy Letter identifies the various positions within the acquisition workforce and includes guidance for agencies to effectively manage the workforce. The Policy Letter calls for a framework of certain core competencies that acquisition personnel should possess. In terms of education, the Policy Letter calls for certification programs that “reflect a government-wide standard for education, training, and experience leading to the fulfillment of core competencies in a variety of acquisition-related disciplines.”

While the legislation and Policy Letter offer a framework for developing a professional procurement workforce, the results have fallen short. This is due in part to the fact that until recently, the federal government failed to address the reductions in the procurement workforce that occurred in the 1990s. However, as noted by Dan Gordon, the former head of OFPP, the acquisition

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workforce crisis is more significant than the mere decline in numbers because training and stature also suffered over the past 20 years.<sup>(55)</sup> Gordon adds that in recent years, virtually every key role in acquisition planning, as well as in contract management, has been overstretched, undertrained and undervalued. *Id.* in addition, the training programs, discussed in more detail below, offered by the Defense Acquisition University (“DAU”) and the Federal Acquisition Institute (“FAI”) have been criticized as being inadequate for purposes of creating a genuinely professional public procurement workforce. Criticisms of the DAU/FAI approach find it overly rules-based with a superficial discussion of procurement topics that is often devoid of any in-depth examination and analysis of any particular topic.<sup>(56)</sup>

#### 4.1. The DAU/FAI Model

The DAU and FAI, which administer the acquisition workforce certification programs, have existed since the 1970s. They were established to promote a professional acquisition workforce and offer education, training and related activities to DoD and civilian agency acquisition personnel. The DAU and FAI programs offer three levels of certification, for a procurement professional, based on levels of experience, training and education. Generally, an applicant must possess a baccalaureate degree with 24 semester hours of business related courses. The candidate is required to complete a set of training courses offered by DAU and FAI, covering a range of procurement topics, such as Contracting Fundamentals and Fundamentals of Cost and Price Analysis. Although these courses are designed to provide fundamental knowledge in core competencies, critics have been rather pointed in their criticism of the DAU/FAI training approach. A fundamental problem is that the procurement courses attempt to cover a wide range of material in a compressed timeframe that precludes a rigorous, in-depth analysis of fundamental principles and concepts that can be applied to a variety of situation and promote sound judgment. As noted by Mr. Edwards:

The standard approach to classroom training in both Government and commercial classes is the lecture seminar: two to ten days, six to seven hours of lecture per day, in which one or more instructors talk about broad topics such as “source selection,” “contract pricing,” and “inspection and acceptance.” Instructors are usually current or former contracting personnel. They lecture and lead discussions, using PowerPoint® or something like it to project key

<sup>(55)</sup> D. I. GORDON, *Reflections On The Federal Procurement Landscape*, in *The Government Contractor*, 2012, Vol. 54, No. 7, 51, also available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2018405](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2018405).

<sup>(56)</sup> V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, Nash & Cibinic Report, January 2008.

points on a screen. Students receive copies of the slides and other handouts and sometimes a “course manual.” There are few if any *textbooks*, as that term is commonly understood. “Case studies” usually consist of brief descriptions of simple situations that are read and discussed in class. Students rarely if ever receive homework, and in many cases there is either no final examination or one consisting mainly of true-or-false or multiple-choice questions. The number and range of topics covered in a classroom session often preclude in-depth exploration and analysis of any particular topic. Government Accountability Office, board of contract appeals, and court decisions are discussed but are not analyzed in depth. Failing a course is generally not an option--everyone passes. Ordinarily, the only real requirement for successful course completion is attendance.(57)

Similar assessments of acquisition workforce training and education have also identified concerns regarding the emphasis on rules-based training. For example, the findings of the bi-annual Professional Services Council Procurement Policy Survey also note the need for improved training to develop more sophisticated business judgment and analytical skills, rather than a rules-based approach, on the part of the acquisition workforce:

Several interviewees stressed the need for better training with a specific focus on the procurement and management of *services* – business skills, analytical skills and management skills. “There is a numbers issue, but even if we solved the numbers issue tomorrow, it wouldn’t fix our problems,” observed an oversight professional. “The current acquisition workforce doesn’t have sophisticated business judgment. They are good at following the rules, but when the rules lead you to an illogical conclusion, you need judgment. Acquisition is more of an art than a science”.(58)

Similar observations are made throughout the Procurement Policy Survey. Thus, in part, the shortcomings in the U.S. framework for developing a professional procurement workforce is due in part to its emphasis on rules based “training” rather than a more in-depth “education” approach.

#### 4.2. Training versus Professional Education

In discussing the development of the U.S. acquisition workforce, the terms “training” and “education” are often used. It is important to clarify the difference between these terms. Edwards offers a useful distinction:

*Training* teaches specific skills – -how to do something – -and is ordinarily designed to teach the trainee how to execute specific processes in an orthodox

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(57) V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, cit., 1-2.

(58) *The Great Divide, The Professional Services Council Acquisition Policy Survey*, cit., 9.

way to obtain predictable results. *Professional education* on the other hand teaches rules, concepts, theories, principles, and general skills (such as market research and decisionmaking).(59)

Given this distinction, Edwards believes the FAI, DAU, and commercial providers should focus on “education” rather than “training”, which should be done primarily on the job.(60) Importantly, Edwards adds that professional education should provide foundational knowledge e.g., “[a] solid foundation in rules, concepts, theories, and principles enables a practitioner to cope with the new and unfamiliar, adapt to circumstances, improve existing processes, and innovate. Professional education classes should be focused, deep, intense, and demanding”.(61)

#### 4.3. Training and Principal Agent Model

Before turning to the discussion of professional education, the importance of training for the procurement professional should be noted. While institutions such as the DAU and FAI, and others, such as universities, should focus on education rather than training, it remains a critical element in the development of the procurement professional. Edwards notes that procurement personnel learn most of what they know about their work through on-the-job training. Thus, it is important that such training is effective. Edwards suggests that successful on-the-job training makes use of the senior, experienced personnel to serve as mentors to the trainees. Ideally, such mentors should possess appropriate professional knowledge and experience, along with the ability to convey that knowledge and experience in a learning environment.(62) As has been recognized in other procurement systems, these mentors must also be taught to train and have an understanding of what the trainees will learn in the classroom.(63)

In addition to enhancing the skills of the procurement workforce, Edward’s approach to on-the-job training can also serve to promote the convergence of the interests of the principal (public procurement authority) and the agent (the contracting professional).(64) By giving the senior employee “mentors” a role

(59) V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, cit., 3.

(60) V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, cit., 3.

(61) V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, cit., 3.

(62) V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, cit., 4.

(63) V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, cit., 4.

(64) See for example a discussion of the principal-agent theory as applied to public procurement in C. R. YUKINS, *A Versatile Prism: Assessing Procurement Law Through The Principal-Agent Model*, in *PCLJ*, 2010, Vol. 40, 64: “The theory builds upon the classic principal-agent model. A *principal* enlists an *agent* to carry out the principal’s goals, presumably because the agent enjoys some comparative advantage in performing the goals. Inevitably, however, the agent’s interests diverge from the principal’s; if the agent’s goals diverge sufficiently, the agent may be said to have a *conflict of interest*”.

in training new employees, these mentors will arguably gain a greater stake in the outcomes of the agency (principal). Under Such an approach is consistent with efforts made at the Environmental Protection Agency (“EPA”). To improve the performance of its Office of Acquisition Management (“OAM”), the agency established four strategic goals: to have a competent and qualified workforce, to enhance the corporate image and provide business leadership, to optimize business processes, and to strengthen the link to EPA’s mission. EPA then established one group comprised of staff members for each of its goals. By forming these groups, OAM got its staff actively involved in implementing the strategic goals. This initiative gave the contracting staff a greater stake in the process and improved morale by allowing them to implement ideas based on their practical experience. As a result of this approach, the agency has noted improved efficiency and greater use of its contracting vehicles.

#### 4.4. The University Model

As discussed above, training has its place in enhancing the skills of the public procurement workforce. However, the available evidence suggests that the rules-based training model offered by DAU/FAI and others is insufficient for creating the professional workforce a modern procurement system demands. Therefore, moving to a more demanding university-based education program should be a key element in the effort to achieve this result. A program of study based on university-based courses offers the opportunity for the procurement professional to obtain the foundational knowledge of concepts, theories, and principles necessary to enhance the business judgment and adaptability of the procurement professional and encourage a sound approach to innovation.

In terms of formal education in public procurement, universities have traditionally focused on the lawyer rather than the procurement professional. As Khi Thai noted some years ago, “[a]lthough public procurement is perceived as a major function of government, and although governmental entities, policy makers and public procurement professionals have paid a great deal of attention to procurement improvements or reforms (...) no university offers a public procurement program even though over 103 colleges and universities offer courses, certificate programs, bachelor, master and Ph.D. in business programs with emphasis in purchasing, materials management, logistics, supply management, or related areas”.<sup>(65)</sup> Thus, given the need as discussed throughout this chapter, an opportunity

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(65) K. V. THAI, *Public Procurement Re-examined*, in *Journal of Public Procurement*, 2000, Vol. 1, 10.

exists for universities to assume a larger role in the professional education of the procurement workforce.

In many ways, limiting the academic study of procurement largely to the legal profession has arguably limited the impact of the valuable findings from this study of the procurement process. Including the procurement workforce in the academic discussion of procurement concepts and theories can not only further the goal of a achieving a professional procurement workforce, but also serve to broaden the impact of the scholarly study of public procurement. It is important for the procurement professional to have a sense of the elements and goals of a procurement system and related concepts. Conveying that knowledge to the broader procurement community also benefits the academic community as its profile and influence in the broader procurement community is raised.

#### 4.5. University courses and the procurement professional

Some universities are currently active in offering a program of study for the contracting professional. The author teaches several public procurement courses to members of the acquisition workforce, both those working for government purchasing authorities and for commercial contractors. Although the courses are part of a certificate program, rather than a degree program, they are standard 3 credit-hour courses, which follow the university's academic calendar. Importantly, the courses 15 week schedule provides an opportunity for the type of in-depth study and discussion of procurement concepts, theories and principles that can provide a foundation of knowledge on which the procurement professional can operate in a variety of situations. Additionally, unlike the DAU/FAI courses, which are limited only to government employees, university courses, such as those taught by the author, are open to both industry and government procurement professionals. Thus, students benefit from an exchange of ideas and different perspectives on the various procurement issues, which again, enhances the procurement professional's broader understanding of the procurement process.(66)

Greater use of the university model to formally educate the procurement workforce can assist in establishing a professionally educated workforce. University certificate programs geared toward the contracts professional are a viable option, particularly if such programs are done in coordination

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(66) Edwards notes that mixed classes of government and industry personnel are best, and the homogeneity of FAI and DAU courses contributes to "parochialism and myopia" in the government workforce. See V. EDWARDS – R. NASH – J. CIBINIC, *Improving Training For The Contracting Workforce*, *cit.*, 2.

with public procurement authorities. The involvement of universities in this education effort could also include course texts that are designed for the procurement professional. Khi Thai at the Florida Atlantic University, has undertaken such an effort. Consideration should also be given to creating degree program for the procurement profession, particularly in areas with a concentration of procurement professionals. Such programs could include existing courses from other disciplines, such as business administration, project management, public administration and law.(67) In fact, the George Washington University in Washington, D.C. recently established a Master of Science in Government Contracting, which is “designed to give working professionals the knowledge and skills necessary to excel in the world of Federal acquisition, and is intended for professionals from a variety of acquisition-related jobs in both Government and private industry”.(68) Expansion of these university based certificate and degree programs in public procurement can raise the profile of the procurement profession while attracting qualified candidates to further the goal of a professionally educated workforce.

### ***5. Discretion in the Selection of Award Criteria and the Contract Award Process***

The preceding discussion highlights the importance and the benefits of education and training for the procurement workforce. As noted, a more professional public procurement workforce can assist in the efforts to curb corruption and promote the integrity of a public procurement system. For many procurement systems, efforts have focused on preventing collusion among tendering parties, along with ensuring the integrity of the award selection process. One element, as discussed by other contributors to this text, is the proper use of discretion by public procurement authorities. Again, lessons learned from the U.S. experience can provide useful insights. Discretion, when used by procurement officials, offers the potential for misuse and mistakes, however, limits can be set on the exercise of such discretion to promote its proper use. Under the U.S. federal procurement system, agency procurement officials enjoy broad discretion in defining a requirement to

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(67) The recent emphasis of the academic community, particularly in the U.S., on online education offers additional opportunities for educating the acquisition workforce. The university program under which the author teaches makes extensive use of online education. This experience has enabled the refinement of the use of this educational tool to effectively teach the procurement professional. The effective use of online education offers greater flexibility in coordinating efforts to educate the busy procurement professional while also expanding its potential reach within the procurement community.

(68) See: the University's website at: <http://business.gwu.edu/msgc/>.

best meet the agency's needs.(69) The regulation addressing an award decision also emphasizes the independent judgment of the procurement official with responsibility for awarding a contract: "[w]hile the SSA [source selection authority] may use reports and analyses prepared by others, the source selection decision shall represent the SSA's independent judgment".(70) This discretion is recognized in both the procurement regulations and the applicable case law.(71)

While discretion remains a key element of the U.S. federal procurement process, such discretion must be exercised in a manner that is consistent with the goal of ensuring the integrity of the process and fairness to all participants. Under U.S. procurement law, it remains a fundamental principle of competitive procurements that competitors be treated fairly.(72) Thus, agencies must select evaluation criteria in a manner designed to achieve full and open competition.(73) Therefore, while procurement officials have broad discretion in selecting the award criteria for a particular requirement, these criteria must reflect the agency's actual needs and not prevent otherwise eligible contractors from bidding. If an offeror believes the award criteria are unduly restrictive or tailored to the advantage of a particular offeror, it may file a protest for a determination on whether the award criteria are proper. This element of a bid protest provides transparency to the award process and acts as a check and balance on the discretion of procurement officials. The protest process also ensures that the source selection process is closely scrutinized to ensure that agencies make proper use of award criteria and that they follow those criteria once they have been announced in the solicitation. Thus, the U.S. procurement system places certain limits and checks on agency authority in the evaluation and award process in an effort to promote the proper use of discretion.

(69) The Government shall exercise discretion, use sound business judgment, and comply with applicable laws and regulations in dealing with contractors and prospective contractors. All contractors and prospective contractors shall be treated fairly and impartially but need not be treated the same. FAR 1.102-2(c)(3), Performance standards.

(70) FAR 15.308, Source selection decision.

(71) Agencies enjoy broad discretion in the selection of evaluation criteria, and GAO will not object to the use of particular evaluation criteria so long as they reasonably relate to the agency's needs in choosing a contractor that will best serve the government's interests. *SML Innovations*, B-402667.2, Oct. 28, 2010, 2010 CPD, 254; "The determination of the agency's minimum needs and the best method of accommodating them is primarily within the agency's discretion." *Leon D. DeMatteis Construction Corp.*, B-276877, Jul. 30, 1997, 97-2 CPD, 36.

(72) *The Boeing Co.*, B-311344 et al., June 18, 2008, 2008 CPD, 114 ("It is a fundamental principle of competitive procurements that competitors be treated fairly ...").

(73) *VSE Corporation; Johnson Controls World Services, Inc.*, B-290452.3, B-290452.4, B-290452.5, May 23, 2005, 2005 CPD, 103 ("Under the Competition in Contracting Act of 1984 (CICA), 41 U.S.C. 253(a)(1)(A), contracting officers have a duty to promote and provide for competition and to provide the most advantageous contract for the government. In doing so, contracting officials must act affirmatively to obtain and safeguard competition; they cannot take a passive approach and remain in a noncompetitive position where they could reasonably take steps to enhance competition.")

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The U.S. experience with the award phase of the procurement process also highlights the need for an educated workforce. The findings from a recent report on bid protests involving Department of Defense procurements are consistent with the findings discussed elsewhere in this chapter.<sup>(74)</sup>

Mistakes in the award process that lead to protests, cause a disruption in the contracting process. Maser notes that when procurement officials do not fully understand a requirement they may be unaware of problems they are creating. Thus, one recommendation offered to address this problem is to simplify requirements.<sup>(75)</sup> In addition, as with the findings of other reports noted in this chapter, Maser states that agencies must invest in educating the decision-makers engaged in selecting sources.<sup>(76)</sup> Maser observes that source selection officials need the “legal, financial, and engineering knowledge to be conversant with major stakeholders in the process and that simply knowing the rules and regulations is not the same as genuinely understanding business sufficiently to interact with offerors”.<sup>(77)</sup>

Therefore, as discussed above, with adequate preparation, transparency and oversight, procurement officials can make effective use of discretion in the award process and throughout the procurement cycle.

## 6. Conclusion

The U.S. experience in the effort to improve the capabilities of its procurement workforce offer valuable lessons for other procurement systems. There are two primary points from the preceding discussion. First, given the central role of the procurement workforce in the procurement process, when assessing the effectiveness and integrity of a public procurement system, consideration must be given to the capabilities of the system’s procurement workforce. Second, the effectiveness of public procurement reforms can be enhanced by efforts to develop a professionally educated workforce.

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(74) S. M. MASER, *Improving Government Contracting: Lessons from Bid Protests of Department of Defense Source Selections*, Improving Performance Series, 2012 at 7, notes that more complex procurements increase the risk for mistakes in the award process: “Especially for service contracts, it is difficult to do performance monitoring. The more difficult it is to define outcomes, the more likely the agency will set input requirements. More input requirements lead to more evaluation criteria. More evaluation criteria create more opportunities for protestable errors”. Available at: <http://www.businessofgovernment.org/report/improving-government-contracting-lessons-bid-protests-department-defense-source-selections>.

(75) S. M. MASER, *Improving Government Contracting: Lessons from Bid Protests of Department of Defense Source Selections*, *cit.*, 8.

(76) S. M. MASER, *Improving Government Contracting: Lessons from Bid Protests of Department of Defense Source Selections*, *cit.*, 8.

(77) S. M. MASER, *Improving Government Contracting: Lessons from Bid Protests of Department of Defense Source Selections*, *cit.*, 8.

Regarding the first point, key questions (as suggested by the AAP) that should be asked in assessing the status of a procurement system:

- I. Is the existing acquisition workforce sufficient in numerical strength to adequately perform the missions that it has been assigned?
- II. Is the existing workforce sufficiently qualified to perform the missions that it has been assigned in an effective, efficient and lawful manner?

With regard to the second point, improvements in the effectiveness, efficiency and lawfulness of a public procurement system can be promoted by establishing a professionally educated workforce through greater use of a substantive, university-based education approach. A more educated and highly trained acquisition workforce will be better prepared to effectively face the challenges of the increasingly complex nature of public procurement.

## CHAPTER 2

### Front-line public servants, discretion and corruption

BY

André SADDY

Adjunct Professor, Federal Fluminense University

#### *1. Introduction*

A primary objective of the research is to establish a correlation in public procurement between the level of corruption, bureaucracy and discretion existent in the lower hierarchy of Public Administration – more specifically in front-line public servants. The main objective is to verify the relationship between those ideas and understand the causes and impacts of corruption exercised by those public servants when participating in any type of commission that selects the most advantageous proposal to the Public Administration, as well as the factors that facilitate resistance to corruption by citizens or participants for those types of procurements at individual and collective levels.

Studying the characteristics of those characters (enterprises/citizens and front-line public servants) is fundamental to understanding this kind of threat to the rule of law and the corruption that is endemic to the society we live in.

Likewise, we believe that this study will add to other research conducted in the context of the corruption research line, developed by other institutions. We normally see scholars studying the predominance of corruption in the Southern hemisphere and investigating in what sector the problem of corruption is particularly prevalent, such as public works, construction, arms and the defence industry, but not focussing on the front-line public servants.

Doctrine normally effects those that work in the high levels of the administrative hierarchy, such as the administrative elites and the managers and supervisors but not as we have stated, not on front-line public servants. Perhaps the level of the corruption in this field is less, here the Swiss bank account does not enter in the equation, but the amount does not matter because the importance is the cost that it brings to society.(1)

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(1) Bidders often form a cartel to manipulate the public procurement with or without the involvement of a corrupt inside official. Collusion agreements can include, for example, assigning “turns” among the cartel members for winning public bids, or agreeing to internal compensation payment for

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So despite knowing that corruption exists in different areas, this research will focus solely on front-line public servants acting in public procurement in two scenarios: those that work in the field and those that work inside an office. Both have different margins of freedom, utilize the public machine in distinct ways and have diverse opportunities to commit corrupt acts. Our task is to establish the correlation between the level of corruption, the bureaucracy and discretion in those servants that have contact with citizens and enterprises in their normal routine work days in a public procurement.

## 2. Public procurement

Public procurement is an instrumental administrative procedure designed to select the most advantageous proposal to the Public Administration guaranteeing equality in the selection.<sup>(2)</sup> It is a very lengthy, laborious and costly procedure and that is why in some countries it is not a mandatory procedure for the award of a public contract. It is by this procedure that the Administration purchases goods and services from the private sector and usually is subject to specific rules and policies covering how the relevant decisions are made.

Identifying this most advantageous proposal to the Administration means the selection of the contractor that provide the best conditions to meet the public interest, in view of not only the price but also the technical capability, product quality, etc.

To achieve this purpose, the Administration must comply with all principles relating to its exercise, after all, the advantage will be satisfied if the public interest is reached. It may be correct to imagine that the best course for the Administration is to minimize spending, to place less burden on the public treasury, and force the private sector to do the best and most complete performance possible. However, the situation of lower cost may not always result in greater benefit to the Administration.

This “advantageousity” is relative. Sometimes the lower cost does not lead to the most advantageous proposal. The benefit will depend greatly on the nature of the contract, so just the circumstances that will determine which proposal is most advantageous to the Administration. The “advantageousity” derives not only

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submitting high or other “*failed*” bids. That type of corruption will not be the object of this research unless it involves the participation of *front-line public servants*.

(2) Public procurement may account for 45% of government expenditure and up to 20% of the Gross Domestic Product for any country. Setting aside government salaries and social service payments, public procurement accounts for the largest share of public expenditures for all levels of government. Worldwide, public procurement is also estimated to equate to 80% of world merchandise and commercial services exports for 1998. (see OECD, *Fighting Corruption and Promoting Integrity in Public Procurement*, 2005, available at: [http://www.oecd.org/document/35/0,3746,en\\_2649\\_34855\\_38447139\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/35/0,3746,en_2649_34855_38447139_1_1_1_1,00.html) and *The Size of Government Procurement Markets of 2002*, available at: <http://www.oecd.org/dataoecd/34/14/1845927.pdf>).

from the burden but also from the quality and capacity. Therefore, the advantage is not related solely and exclusively with financial matters, the State must receive satisfactory performance, with quality that is carried out by capable persons.

It is also important mention that public procurement must also be realized with isonomic. This means that it is necessary but not sufficient simply to select the most advantageous proposal. One has to respect the Law itself and all boundaries within the existing legal system, especially the equality.

### 3. *Corruption*

The changes that the world has seen in recent years have many contributing factors, one of them perhaps, is the endemic corruption that exists in all countries these days. Since the introduction of the Welfare State and the increase in State intervention in the economic and social order, corruption and bureaucracy has increased.

At the same time we have observed this increase in corruption during the 20th century, over the last decades there has been also a marked increase in the understanding of corruption's ills and the need to prevent, mitigate and combat it. But even after some decades of driving progress and achieving success in the fight against corruption, we recognize that significant challenges remain.

Indeed, despite the cost of corruption being impossible to quantify, its impact on the political, economic, social, and environmental areas is evident.<sup>(3)</sup>

Corruption and its effects are a global dilemma. From small bribes paid to any public servant to the holding of stolen assets by banks, the impacts from these abuses on states and citizens are the same: the undermining of the rule of law, the violation of rights, opaque institutions, lost public resources and weakened national integrity.

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(3) On the political front, corruption constitutes a major obstacle to democracy and the rule of law. In a democratic system, offices and institutions lose their legitimacy when they are misused for private advantage. Though this is harmful in the established democracies, it is even more so in newly emerging ones. Accountable political leadership cannot develop in a corrupt climate.

Economically, corruption leads to the depletion of national wealth. It is often responsible for the funnelling of scarce public resources to uneconomic high-profile projects. Furthermore, it hinders the development of fair market structures and distorts competition, thereby deterring investment.

The effect of corruption on the social fabric of society is the most damaging of all. It undermines people's trust in the political system, in its institutions and its leadership. Frustration and general apathy among a disillusioned public result in a weak civil society. That in turn clears the way for despots as well as democratically elected yet unscrupulous leaders to turn national assets into personal wealth. Demanding and paying bribes become the norm. Those unwilling to comply often emigrate, leaving the country drained of its most able and most honest citizens.

Environmental degradation is yet another consequence of corrupt systems. The lack of, or non-enforcement of, environmental regulations and legislation has historically allowed the North to export its polluting industry to the South hemisphere. At the same time, careless exploitation of natural resources, from timber and minerals to elephants, by both domestic and international agents has led to ravaged natural environments. Environmentally devastating projects are given preference in funding, because they are easy targets for siphoning off public money into private pockets.

Transparency International has defined corruption as the abuse of entrusted power for private gain. This can be 'according to rule' corruption or 'against the rule' corruption. Facilitation payments, where a bribe is paid to receive preferential treatment for something that the bribe receiver is required to do by law, constitute the former. The latter, on the other hand, is a bribe paid to obtain services the bribe receiver is prohibited from providing.

It is important to note that bribes do not take only monetary form: favours, services, presents and so on are just as common.

Some believe that keeping corruption in check is only feasible if representatives from government, business and civil society work together to agree on a set of standards and procedures they all support. Others believe that corruption cannot be rooted out in one fell swoop. Rather, fighting it is a step-by-step, project-by-project process.

Corruption involves distrust in politics and law and it undermines the working of the economy as well as the implementation of policies. This is the principal reason any country should study the causes and impacts of corruption and the resistance to corruption itself. It is important to study corruption because the effectiveness of internal policies in areas such as transport, energy, telecommunications, and environmental protection, as well as its external policies – e.g. development assistance, trade – is influenced by the issue of corruption. The credibility of any country and all national institutions and policies relies upon, among other things, its own integrity and on its ability to prevent and fight corruption.

Different experiences exist within countries with regard to how corruption is perceived, its scope and nature, whether it is linked to specific forms of organised crime and how it can be fought – including with a more or less prominent role, legislative measures, anti-corruption institutions or agencies, the use of media and advocacy in unveiling corruption.

However, no country is spared and the phenomenon calls for comparative analysis of different cultures of corruption, identification of good practices and cooperation at EU and international levels.

#### ***4. Public servant in public procurement***

There are different public servant levels in the hierarchy of the Public Administration that deal with bureaucracy that have some level of discretion. Basically three levels exist: administrative elites; managers and supervisors; and street-level bureaucrats. All of them deal with bureaucracy and also with corruption in different ways.

In any public procurement we can observe the presence of those basic three types of public servants. Normally, there is the person that authorizes the expenditures (administrative elites), the head of the Administration (managers and supervisors), and the responsible members of the bid committee

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and support team (street-level bureaucrats). We will focus specific on street-level bureaucrats and more specifically on front-line public servants.

#### 4.1. Concept of Front-line public servants

The original idea of “street-level bureaucrats” emerged in 1974 and it is attributed to Michel Lipsky(4) who defined them as the individuals representing the Administration directly to their citizens while exercising discretion in doing so.(5) They are the ones that deal with some of the most persistent and troubling problems in society,(6) because they are the ones that manipulate bureaucracy on a daily basis and also because they regularly exercise significant amounts of discretion in the process of their work(7) and are therefore open to receiving proposals of corruption.

This concept has been continuously developed since then and different definitions and points of view are emerging. Keith Hawkins(8) speaks of “‘field’ or ‘street’ level whose work as a ‘screening’ or ‘gatekeeping’ official means direct contact with the difficulties of the real world”. Matthew Diller(9) calls them “ground-level administrators” and “low-level administrators”. Others such as David Osborne and Ted Gaebler(10) utilize “front-line workers”.

We prefer to call them front-line public servants and we believe in the existence of at least two types: those that work in the field or on the street and those that work

(4) M. LIPSKY, *Street-level bureaucracy: dilemmas of the individual in Public Services*, New York: Russell Sage Foundation, 1974, 7 et seq.

(5) Also talk about discretion in this sense: E. BARDACH – R. KAGAN, *Going by the book: the problems of regulatory unreasonableness*, Philadelphia: Temple University Press, 1982; D. TANNER, *Empowerment and care management: swimming against the tide. Health and Social Care in the Community*, Hoboken, v. 6, n. 6, 447-457, nov., 1998; K. CORAZZINI, *Case management decision-making: goal transformation through discretion and client interpretation. Home Health Care Services Quarterly*, Philadelphia, 2000, v. 18, n. 3, 81-96.

(6) J. C. VINZANT – L. CROTHERS, *Street-level leadership: discretion and legitimacy in front-line public service*, Washington, DC: Georgetown university press, 1998, ix, 3-6.

(7) J. C. VINZANT – L. CROTHERS, cit., 35, states: “Street-level servants often confront situations that are ambiguous, complicated, unpleasant, and sometimes even dangerous. In making decisions about how to handle these situations, there are multiple and sometimes competing variables which can influence their choices. In balancing these pressures, workers exercise discretion. A consideration of the legitimacy of those discretionary choices is necessary not only to improve the effectiveness of their choices, but also to fully understand worker discretion in the context of governance”. Based on those concepts asserts that the decision will be lawful if they have at least acquiescence and acceptance of the political order as generally reasonable and complete. They bring many doctrines claiming that discusses and argue that: “legitimate administrative discretion should be seen as a matter of constitutional principle (Rohr 1986), conservatorship (Terry 1990), morality and ethics (Lovich 1981; Jos 1990), personal responsibility (Harmon 1990) stewardship (Kass 1990), practical wisdom or phronesis (Morgan 1990), citizenship (Cooper 1991), a means to check the power of politicians (Spicer 1990; Spicer and Terry 1993), and even potential heroism (Bellavita 1991)”.

(8) K. HAWKINS, *Using judicial discretion*, in K. HAWKINS (ed.), *The Uses of Discretion*, Oxford: Oxford University Press, 1992, 12.

(9) M. DILLER, *The revolution in welfare administration: rules, discretion, and entrepreneurial government*. New York University Law Review. New York, v. 75, n. 5, 1121-1220, nov. 2000, 1129 and 1173.

(10) D. OSBORNE – T. GAEBLER, *Reinventing Government: how the entrepreneurial spirit is transforming the public sector*, Reading: Addison Wesley, 1992.

inside an office. Both can exercise formal or informal rules and decision-making but there will be always individual decisions, some recurring, others not.

Both types of front-line public servants, as we have described, deal with different types of problems in society, manipulate bureaucracy and are able to exercise significant amounts of discretion in their jobs but the work environment is diverse. Those that work in the field or in the street cannot depend on their supervisors or the rules to make decisions. They do not work under the direct observation of their supervisors. They are usually geographically distant from them and the location of their work is usually imprecise. They have to make decisions on the spot, which means that they have to make decisions alone. Otherwise they must choose the procedure *in situ* and execute their decision immediately.<sup>(11)</sup> On the other hand, the inside officers are normally well known where they are. The environment is more predictable and much less volatile. They are directly supervised by the hierarchical servant and they can also make their decisions with the help of other people.

Examining the front-line public servants in the public procurement we can affirm that almost all servants involved in the procedure (responsible, members of the bid committee and support team) are inside workers.

Those inside workers cast three essential characteristics: discretion,<sup>(12)</sup> visibility<sup>(13)</sup> and vulnerability of certain areas.<sup>(14)</sup>

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(11) M. LIPSKY, *Street-level bureaucracy: dilemmas of the individual in Public Services*. New York: Russell Sage Foundation, 1974.

(12) Discretion refers to the nature of the power conferred and how it is exercised. Can be defined as the relative margin of freedom, independence or volition conferred by law to the public servants, for the adoption or not of a decision between the legal consequences offered alternatives and disjunctively that best serves the public interest. The exercising of discretion by front-line public servants exists even where they are, in principle, most strictly constrained by procedural regulations. In practice, when enforcing a law, those servants exercise enormous discretion. Field observation studies demonstrate this point (W. K. MUIR, *Police: street-corner politicians*, Chicago: University Press, 1977; M. BALDWIN, *Care Management and Community Care: Social Work Discretion and the Construction of Policy*, Aldershot: Ashgate, 2000). If the situation is so, why give this prerogative. The doctrine gives different reasons aspiring to optimum realization of the purposes of the law, preserving fair treatment of the parties involved and others. Otherwise sometimes citizens cannot execute some actions without the help of State forces. Citizens cannot impose on the other party through private coercion, but must defer to the State to give him the assistance of public coercion (the only legitimate form). Public Administration has this power included in its prerogatives. It does not need to interdict, it can use its own compulsion to defend or regain, e.g. certain possessions. Discretion is neither good nor bad. In certain circumstances it may be an important professional attribute, in other circumstances it might be a pretext for those responsible for political decisions to hide behind or can be an opportunity for the abuse of power.

(13) Visibility is strictly related to discretion. A large proportion of front-line public servants who have direct contact with citizens in the course of their activities, are in a situation of low visibility, where many of their actions are not witnessed either by their superiors or by other citizens who are not in contact with them. All institutions should be concerned with overseeing the work of their agents. However, often the multitudes of situations, mobility, geographic dispersion, limited resources, among other factors, lead to many of the activities going entirely unsupervised. Front-line public servants should be especially vigilant when their companies engage in this area of work.

(14) Vulnerability arises because there are certain functions which by their nature and type of activity, lead to a greater vulnerability and to the occurrence of errors, even illegalities. Front-line public servants are more susceptible to creating such opportunities and because of this such areas must be more guarded.

#### 4.2. Front-line public servants as public policies makers

The doctrine also says that these types of workers are significantly enmeshed in politics. As they are engaged in the distribution of services or the regulation of social behaviour, front-line public servants are subject to the contending claims of political groups and interests. What they do has demonstrable political consequences.(15)

This happens because of the discretion they have to make decisions. Decision – making in Public Administration is in accordance with K. J. De Graaf, J. H. Jans, A. T. Marseille and J. De Ridder(16) “fact of life: members of the public are confronted with them all the time”. Thus, for those authors the quality of administrative decisions obviously matters to people in at least three senses: “First of all, when issuing administrative decisions, public authorities should treat citizens according to their rights, including the right to equal treatment and the right to legal certainty. Secondly, the rights of third parties should be protected; for instance, they should not suffer from the external effects of an administrative decision without adequate compensation. Thirdly, the public is entitled to the protection of general public interests”. Goals, laws and guidelines must be interpreted by these agents and when that happens they create an organizational policy.(17)

The feature of public policy maker was developed by Kenneth Culp Davis(18) who argued in 1969 that front-line servants are important policy makers in our society, after all it is they who must decide what to do when faced with a problem.

Michel Lipsky(19) also argues that public policy is indeed what the street agents do. He states that: “street-level bureaucrats make policy in two related respects. They exercise wide discretion in decisions about citizens with whom they interact. Then, when taken in concert, their individual actions add up to agency behaviour”.

(15) M. K. BROWN, *Working the street: police discretion and the dilemmas of reform*, New York: Russell Sage Foundation, 1988, 34.

(16) K. J. DE GRAAF – J. H. JANS – A. T. MARSEILLE – J. DE RIDDER, *Quality of Decision-Making in Public Law: Studies in Administrative Decision-Making in the Netherlands*, Groningen: Europa Law Publishing, 2007, 3.

(17) T. EVANS – J. HARRIS, *Street-Level Bureaucracy, Social Work and the (Exaggerated) Death of Discretion*, British Journal of Social Work, Oxford, 2004, v. 34, n. 6, 871-895.

In the same way: K. C. DAVIS, *Discretionary justice: a preliminary inquiry*, Hardcover: Greenwood Pub Group, 1969; M. LIPSKY, *Street-level bureaucracy: dilemmas of the individual in Public Services*, New York: Russell Sage Foundation, 1974; K. ELLIS – A. DAVIS – K. RUMMERY, *Needs assessment, street-level bureaucracy and the new community care*, Social Policy & Administration. Hoboken, 1999, v. 33, n. 3, 262-281.

(18) K. C. DAVIS, *Discretionary justice: a preliminary inquiry*, Hardcover: Greenwood Pub Group, 1969 and K. C. DAVIS, *Police Discretion*, Chicago: West Publishing Co., 1975.

(19) M. LIPSKY, *Street-level bureaucracy: dilemmas of the individual in Public Services*, New York: Russell Sage Foundation, 1974, 13.

This behaviour can significantly affect the law, order and justice in society.

The danger of these agents carrying out public policy is in the on-position of the executive in relation to the legislature. It is the public servant who determines the criteria to give a “benefit” or a “punishment” rather than the directly elected representatives.(20)

Many public servants feel guilty about exercising discretion and the duty of a policy making. They believe that their actions were not all appropriate and often know that they act without any legal basis. Perhaps that is why these public servants genuinely appreciate that such power exists.(21)

#### 4.3. Front-line public servants enforcing rules

Rules are made to be obeyed. If public servants fail to follow the rules, they must be enforced by the Executive. Normally, the doctrine affirms that is not possible to undertake any type of planning to implement or enforce a rule, in the sense of when it is to be executed, against whom and on what occasions, because every rule must be enforced without exception(22). But unfortunately – or fortunately – it is not like that. The premise of full enforcement is misguided because in practice, there is a selective enforcement or non-enforcement of the rules. However, if the Administration enforces the rules in a selective way or simply fails to enforce them, it may be accused of favouritism. Further, if it enforces all rules without exception, it will probably be accused of being inflexible.(23)

The selective, partial or non enforcement of law means all decisions become extremely complex. The line between the existing margin of freedom

(20) R. COTTERRELL, *The Sociology of Law: An Introduction*, 2. ed. London: Butterworths/Oxford University Press, 1992.

(21) H. GOLDSTEIN, *Police Discretion: The Ideal versus the Real*, in *Public Administration Review*, Washington, 1963, v. 23, n. 3, 140-148.

(22) J. ALBERT – J. REISS JR. (REISS JR, Albert J. Consequences of compliance and deterrence models of law enforcement for the exercise of police discretion. *Law and contemporary problems*. Durham, v. 47, n. 4, 83-122, autumn 1984, p. 91) distinguishes: “*Compliance and deterrence strategies of law enforcement have different objectives. The principal objective of compliance law enforcement is to secure conformity with law by resorting to means that induce conformity or by taking actions to prevent law violations without the necessity of detecting, processing, and penalizing violators. The principal objective of deterrence law enforcement is to secure conformity with the law by detecting violations of the law, determining who is responsible for the violations, and penalizing violators to inhibit future violations by those who are punished and to inhibit those who might be inclined to violate the law if violators were not penalized. There are two principal types of compliance strategies of law enforcement, one based on incentives to comply, and the other on threats to invoke penalties for noncompliance unless actions to comply are taken. Compliance is voluntary in incentive-based systems whereas it is to some degree coerced in threat based systems*”.

(23) About *selective enforcement*: K. C. DAVIS, *Police Discretion*, cit.; J. Q. WILSON, *Varieties of police behaviour: the management of law and order in eight communities*, Cambridge: Harvard University Press, 1968; J. H. SKOLNICK, *Justice without trial: law enforcement in democratic society*, New York: Wiley, 1966; W. R. LA FAVE, *Arrest: the decision to take a suspect into custody*, Boston: Little, Brown, 1965.

to enforce the law and an arbitrary situation is very thin. People must not confuse a wrong use of criteria with an arbitrary decision, nor arbitrariness with lawful decisions. Now, to answer as to whether the action is proper or not is much more complicated.

States have to rethink the enforcement idea. According to Kenneth Culp Davis(24) the absence of an institutional position is bad for society. Sometimes the issue is that the Executive must enforce all laws while at other times it is that Executive cannot enforce all laws. This distorts reality. There must be a balance between the two points of view. It seems as if citizens prefer to know the truth about law enforcement than to continue believing in the false premise of full enforcement.

The truth is that full enforcement is a myth and has devastating consequences. So in practice what happens is a selective, partial or a non enforcement because of the simple reason that it is impossible to promote full enforcement however rule of law requires the State to implement all laws.

The question is whether to enforce the law selectively is legal or not. According to Kenneth Culp Davis(25) “open selective enforcement is legal”. To this author the problem related to the selective enforcement can be legal in some circumstances: many times the answer is not explicit in the rule (taking into custody someone who probably will not be condemned, for example); in others it is physically impossible to enforce all rules, then they must prioritize one action or another (each suspect running in different directions, for example); others times enforcement is impossible because the resources do not exist (for example attempting to arrest all those who are smoking marijuana at a concert in a public park); among many other situations. The author states that the Legislature recognizes that not all laws can be enforced. They make the laws in an excessive way so the Executive has a greater input into how they are implemented. The author concludes by saying that non enforcement is also legal,(26) after all if it allows selective enforcement then nothing is more logical than to also allow non enforcement.

Despite the general rule being the duty to enforce all rules, we believe that the Executive has a delegation to regulate the general obligation. But this regulation, which is nothing more than the materialization of public policy, must be based on studies, professional work and must be transparent and subject to criticism from within and outside the environment in which it is to be applied, i.e. should follow a due process. All those who enforce or implement law should be coordinated.

(24) K. C. DAVIS, *Police Discretion*, cit., 52 and other.

(25) K. C. DAVIS, *Police Discretion*, cit., 79.

(26) K. C. DAVIS, *Police Discretion*, cit., 92.

**5. Relationship between bureaucracy, discretion  
and corruption exercised by front-line public servants  
in public procurement**

Public procurement is particularly susceptible to corruption because of the amount of money involved in the contracts. As we can image the corruption can take place along the entire cycle of public procurement. During the internal phase (preparatory acts) the opportunities to bribe are different than those occurring in the external phase (after the disclosure of the procedure to third parties).(27)

During the internal phase no public servant should have contact with the public about the procedure that is being prepared but in many countries this does not occur. The deviation of conduct by different types of public servant can be observed, for example, when the convening act is modelled to favour someone or to exclude another. At this phase the private sector can bribe the public servant to obtain the promise of a contract or at least a higher probability of gaining the contract.(28)

Beside those possibilities we are more concerned in this research with the external phase. Here, the susceptibility of public procurement to corruption is further exacerbated by the relatively high degree of discretion that the front-line public servant has over the procedure. Here the private sector can, for example, offer a bribe to obtain proprietary information about other parties, or request the public servant to close his eyes to some illegal conduct, etc.(29)

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(27) The five common illegal acts in public procurement are: (i) "corrupt practice" is the offering, giving, receiving, or soliciting, directly or indirectly, of anything of value to influence improperly the actions of another party; (ii) "fraudulent practice" is any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a party to obtain a financial or other benefit or to avoid an obligation; (iii) "collusive practice" is an arrangement between two or more parties designed to achieve an improper purpose, including to influence improperly the actions of another party; (iv) "coercive practice" is impairing or harming, or threatening to impair or harm, directly or indirectly, any party or the property of the party to influence improperly the actions of a party; (v) "obstructive practice" is (v.i) deliberately destroying, falsifying, altering, or concealing of evidence material to the investigation or making false statements to investigators in order to materially impede a public investigation into allegations of a corrupt, fraudulent, coercive or collusive practice; and/or threatening, harassing or intimidating any party to prevent it from disclosing its knowledge of matters relevant to the investigation or from pursuing the investigation, or (v.ii) acts intended to materially impede the exercise of the public inspection and audit rights (see: The World Bank, *Guidelines procurement of goods, works, and non-consulting services*, Washington: [s. ed.], January, 2011, 6, Downloading at: [http://siteresources.worldbank.org/INTPROCUREMENT/Resources/278019-1308067833011/Procurement\\_GLS\\_English\\_Final\\_Jan2011.pdf](http://siteresources.worldbank.org/INTPROCUREMENT/Resources/278019-1308067833011/Procurement_GLS_English_Final_Jan2011.pdf)).

(28) Doing the internal phase we can give as examples: unnecessary investment; investment is economically unjustified or environmentally damaging; goods or services needed are over or underestimated to favour a particular provides; old political favours; conflicts of interest; designed the bidding documents to favour a particular provides; complexity bidding document to confuse the parties; etc.

(29) Examples of corruption in this external phase are: selection criteria are subjective; clarifications are not shared with all the bidders; confidentiality is abused; etc.

Usually larger amounts of bribes are given to the administrative elites or to the managers and supervisors and the front-line public servant receive a smaller amount to accelerate/facilitate a decision. Both are forms of corruption and constitute illegal behaviour in most countries.

All types of corruption are strictly related with the discretion of the public servant. John Gardiner(30) and Mark Philp(31) affirm that it occurs when a bureaucrat misuses its discretion to further their private interests to the detriment of public interest. Accepting the relationship between discretion and corruption, it is common see different authors propose a reduction in discretion to control corruption. In a very simple formula, the greater the discretion of bureaucrats, the higher the corruption and some suggest that creating more laws will resolve the problem. On the contrary, creating more laws does not resolve the problem. Discretion and bureaucracy originated from laws. Tony Evans and John Harris(32) state that the proliferation of “rules and regulations” should not be synonymous with greater control over professional discretion; paradoxically more rules may create more discretion.

The same can be said of bureaucracy. Frank Anecharico and James Jacobs(33) state that the creation of more bureaucracy to promote the integrity of public servants could result in more public sector corruption. Bureaucracy can be the perfect excuse to ask for bribes. In this sense, reducing discretion is not enough, rather it is essential to subject it to public control without this resulting in more bureaucracy.

Thus, any model of reform should not increase the bureaucracy, since that normally results in more discretion and as we can observe, for example, through the use of incentives such as improper payments of kickbacks and bribery, i.e., a broadening of corrupt practices.

Therefore, we can say that the bureaucracy and discretion are the two most important factors that encourage acts of corruption. One of the first to observe the relationship between corruption and discretion was Robert Klitgaard.(34) He claims that corruption is more pronounced in systems characterised by the formula  $C=M+D-A$  [Corruption = Monopoly + Discretion – Accountability]. It means: “Corruption equals monopoly plus discretion minus accountability. Whether the activity is public, private, or non-profit, whether you are in

(30) J. GARDINER, *Defining Corruption*, in A. Heidenheimer – M. Johnston (eds.), *Political Corruption: Concepts and Contexts*, New Brunswick, Transaction Publishers, 2005, 25-40.

(31) M. PHILP, *Conceptualizing Political Corruption*, *cit.*, 41-58.

(32) T. EVANS – J. HARRIS, *Street-Level Bureaucracy, Social Work and the (Exaggerated) Death of Discretion*, in *British Journal of Social Work*, 2004, v. 34, n. 6, 871.

(33) F. ANECHARICO – J. JACOBS, *The Pursuit of Absolute Integrity, How Corruption Control Makes Government Ineffective*, Chicago: The University of Chicago Press, 1996.

(34) R. KLITGAARD, *International Cooperation Against Corruption*, November, 1997, downloading at: [http://www.icgg.org/downloads/contribution02\\_klitgaard.pdf](http://www.icgg.org/downloads/contribution02_klitgaard.pdf).

Washington or Ouagadougou, you will tend to find corruption when someone has monopoly power over a good or service, has the discretion to decide whether you receive it and how much you get, and is not accountable". What we assume is that in this equation can be include a "+B" of bureaucracy. This way we can affirm that corruption equals monopoly plus discretion plus bureaucracy minus accountability ( $C=M+D+B-A$ ).

## 6. Conclusion

The characteristics of front-line public servants include the ability to exercise significant amounts of discretion, coupling this with the fact that they are important policy makers in any society, means they can increase the risk of criminal behaviour if they are open to receiving proposals of corruption.

Studying the characteristics of those types of public servants is fundamental to understanding some of the threats to the rule of law and the endemic corruption that we experience in society.

Society observes corruption with scepticism but forgets that public servants are not the only factor that create and develop it. It would not exist without the citizen. Corruption and its resistance must be studied in the private and public sphere.

The private and public sphere must work together to decrease bureaucracy, discretion and corruption and consequently improve profit sharing and minimize losses within the political, economic, social, and environmental arenas. The State should not be the only way to bail out the irresponsible actions of the citizen and the private sector, neither should the citizen and private sector suffer the consequences of State inefficiency. Only the perfect balance between the State and the citizen, and private actions will lead to development and well-being in our society. Transparency and division of powers should be the spokesman of the new environment, eliminating any attempt to forcefully disrupt the balance. This suggests that a new paradigm should be built and introduced to combine States and citizen/private initiative forces. Clearly, the State and the citizen/private sector do not operate at their best without each other.

It is clear that the multiplicity of controls is only useful to society while the controls show solidarity in this task, harmonizing different understandings, standardizing pipelines, preventing disputes between the Branches, in order to give legal security to citizens, servers and authorities. Disharmony only facilitates corruption, lawlessness and insecurity.

Beside all this we believe that principles such as the maximum objectivity of the Public Administration which impose objectivity on the actions of the public servant must be used and applied by the State. This means that when

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exercising discretion on behalf of the Administration, the decision-maker should, if possible, take into account objective criteria in relation to the facts, stating in advance the requirements on which he makes the decision. The idea is to prevent the administrator from changing the decision criteria once they have been selected. According to this principle, such criteria should be clearly and publicly identified with a detailed scale/schedule which fixes the precise value of the criteria, both quantitative and qualitative. Such criteria should be detailed with default parameters. The citizen has the right to know the criteria selected. This principle promotes the rationale and benefits of equality and legal certainty, since it gives transparency to the performance. Knowing in advance the criteria given the citizens may require consistency in decisions and actions.<sup>(35)</sup>

Another mechanism that can help solve the corruption problem is less bureaucracy. This requires the revision of standards that promote costly or unnecessary administrative action without a commensurate benefit to the community. It is worth remembering that the high cost of bureaucratic supervision may simply generate corruption without contributing to the welfare of the community.

Regardless of all these possible avenues of solutions, which surely will bring good results, leading to great savings for public money and the prevention of potential damage to the treasury, supervision should always be improved, so the irregularities can be curbed. But we must be realistic that some level of corruption is inevitable. Regardless of how sophisticated and well-developed the control structures, they will never be able to fully eradicate corruption.

Corruption is a cancer that hurts all countries. Perhaps the variable that best explains the differences between a successful and unsuccessful Public Administration is the level of corrupt present. Corruption strikes the heart of the administrative process, so a non or less-corrupt administration is essential to ensure that everyone's rights are respected.

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(35) See: A. SADDY, *El concepto de apreciatividad en el derecho administrativo: analogías y diferencias con la discrecionalidad administrativa (tesis doctoral)*, Universidad Complutense de Madrid, 2011.



## CHAPTER 3

### Integrity and efficiency in collaborative purchasing

BY

Bushra RAHMAN

MBA Research Administrator, Arizona State University

Eugene S. SCHNELLER

Professor of Supply Chain Management, Arizona State University

Natalia WILSON

Assistant Professor of Supply Chain Management, Arizona State University

### Introduction

This Chapter constitutes a case study of corporate political activity (CPA), industry self-regulation and governance through codes of conduct.(1) The chapter is divided into two parts. Part 1 considers the idea of codes of conduct in general with a focus on their characteristics, prevalence, difference in application and factors associated with their implementation and performance. Part 2 provides an overview of the US health Group Purchasing Organization (GPO) relief from antitrust violations through a safe harbor, challenges faced by GPOs adhering to rules pertaining to the safe harbor, their advancing openness/fairness in purchasing and the subsequent development of a code of conduct by GPOs and their trade association to meet the criticisms of legislators and industry critics.

The chapter utilizes the lens of resource dependency theory(2) which proposes that organizations engage in a variety of “buffering” strategies to protect themselves from environmental influences. As Hillman and her colleagues have pointed out, firms do not merely react to public policy decisions but are active in shaping social and economic issues related to their interest in areas such as antitrust Without doubt trade associations evolve as a mechanism by which similar organizations come together to buffer themselves against antagonistic environments and form interorganizational linkages between the

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(1) J. D. THOMPSON, *Organizations in Action*, New York: McGraw-Hill, 1967.

(2) J. PFEFFER – G. SALANCIK, *The External Control of Organizations: A Resource Dependence Perspective*. New York: Harper Row, 1978.

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association and its members and government.(3) CPA “focuses on the creation and maintenance of a specific set of external stakeholder relationships and policy outcomes, specifically with political and regulatory publics”(4) and is thus a primary process for achieving organizational aims and objectives.

Association driven collective action requires that competitors align to achieve common goals and, as challenges to their common pursuit evolve from “dangerous” stakeholders, collaborating organizations must also craft strategies to provide foundation for their individual and collective survival. To the extent that codes of conduct reflect public policy or reflect “contractual” agreement between parties, they are frequently treated as establishing a “legal as well as the ethical minimum requirement regarding the subject” and have implications for liabilities for those engaged in the code of conduct.(5) Thus the ways in which codes are monitored and enforced, both internally and by government, require understanding and scrutiny.

In an extensive review of the literature on corporate political activity Lawton and colleagues suggest that CPA research needs to be further explored collectively from the perspective of trade associations and lobbying organizations with the goal to “specify more closely the relationship between firms and governments”.(6) This chapter takes a significant step in filling the perceived gap in studies linking codes of conduct to CPA and corporate social responsibility (CSR).

The chapter also contributes to the important area of CSR and its extension into the area of “purchasing social responsibility (PSR)” which Carter and Jennings have observed to be divergent from the broader area of corporate social responsibility due to purchasing’s “distinct interaction with a broad set of stakeholders including buyers, suppliers, contractors, the community, and internal employees”.(7) As pointed out by Carter and Jennings, “PSR is a second-order construct that includes activities surrounding the areas of diversity, the environment, human rights, philanthropy and community, and safety. By using the PSR framework to bring these activities together, a more inclusive picture of the significance of supply management actions with a social dimension can be developed”.(8) Purchasing makes up a significant portion of annual spend of the health care industry, second only to human resources. In both the private sector,

(3) A. J. HILLMAN – A. ZARDKOOHI – L. BIERMAN Corporate Political Strategies and Firm Performance: Indications of Firm-Specific Benefits from Personal Service in the U.S. Government Author(s): *Strategic Management Journal*, Wiley-BlackwellStable, Vol. 20, No. 1 (Jan., 1999), 71.

(4) T. LAWTON – S. MCGUIRE – T. RAJWANI, *Corporate Political Activity: A Literature Review and Research Agenda*, in *International Journal of Management Reviews*, Volume 15, 2013, 86–105.

(5) J. BEACH, *Codes of Ethics Court Enforcement through Public Policy*, in *Business and Professional Ethics Journal*, 1985, Volume 4, Issue 1, 53-64.

(6) Lawton et al. *op.cit.*, 100.

(7) C. CARTER – M. JENNINGS, *The Role of Purchasing in Corporate Social Responsibility*, in *Journal of Business Logistics*, 2004, Vol. 25, No. 1, 145-186.

(8) C. CARTER – M. JENNINGS, *Op. cit.*, 151-153.

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where there is a need to satisfy the customer and financial stakeholders and within the public sector where there is an even broader range of accountabilities, PSR must be mindful of the range of activities involved in procurement and the need to achieve “value for money.” Charles A. Manu(9) reflects that:

*“Procurement continues through the processes of risk assessment, seeking and evaluating alternative solutions, contract award, delivery of and payment for the goods and/or services and, where relevant, the ongoing management of a contract and consideration of options related to the contract. Procurement also extends to the ultimate disposal of property at the end of its useful life.”*

Additionally,

*“Procurement is a hotbed of ethical challenges because the decisions and choices made in procurement affect the entire public sector”. Value for money is the core principle underpinning public procurement, incorporating ethical behavior and the ethical use of resources. The application of the highest ethical standards will help ensure the best achievable procurement outcome. It entails more than just getting the best price – ethics are important when considering value for money.”*

Quality, efficiency, integrity, customer service and effectiveness are fundamental to procurement(10) and, with significant funds at stake, codes of conduct have the potential to serve an important governance function.

Buying collectives such as GPOs are increasingly paying attention to meeting their social responsibility while engaging in purchasing functions through their suppliers. They are scrutinizing suppliers to seek those who value and imbibe socially responsible behavior in both upstream and downstream functions. How codes of conduct originate, evolve, are enforced and contribute to the governance of the procurement process, and serve as a stimulus and demonstration for PSR in an area such as health care where public and private funding are increasingly scarce and where good business practices must be valued, is the subject of this chapter.

## Part I

### 1. The idea of Codes of Conduct

Codes of conduct have been with us for many years. The Hippocratic Oath, which originated in the 5<sup>th</sup> century BC, focused significantly on the behavior of professionals. Over the centuries we have seen codes of conduct evolve with a focus on individuals in occupational groups, trade and other commercial associations, and codes oriented to specific organizations and their employees. The

(9) C. MANU, *The Principle of Value for Money in Procurement*, June 19, 2005, 5.

(10) F. BLUESTEIN, *The Legal Aspects of Public Purchasing*, in *Journal of Public Procurement*, 2006, 321-323.

focus of this chapter is principally on codes of conduct as developed by associations and organizations. Individuals ultimately are responsible for carrying out behaviors associated with organizational or association designed codes of conduct. Yet such codes are frequently oriented toward the behavior of a corporate entity. While codes, as discussed above, may take on some of the features of laws, codes of conduct are different than laws, rules and regulations. Although by themselves codes may not create a “legal liability” that is recognized by the courts and thus serve as a basis for action outside of the organization, they can constitute an effective means for internal organizational control and may be used to establish “an appropriate minimum” standard of care for the organization(11). Unlike the Sherman Anti-Trust which regulates kinds of corporate behavior, or Sarbanes Oxley Act of (Pub.L. 107-204) which requires management to carry out certain duties, codes of conduct tend to be voluntary.

Codes of conduct evolved for many reasons. Ethical standards of corporations, even prior to the economic failures of the early years of this century, have not been held in high regard by the American public.(12) Feeling a need to improve their images and facing increasing accusations of corruption, businesses turned to ethical codes to publicize their virtues and create a more positive impression with stakeholders.(13)

Some critics argue the codes are simply public relations tools; others believe they could be effective in encouraging more ethical behavior in and by organizations. The debate over ethical code purpose and effectiveness continues today. American ethical codes were first called « creeds » or « credos » and those in the 1980's were considered « legalistic » and « more likely to talk about ethics or the reputation of the company ».(14) More recently they were defined as written documents, which attempt to state the major philosophical principles, and articulate the values embraced by the organization.(15) When codes of conduct work well, they furthermore provide a set of guidelines for organizational governance and accountability. Importantly, while not laws, they may also take on a more formalistic role and may actually be reflected in legal decisions and other recognized evaluations of organizations and individuals.

Codes of conduct are described as policy documents defining responsibilities of the organization to stakeholders and articulating the conduct expected of employees.(16) Many codes contain open guidelines describing desirable behav-

(11) J. BEACH, *cit.*, 53-72.

(12) B. STEVENS, Corporate Ethical Codes, in *Journal of Business Ethics*, 2008, 78, b601-602.

(13) D. CRESSEY – C. A. MOORE, *Managerial Values and Corporate Code of Ethics*, in *California Management Review*, 1983, 25(53), 53-57.

(14) G. C. S. BENSON, *Code of Ethics*, in *Journal of business ethics*, 1989, Volume 8, Number 5, 305-319.

(15) S. BETSY, *Corporate ethical codes: effective instruments for influencing behaviour*, in *Journal of business ethics*, 2008, Volume 78, number 4, 601-609.

(16) M. KAPTEIN, *Business Codes of Multinational Firms: What do they say?*, in *Journal of Business Ethics*, 2004 13-31.

iors and proffer guidelines prohibiting certain behaviors.(17) As instruments to enhance social responsibility, codes may also clarify the norms and values the organization or occupational group seeks to uphold.(18)

Scrutinizing trade associations, three distinct sub codes for a code of conduct(19) are described by Hemphill:

- I. The economic code is the original basis for the development of such self-regulatory schemes. A modern economic code should be designed as a guide to maintaining the most competitive environment for the industry. Areas that should be addressed include product/service attributes, advertising, industrial espionage, and information disclosure.
- II. The environmental code emerging in the « green » decade of the 1990s. This code includes environmental issues, health and safety, and product liability issues. The Chemical Manufacturers Association and the American Petroleum Institute are two major industry trade associations that have recently included a comprehensive set of environmental principles as part of their association bylaws (Chemical Manufacturers Association, 1991; and American Petroleum Institute, 1990).
- III. The sociopolitical code, the last industry sub code to be developed, has yet to emerge as a distinct sub code within the industry code of conduct. This code will eventually include principles addressing political participation, bribery, philanthropy, local community and affirmative action issues.(20)

Studies of ethical code content conducted in the 1980's concluded that codes reflected concern over unethical behavior that might decrease profits and showed a weak commitment to social responsibility.(21) Conflict of interest was an important theme(22) along with compliance with federal laws.(23) An extensive content analysis was performed by Mathews,(24) which showed that firms primarily emphasized legal activities and employee misconduct in codes and placed little emphasis on the environment, quality, or product safety. Pitt and Groskaufmanis

(17) A. NIJHOF – S. CLUDTS – O. FISSCHER – A. LAAN, *Measuring the Implementation of Codes of Conduct. An Assessment Method Based on Process Approach of the Responsible Organization*, in *Journal of Business Ethics*, 2003, 45, 65-78.

(18) M. KAPTEIN, *cit.*, 13.

(19) T. A. HEMPHILL, *Self-regulating industry behaviour: Antitrust limitations and trade association codes of conduct*, in *Journal of business ethics*, 1992, Volume 11, Number 12, 915-920.

(20) T. A. HEMPHILL, *cit.*, 915-920.

(21) D. CRESSEY – C. A. MOORE, *cit.*, 71

(22) B. J. WHITE – R. MONTGOMERY, *Corporate Code of Conduct*, in *California Management Review*, 1980, 13(2), 38-46.

(23) R. SANDERSON – I. I. VARNER, *What's Wrong with Corporate Code of Conduct?*, in *Management Accounting*, 1984, 66, 28-35.

(24) M. C. MATHEWS, *Code of Ethics, Organizational Behavior and Misbehavior*, in *Research in Corporate Social Performance*, 1987, 9, 107-130.

found that conflict of interest, gifts, and misuse of confidential information were frequently mentioned topics.(25) Stevens indicated that the content in ethical codes was primarily designed to defend organizations against illegal behavior and was found lacking in visionary perspectives and in providing ethical guidance.(26) Interesting, and germane to our discussion, Snell and Herndon agreed, concluding codes were oriented toward corporate self-defense.(27)

In summary codes of conduct are highly heterogeneous in their design and intent. They may provide guidelines for an organization, its subsidiaries, divisions, operating entities to carry out their business in an ethical manner. Codes of conduct also provide guidance around health and safety, corruption, discrimination, protection of labor rights, protection of environment, compensation and on-the-job hours etc. Table 1 provides a detailed overview of the code of conduct content:

*Table 1: Code of Conduct Content (28)*

|  |  |
|--|--|
| <p><b>I. Conduct on behalf of the firm</b></p> | <ol style="list-style-type: none"> <li>1. Relations with home gov't</li> <li>2. Relations with customers/suppliers</li> <li>3. Relations with employees-health, safety</li> <li>4. Relations with competitors</li> <li>5. Relations with foreign gov'ts</li> <li>6. Relations with investors</li> <li>7. Civic and Community affairs</li> <li>8. Relations with consumers</li> <li>9. Environmental affairs</li> <li>10. Product safety</li> <li>11. Product quality</li> <li>12. Payments or political contributions to gov'ts or gov't officials or employees</li> <li>13. Acceptance of bribes, kickbacks, gifts/entertainment</li> <li>14. Giving of bribes, kickbacks, gifts/entertainment</li> </ol> |
| <p><b>II. Conduct against the firm</b></p>     | <ol style="list-style-type: none"> <li>15. Conflict of interest</li> <li>16. Divulging trade secret</li> <li>17. Insider trading inform</li> <li>18. Personal character mat</li> <li>19. Other conduct against</li> <li>20. Integrity of books an</li> <li>21. Legal responsibility</li> <li>22. Ethical responsibility</li> </ol>   |

(25) H. L. PITT, – K. A.GROSKAUFMANIS, *Minimizing Corporate Civil and Criminal Liability: A Second Look at Corporate Codes of Conduct*, in *The Georgetown Law Journal*, 1990, 78, 1559.

(26) B. STEVENS, *Using the Competing Values Framework to Assess Corporate Ethical Codes*, in *Journal of Business Communication*, 1996, 33(1), 71-83.

(27) R. S. SNELL – N. C. HERNDON, *An Evaluation of Hong Kong's Corporate Code of Ethics Initiative*, in *Asia Pacific Journal of Management*, 2000, 17(3), 493-518.

(28) G. WOOD, *A Cross Cultural Comparison of the Contents of Codes of Ethics*, in *Journal of Business Ethics*, 2000, Vol. 25, No. 4, 287-298.

|  |  |
|--|--|
| <p><b>III. Laws cited</b></p>                                    | <p>23. Competition act/Anti-trust<br/>                 24. Securities<br/>                 25. Environment<br/>                 26. Food and drug<br/>                 27. Product safety &amp; quality<br/>                 28. Worker health/safety<br/>                 29. Bribes or payments to governments or officials<br/>                 30. False advertising<br/>                 31. Other laws</p>   |
| <p><b>IV. Governmental agencies /commissions referred to</b></p> | <p>32. Competition tribunal/TPA<br/>                 33. Other agencies</p>  |
| <p><b>V. Types of compliance / enforcement procedures</b></p>    | <p>Internal – oversight<br/><br/>                 34. Supervisor surveillance<br/>                 35. Internal watchdog committee<br/>                 36. Internal audits<br/>                 37. Read and understand affidavit<br/>                 38. Routine financial budgetary review<br/>                 39. Legal department review<br/>                 40. Other oversight procedures</p>  |
| <p><b>VI. Penalties for illegal behavior</b></p>                 | <p>Internal – personal integrity<br/>                 (For questions repolicy or reporting misconduct of self or others to :)<br/>                 41. Supervisor<br/>                 42. Internal watchdog committee<br/>                 43. Corporation’s legal counsel<br/>                 44. Other (in firm)<br/>                 45. Compliance affidavits<br/>                 46. Employee integrity<br/>                 47. Senior management role models</p> |
| <p><b>VI. Penalties for illegal behavior</b></p>                 | <p>External<br/>                 48. Independent auditors<br/>                 49. Law enforcement<br/>                 50. Other external<br/>                 51. Codes mentioning enforcement or compliance proceedings</p>   |
| <p><b>VI. Penalties for illegal behavior</b></p>                 | <p>Internal<br/>                 52. Reprimand<br/>                 53. Fine<br/>                 54. Demotion<br/>                 55. Dismissal/firing<br/>                 56. Other internal penalty</p>   |
| <p><b>VI. Penalties for illegal behavior</b></p>                 | <p>External<br/>                 57. Legal prosecution<br/>                 58. Other external penalty</p>   |

|                          |  |
|--------------------------|--|
| VII. General information | 59. Need to maintain corporation's good reputation<br>60. Letter/introductory remarks from the president/CEO/chairperson of the board<br>61. Code specific to which country i.e.,<br>Home Country<br>World/general<br>Others<br>62. Equal Employment Opportunity |
|--------------------------|--|

## 2. Prevalence of Codes

Corporations increasingly adopted codes throughout the 1980's and 1990's and many American companies now have an ethical code.(29) Worldwide, fifty eight percent of the 100 largest companies use ethical codes.(30) "There are an estimated 6,300 national trade and professional associations representing processors, manufacturers, and service industries in the United States".(31) As there is a high degree of apprehension exhibited over unethical business practices in many industries, trade associations(32) publicize and promote their industry codes of conduct.(33)

A 1987 American Society of Association Executives survey showed that 43% of industry associations had promulgated a code of conduct; 46% stated that they had a method to enforce their code.(34) Codes of conduct are also prevalent outside of the US. As a part of their corporate social responsibility policy (CSR), 38% of the top one hundred organizations in the Netherlands have drawn up a code of conduct. Sixty five percent of the top five hundred organizations in Spain(35) and 50% of the largest companies in Australia have adopted a code. The United States and Canada top the list with 78% and 85% respectively of the top 1000 organizations having drawn up a code of conduct.(36)

(29) L. B. CHONKO – T. R. WOTRUBA – T. W. LOE, *Ethics Codes Familiarity and Usefulness: Views on Idealist and relativist managers under Conditions of Turbulence*, in *Journal of Business Ethics*, 2003, 42, 237-252.

(30) M. KAPTEIN, *cit.*, 13.

(31) National Directory of Trade and Professional Associations, 1991.

(32) National Directory of Trade and Professional Associations, 1991.

(33) S. PRIEST – J. KAPLAN, *Codes of Conduct in Light of Sarbanes Oxley*, *Ethical Leadership Group*, 2003, accessed at: <http://www.ethicalleadershipgroup.com/articles/CodesofConductarticlewithrevisions.pdf>.

(34) American Society of Association Executives, 1987.

(35) D. MELÉ – P. DEBELJUH – M. CECILIA ARRUDA, *Corporate Ethics Policies in the 500 Largest Companies in Spain*, Working Paper No 5 00/4bis, IESE Publishing, Barcelona, 2006, 9.

(36) S. P. KAPTEIN – H. K. KLAME – J. C. J. TER LINDEN, *De integere organization; het nut van een bedrijfscode*, 2000

### 3. *The value of self-regulation*

At the industry wide level voluntary codes of conduct may vary based on a number of factors. Prakash states that, “voluntary codes could be designed and enforced by regulators, nonprofit groups, industry associations, and individual firms (and) vary in their scope, focusing on firms around the globe, in a given region, within a country, or in a given industry”.<sup>(37)</sup> Thus while it has been suggested earlier that codes of conduct are “voluntary” in nature, understanding (1) their origin (e.g., as a result of governmental concern, consumer, company or sector concern), (2) the extent to which they thwart threats or challenges to an industry or practice (i.e., counter a threat for more restrictive government regulation) and (3) the point of oversight (government *vs.* internal) and penalty for violations, reflects the extent to which codes take on many of the trappings of formal and less voluntary aspects of regulation.

Self-regulation at the industry level is defined as “a regulatory process whereby an industry-level organization (such as a trade association) sets and enforces rules and standards relating to the conduct of firms in the industry”.<sup>(38)</sup> Gupta and Lad concur with Garvin that “some form of government oversight and threat of direct regulation often coexist alongside industry self-regulation”.<sup>(39)</sup> Carter and Jennings point out that the research literature on the relationship between government regulation and corporate social responsibility has been “mixed”.<sup>(40)</sup> Government, they suggest, may create a necessary hurdle, in the area of PSR and may not be an effective driver. It is noteworthy that their research focused on consumer products manufacturing industries – where the influence of government might well be different from sectors with greater public accountability.

Most attempts at industry self-regulation have involved national trade associations among the trade and professional associations representing processors, manufacturers, and service industries in the United States.<sup>(41)</sup> These national associations provide a variety of services for their specific industry/professional membership, including data collection, educational programs, facilitating technical standards and specifications, insurance programs, legal assistance and government relations. A high degree of concern has often been exhibited by these organizations over the business practices of their industry members. This concern has resulted in trade associations’ members promulgating industry codes of conduct.

(37) A. PRAKASH, *Responsible Care: An Assessment*, in *The George Washington University, Business Society*, 2000 vol. 39, no. 2, 183-209.

(38) A. K. GUPTA – J. LAWRENCE LAD, *Industry Self-Regulation: An Economic, Organizational and Politic Analysis*, in *The Academy of Management Review*, 1983, Vol. 8, No. 3, 416-425.

(39) A. K. GUPTA – J. LAWRENCE LAD, *op. cit.*, 1983, 4117

(40) C. CARTER – M. JENNINGS, *cit.*, 155.

(41) National Directory of Trade and Professional Associations, 1991.

Hemphill has identified a range of industry code of conduct items including “fair business dealings, advertising, favorable industry policies and related issues.... sanctions or penalties for noncompliance (for example, fines, suspension, and expulsion) to be applied against members who have violated provisions of the code.”(42) Furthermore, Carter and Jennings placed such formerly stand-alone issues as environmental purchasing, sourcing from minority business enterprise (MBE) suppliers, and other supply management issues such as human rights and safety within a broader conceptual and empirical framework of purchasing social responsibility (PSR).(43) Importantly, not all assessments of codes of conduct and self-regulation have been highly positive. Maitland emphasizes, “industry or trade associations appear to hold out little promise of being transformed into vehicles for self-regulation.”(44) He fears that “entrenchment” works against self-regulation, and, while initial rationale is plausible, codes of conduct “eventually degenerate into industry protectionism”.(45)

#### 4. *International comparisons*

In a study of codes from the US, Germany, France and England, Langlois and Schelgelmilch(46) concluded that American codes discussed government and customer relations more than European and British codes. Kaptein, as we discussed above, found that most codes described company responsibilities for product quality and services, obeying laws and protecting the environment.(47) He also found content differences in European, American, and Asian codes. European codes focused almost 50% more on the environment than American codes.

Honesty was a major theme in American codes (64%), but it was mentioned less frequently in European codes (45%) and in Asian codes (38%). Fairness was a less prevalent topic in American codes than in European and Asian codes.(48) Gaumnitz and Lere proposed a classification scheme for ethical code content, but their scheme appears to be basic content analysis that does not fully incorporate much of existing ethical code research (2004).(49) European companies have increasingly adopted codes of conduct to regulate labor relations.(50)

(42) T. A. HEMPHILL, *cit.*, 917.

(43) C. CARTER – M. JENNINGS, *cit.*, 145-186.

(44) I. MAITLAND, *The Limits of Business Self-Regulation*, in *California Management Review*, 1985, 27 (3), 132-146.

(45) *Ibid.*, 137.

(46) C. LANGLOIS – B. SHLEGEMILCH, *Do Corporate Code of Ethics Reflect National Character? Evidence from Europe and the US*, in *Journal of International Business Studies*, 1990, fourth quarter, 519-539.

(47) M. KAPTEIN, *cit.*, 21.

(48) M. KAPTEIN, *cit.*, 21.

(49) B. R. GAUMNITZ – J. C. LERE, *A Classification Scheme for Codes of Business Ethics*, in *Journal of Business Ethics*, 2004, 49 (4), 329-335.

(50) A. SOBCEK, *Codes of Conduct in Subcontracting Networks: A Labor law Perspective*, in *Journal of Business Ethics*, 2003, 44, 225-234.

*Table 2: Examples of Areas of Emphasis of Codes of Conduct*

| Markets | Emphasis  |
|---------|---|
| US      | Government<br>Customer Relations<br>Honesty<br>Legal Responsibility<br>Ethical Responsibility |
| Europe  | Environment<br>Fairness<br>Labor Relations  |
| Asia    | Fairness  |

### 5. Implementation, enforcement and performance

Code implementation (which included enforcement) was a key factor in determining whether a code was effective. (51) Ferrell and Gresham suggested that codes of ethics that are actually enforced would be most effective. (52) Adams and colleagues note that codes serve as formalized advance warning via the threat of sanctions and thus dissuade certain people from violating its principles. (53)

Appropriate enforcement of a code contributes to its influence on organization members' behavior. (54) Modes for compliance include both the presence of an active monitoring agency and regular reporting system. A code of conduct should be well embedded in the organization to be effective. Employees need to understand and incorporate behavior that reflects on an organization's adoption of code of conduct. Management needs to adopt and ensure implementation of the code of conduct. It has been observed that the review of code of conduct is anecdotal in organizations where it is triggered only by untoward incidents.

(51) M. S. SCHWARTZ – D. IZRAELI – J. E. MURPHY, *Corporate Codes of Ethics: factors Leading to Effectiveness*, Proceedings of the Academy of Management Annual Conference, 2000. Submission 10942, 26.

(52) O. C. FERRELL – L. G. GRESHAM, *A Contingency Framework for Understanding Ethical Decision Making in Marketing*, in *Journal of Marketing*, 1995, 49, 87-96.

(53) S. J. ADAMS – A. TASHCHIAN – T. H. SHORE, *Codes of Ethics as Signals for Ethical Behavior*, in *Journal of Business Ethics*, 2001, Volume 29, Number 3, 208.

(54) M. S. SCHWARTZ – D. IZRAELI – J. E. MURPHY, *cit.*, 2000, 54.

## Part II

### *1. GPO Code of Conduct in the US*

Healthcare delivery in the US is an industry that is highly dependent upon a large number of stakeholders representing the complex set of supply chain activities to achieve the goals of high quality patient care, cost control and improved public health. Stakeholders include the many organizational providers of care (hospitals, outpatient clinics, and surgeries, etc.), suppliers of the products that contribute to care (pharmaceutical companies, medical device companies, information technology companies), those who distribute and transport goods to points of care, human resource providers (medical schools, nursing schools, physician assistant programs and the many technology professionals involved in care) the associations that represent these many entities (e.g., AHA, AMA, ACHE, ANA, MGMA, MDMA, etc.), payers (private health insurance and government), and regulators at the state and national levels (e.g., local, regional and state health departments, the U.S. Food and Drug Administration and the Federal Trade Commission) and, finally, the legislators who enact laws that govern such relationships.

While health care provision in the US is principally delivered through non-governmental organizations, health care is heavily financed through public funding (especially Medicare and Medicaid) and the behavior of the organizations and individuals involved in delivery is subject to adherence to both unique governmental legislation, rules and regulations as well as broader legislation that affects organizational and individual behavior in other sectors of the economy (e.g., interstate commerce and anti-trust). Within the context of US healthcare reform there is a strong focus on achieving “value for money” – and much of this value can be achieved in the procurement process.

The following analyzes a government stimulated code of conduct as one foundation feature for governance of relationships between suppliers/manufacturers of products and hospitals and hospital purchasing through group purchasing organizations (GPOs) that represent them. The scrutiny considers (1) the structure of providers and suppliers in the U.S. Healthcare system, (2) the Ascent of GPOs, (3) GPO behavior in the Legal Environment and (4) Challenges to GPO Sustainability & the Industry Response.

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## **2. The structure of Providers and Suppliers in the US health care system**

The US health care system consists of over 5,700 registered hospitals and as many as 10,000 additional non-registered specialty and public hospitals with well over a million beds, 3,500 ambulatory surgical centers, and thousands of outpatient clinics and group practices. Many are located in large urban areas, but there are nearly two thousand rural hospitals in the US. With many hospitals having tens of thousands of products recorded in their item master (product registry), the strategic sourcing and contracting for goods is, indeed, a daunting task.

Hospitals secure needed products from large suppliers (e.g., Johnson and Johnson, B&D, and Care Fusion) as well as from a myriad of smaller companies operating in the US and abroad. Each year approximately 4,000 new products that are “equivalent” to other products seek market entry (through the FDA) with about three quarters actually achieving approval. Developers of these products seek to compete in a marketplace characterized by fairness and opportunity. In addition, a significantly smaller number of products each year seek “Premarket Approval” as significantly innovative products. (Figure1).

*Figure 1: Combined 510 (k) and PMA submissions*

| TYPE OF SUBMISSION | FY 99 – FY 09        |                      |                      |                      |                      |                     |                     |                     |                     |                     |                     |
|--------------------|----------------------|----------------------|----------------------|----------------------|----------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
|                    | 1999<br>ODE&<br>OIVD | 2000<br>ODE&<br>OIVD | 2001<br>ODE&<br>OIVD | 2002<br>ODE&<br>OIVD | 2003<br>ODE&<br>OIVD | 2004<br>ODE<br>Only | 2005<br>ODE<br>Only | 2006<br>ODE<br>Only | 2007<br>ODE<br>Only | 2008<br>ODE<br>Only | 2009<br>ODE<br>Only |
| Original PMAs      | 64                   | 67                   | 71                   | 49                   | 54                   | 37                  | 43                  | 25                  | 31                  | 26                  | 20                  |
| PMA Supplements    | 557                  | 546                  | 641                  | 645                  | 666                  | 565                 | 712                 | 1,113               | 1,087               | 1,448               | 1,394               |
| Original IDEs      | 304                  | 311                  | 283                  | 312                  | 242                  | 222                 | 226                 | 251                 | 211                 | 216                 | 222                 |
| IDE Supplements    | 4,127                | 4,388                | 4,810                | 4,722                | 4,415                | 4,297               | 4,264               | 4,485               | 4,345               | 4,409               | 4,281               |
| 510(k)s            | 4,458                | 4,202                | 4,248                | 4,320                | 4,247                | 3,107               | 3,130               | 3,240               | 3,192               | 3,363               | 3,597               |
| Original HDE       | 12                   | 11                   | 5                    | 5                    | 10                   | 9                   | 4                   | 4                   | 6                   | 3                   | 3                   |
| HDE Supplements    | 4                    | 10                   | 16                   | 16                   | 29                   | 28                  | 24                  | 53                  | 23                  | 40                  | 40                  |
| 513(g)s            | 43                   | 59                   | 82                   | 104                  | 156                  | 239                 | 287                 | 244                 | 381                 | 96                  | 98                  |
| <b>Total</b>       | <b>9,569</b>         | <b>9,594</b>         | <b>10,156</b>        | <b>10,192</b>        | <b>9,819</b>         | <b>8,504</b>        | <b>8,690</b>        | <b>9,415</b>        | <b>9,276</b>        | <b>9,601</b>        | <b>9,655</b>        |

*Source: US Food and Drug Administration*

## **3. The Ascent of GPOs**

Hospitals and other healthcare providers require a large number and complex mix of products to carry out their everyday work. Going to market for tens of thousands of items, in an environment characterized by a large number of

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suppliers, can be a time consuming and challenging task for hospitals. While many hospitals carry out self-contracting and increasingly employ technology to purchase on their own, the vast majority of hospitals develop relationships with GPOs to simplify their strategic sourcing, contracting and procurement.(55)

Many products sought by hospitals are relatively simple commodity medical products. Others are complex/high technology products such as orthopedic implants, cardiac stents, and pacemakers known as physician preference items (PPIs) or clinical preference items. Yet others are the hundreds of different pharmaceuticals necessary for patient care. Products that support hospital business operations, information technology, food service, housekeeping, other non-clinical items and services also are purchased by hospitals. Hospitals, in their search for new products to improve patient care and reduce costs, must also take into account factors other than selling price – such as the costs of switching or “conversion” (including training) from one product to another, the interaction between one product’s performance and another product, and the quality of service and dependability of suppliers.(56) Thus just because a new product receives approval to compete in the marketplace, for a company with a new product, many factors go into achieving success.

GPOs in the health care industry are not new. The Hospital Bureau of New York reportedly established the first healthcare GPO in 1910.(57) The decades through the 1960s led to the formation of about ten GPOs(58) and by the early 1970s there were forty hospital GPOs in the United States.(59) Throughout this period, hospitals had traditionally been paid generously for their charges to patients and insurance companies (including supplies) under cost-based reimbursement. GPOs began to grow in popularity in the early 1980s as health care costs grew and there was greater consolidation within the industry. In the mid-1980s, Medicare instituted the Prospective Payment System through which hospitals were reimbursed a fixed rate based on a defined service rather than the actual cost to the hospital for providing that service. At the same time, private sector managed care programs, with deeply discounted contracts to hospitals, reduced hospital reimbursement. These external market factors,

(55) L. R. BURNS – P. F., W. DANZON – W. KISSICK – J. KIMBERLY, *The Wharton School Study of the Health care Value Chain – The Health Care Value Chain: Producers, Purchasers, and Providers*, 2002, Jossey-Bass, San Francisco, 3-11.

(56) E. S. SCHNELLER – L. R. SMELTZER – R. LARRY, *Strategic Management of the Health Care Supply Chain*, San Francisco, Jossey Bass, 2006, 84-88.

(57) C. ROONEY, *The Value of Group Purchasing Organizations in the United States*, accessible at [http://higpa.site-ym.com/resource/resmgr/press\\_releases\\_2011/rooney\\_article\\_in\\_journal\\_20.pdf](http://higpa.site-ym.com/resource/resmgr/press_releases_2011/rooney_article_in_journal_20.pdf), Accessed August 18, 2011, also in *World Hospitals and Health Services* Vol. 47 No. 1.

(58) HIGPA, *A Primer on Group Purchasing Organizations*. Health Industry Group Purchasing Association, [http://www.higpa.org/resource/resmgr/research/gpo\\_primer.pdf](http://www.higpa.org/resource/resmgr/research/gpo_primer.pdf).

(59) R. E. BLOCH, *An analysis of Group Purchasing Organizations’ Contracting Practices Under the Antitrust Laws: Myth and Reality*, Myer, Brown, Rowe & Maw, Washington D.C.:P. 5.

especially the fact that hospitals were paid a flat rate for an admission regardless of the length of stay or employment of most materials, made it important for hospitals to control costs. All of this supported the idea that there might be efficiencies for hospitals to go to market in a more collaborative manner. In 2002 the Government Accountability Office reported that there were hundreds of health related GPOs in the United States, with 30 of great impact.<sup>(60)</sup>

GPOs developed as a result of healthcare provider demand and continue to evolve as a result of that demand. In this complex environment, hospitals assess GPOs by the extent to which they serve their customers/members (generally referred to below as customers) and reduce risk as they respond to the demand for needed products.<sup>(61)</sup> Except in hospitals and health care systems that have developed GPOs to specifically serve their membership (e.g., HCA and its GPO, HealthTrust), GPO, participation, or membership is voluntary. US hospitals are also frequently part of a large multi-hospital system with as many as one hundred hospitals coming together within a governance structure. These systems frequently recognize that there is diversity in needs and that they require some level of flexibility to not utilize national GPO contracts. For example, HCA regions, while recognizing the value brought by many of the available national HealthTrust contracts, carry out their own contracting for selected goods and services. Moreover hospitals and systems periodically require GPOs seeking to obtain or maintain a relationship with them to submit responses to “Requests for Information” (RFIs) and/or “Requests for Proposals” (RFPs) focused principally on prices for a “market basket of goods”. Thus hospitals effectively make the GPOs compete against each other for customers in virtually the same way GPOs require suppliers to compete for contract awards. If a particular GPO’s contract prices for the categories of interest to these hospitals are not competitive, the hospital can select to affiliate with a different GPO or even more than one GPO or, if it believes it can engage the marketplace effectively, decide to engage in increased levels of self-contracting. GPOs that do not have competitive supplier agreements or desired products or services simply will not retain their customers. Indeed, there have been numerous hospitals and health systems that have switched GPOs in recent years. A report by the General Accounting Office to US Senate explained:

*Hospitals and other health care providers, including those that participate in Medicare and Medicaid, face continuing pressure to address rising health care costs. These types of providers have increasingly relied on purchasing intermediaries, known as group purchasing organizations (GPO), as one means to help keep the cost of medical products in check. Providers use GPOs to negotiate contracts*

(60) General Accounting Office, *Group Purchasing Organizations: Pilot Study Suggests Large Buying Groups Do Not Always Offer Hospitals Lower Prices GAO 02-690T: P5*. In 2004, the name of “General Accounting Office” was changed to “Government Accountability Office”.

(61) E. S. SCHNELLER -L. R. SMELTZER – R. LARRY, *cit.*, 107-108.

*with vendors such as manufacturers, distributors, and other suppliers to purchase a range of products – from commodities such as cotton balls and bandages to high-technology medical devices such as pacemakers and stents.*(62)

GPOs incur significant costs with respect to their processes. Those costs include (1) identifying customer needs, (2) confirming source selection, (3) developing and releasing requests for proposal, (4) elimination of unacceptable proposals, (5) evaluation of potentially acceptable proposals, (6) optimization of proposals, (7) obtaining best and final offer, (8) presenting award options to customers for customer decision, (9) finalizing awards and (10) launching contracts. Of course, if hospitals decided to handle contracting without GPO involvement, they would incur many of those costs. It has been estimated that a system not utilizing a GPO would require as many as 15 new employees to carry out the functions performed by GPOs.(63)

GPOs are characterized by differing expectations regarding customer ability to standardize on products to support purchasing strategy – especially contract compliance. Indeed, simply having a contract with a GPO does not guarantee sales to GPO contracted suppliers. GPOs also vary in their support of regional or affinity groups or vary in their needs by non-regional criteria (e.g. academic medical centers or children’s hospitals), as well as in supporting customers in individual contracting, spot purchasing and other purchasing opportunities. Regional alliances also enter into local contracts for their customers. Thus off-contract suppliers, while lacking the GPO point of access, have avenues to secure business on the basis of pricing or unique products and services.

Many hospitals and systems use GPO pricing to “benchmark” pricing from which to begin their own negotiations for products when they purchase outside of the GPO or negotiate local agreements with GPO vendors.(64) Although it is difficult to precisely estimate the value gained from such benchmark pricing, suppliers could attempt to impose much higher pricing if there were the absence of GPO-facilitated transparency to their customers in the market.

GPO pricing is one manner for combating price secrecy in the marketplace. As Kolaski has pointed out, “Almost all hospitals retain the right to make whatever ‘off-list’ purchases from any vendor they choose. ... hospitals often make such purchases and use GPO-contract prices as a price ceiling in their negotiations for whatever ‘off-list’ products”.(65)

(62) GAO-12-399R Group Purchasing Organizations, March 30, 2012, 6-7.

(63) E. S. SCHNELLER, *The Value of Group Purchasing*, in *Health Care Sector Advances*, 2009, accessible at [https://www.novationco.com/media/industryinfo/value\\_of\\_gpo\\_2009.pdf](https://www.novationco.com/media/industryinfo/value_of_gpo_2009.pdf), accessed: September, 24, 2012, 14.

(64) E. S. SCHNELLER, *cit.*, 9.

(65) W. KOLASKI, *Group Purchasing Organization (GPO) Contracting Practices and the Law*, a report prepared for *The Health Industry Group Purchasing Association*, November 2009, 8.

A number of hospital systems have developed their own “captive” GPOs.<sup>(66)</sup> Such efforts have resulted in very robust purchasing companies acting for the benefit of a system, and frequently for other systems. Notable among these, LeeSar (initiated by two hospital systems in South Florida) and ROI (initiated by the Mercy System in St. Louis) have become national models for system-based and system-owned GPOs. These entities flourish because they require all hospitals in their systems to participate and to principally use contracted suppliers. They owe their success to their ability to standardize on a limited number of products and to bring value to their “internal customers”. They also owe their success to (1) senior hospital leadership that has seen supply chain management as a strategic advantage and (2) investment by senior leaders in GPO leaders who are highly strategic in their thinking and have a willingness to build a total supply chain company.<sup>(67)</sup> Both of these GPOs have begun to expand their services regionally and to offer their services to “outside” hospitals and networks that are willing to require use of on-contract vendors. ROI reports having over 300 contracts secured through aggregated buying events for their customer hospitals for which they carry out efficiency based sourcing for \$681 million dollars in product. The value to 26 hospitals with over 4,300 beds is almost \$7 million dollars in savings through ROI’s GPO process.<sup>(68)</sup> In fact, these entities may be models for GPO and broader supply chain function development and are, perhaps, an archetype for the idea of a “Fully Integrated Supply Chain Company” (FISCO) based on their insourcing the wide range of supply chain management functions including GPO contracting, self-distribution and other key supply chain functions.

#### 4. GPO Behavior and the Legal Environment

The legal environment under which GPOs act today can be traced to the continued evolution of the Sherman Anti-Trust Act of 1890 which was passed in response to the concentration of economic power in large corporations and in combinations of business and the 1914 passage of the Clayton Antitrust Act with its focus on illegal practices that either contributed to or resulted from monopolization. The Clayton act explicitly outlawed commercial practices such as *price discrimination*. In 1914 the Federal Trade Commission was established as an agency with the power to investigate possible violations of antitrust laws and to issue orders forbidding unfair competitive practices and to even stop them in their

(66) SMG Marketing Group, *2002 SMG MHS/GPO Market Report*, estimates there are at least 441 such GPOs.

(67) Today, ROI is one of the healthcare industry’s leading supply chain management companies. With more than \$670 million in contracted purchasing volume and more than 1,400 customers, ROI claims to be the fifth largest GPO in the country in purchasing volume, <http://www.roiscs.com/iss>.

(68) V. MOORE, *Too Big to Fail: The Risk and Value of the Healthcare Supply Chain*. Presentation at the annual meeting of the *American College of Healthcare Executives*, Session 114X, March 24, 2011, Slides 32 & 33.

incipiency.(69) As early as 1949 analysts such as Callman argued for a “rule of reason” in assessing conditions under which free competition becomes “economically impractical and realistically unworkable”(70) and argued for flexibility and deviation in situations, where combination “is vital to the existence of competitors and their ultimate ability to revive a competitive market”.(71)

Typically, decisions to award contracts are made by GPO committees made up of representatives of GPO customer organizations-the entities that actually utilize GPO contracts to purchase and utilize the goods and services. As a result of this competition for contracts, some suppliers are not granted contracts. Indeed, if products brought under contract are not acceptable to GPO customer clinicians and other users of the products, contract utilization would be extraordinarily low and satisfaction with the GPO would be minimal as would be compliance with GPO contracts. This contest for contracts typically results in discounted prices based on levels of contract compliance and allows small as well as large hospitals to take advantage of volume purchasing. For the health care provider there are purported efficiencies beyond favorable pricing, such as a reduction in the costs associated with purchasing and contracting processes. Because product choice committees (frequently referred to as “value analysis teams” [VATs]) are made up of customers, there is greater likelihood that contracts will be secured to meet actual customer need. GPOs reduce risks associated with product strategy (inappropriate strategy for a given good or service), market strategy (inappropriate strategy for current market conditions), demand strategy (buying too much or too little of the good or service), and implementation strategy (the supply strategy is appropriate but not implemented correctly).

Predicting GPO customer adherence to contracts, in an environment characterized by voluntary commitment to contract participation, is very much easier said than done. Thus while some analysts(72) have depicted the hospital/GPO relationship as one of “outsourcing” of the strategic sourcing and contracting process, it is perhaps more accurate to portray a relationship that is highly variable as “co-sourcing.” That is hospitals see GPO participation as one of several strategies for securing goods and services. Hospitals across a system may experience different levels of satisfaction with a specific vendor or have clinicians who have developed strong preferences relating to product familiarity and a high level of service, with a vendor they have used for many years. Thus when a hospital changes suppliers, conversion to a new supplier is frequently less than complete. Again this means that suppliers have multiple opportunities to seek business with hospitals and hospital systems.

(69) *Fashion Originators' Guild v. FTC*, 312 U.S. 457 (1941); *FTC v. Raladam Co.*, 316 U.S. 149 (1942).

(70) R. CALLMAN, *The Essence of Antitrust*, in *Columbia Law Review*, 1949, Vol 49, No 8, 1112.

(71) R. CALLMAN, *cit.*, 1112.

(72) E. S. SCHNELLER, *The Value of Group Purchasing, cit.*, 9

GPOs engage in a variety of contracting practices to attempt to secure larger discounts and increase value for their customers, including using sole-source contracts, percentage of purchase discounts and multi-product discounts.<sup>(73)</sup> These contracting practices enable the GPO to obtain greater value from a particular vendor by concentrating a greater percentage of its customers' potential purchases for a particular product or service with that vendor. Obviously, this means that some vendors will be excluded from participation and others are likely to obtain a smaller percentage of that GPO's customers' purchases of the relevant product during the term of the contract. Given that GPO contracts typically account for over seventy percent of hospital purchases, failure to win one or more GPO contracts may result in a significant loss of business to the non-contracted vendor.

While the primary obligation of a GPO is to its customers, GPOs also have extensive relationships with vendors with whom they negotiate contracts and thus must balance many criteria when selecting vendors and negotiating contracts. In many ways, GPOs should be thought of as a vendor's customer. Some of this balancing revolves around criteria associated with products and the actual selection of suppliers/manufacturers, to the exclusion of others and channeling business to their customers. And to the extent that GPO engagements with suppliers include communicating expectations for sales, one cannot help to observe that GPOs are faced with both "dual agency" problems as well as problems associated with antitrust. Recognition of this is a good reason to work to assure that GPOs are truly serving their downstream hospital customers while supporting the sustainability and value need by their upstream suppliers.

In recent times, the activities of GPOs have raised serious questions as to whether GPOs continue to truly reduce costs for customers or whether they have used the safe harbor provisions (see below) of the anti-kickback statute to evolve into far more powerful entities with monopoly and monopsony powers which reduce competition, create barriers to market entry, and impede the functioning of a free market. There are a variety of contracting practices that have raised competitive concerns, including sole source contracting, bundling of unrelated products, and market share. As a Government Accountability Office (GAO) report suggests, there is concern that GPOs have evolved from neutral buying units to "gateways" which permit manufacturers to enter into arrangements that may raise entry barriers, ultimately leading to higher prices and less innovation. The relationships

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(73) Savings Attributed to GPOs The Value of Group Purchasing 2009 study estimated a \$36 billion cost savings associated with group purchasing in the US for pharmaceuticals, medical surgical items and physician preference items. A 2008 study, reviewing the comprehensive range of items purchased nationally through GPOs, estimated that GPOs saved healthcare providers up to \$64 billion – with savings to public health care programs ranging from \$16 billion to \$36 billion.

between medical device manufacturers and GPOs have the potential to create incentives for the manufacturers to share profits with a GPO. A GAO report noted GPOs acknowledged that “a manufacturer dominant in a product line may contract with a GPO, or agree to a favorable contract, to preserve its market share and exclude competition”.<sup>(74)</sup> Thus as GPOs “go to market” with the goal of securing the “best available” agreement for their customers, where “best” may be related to cost, quality, and service, the sustained openness of markets is an important area for scrutiny.

It is within this context that challenges to the US GPO structure have arisen. Some suppliers have complained that GPOs exclude and create barriers to entry for small, innovative suppliers. They claim that sole-source contracts, percentage of purchase discounts and multi-product discounts, individually and collectively, have the effect of establishing exclusive contracts between the customer hospitals and the contracted supplier.<sup>(75)</sup> Others have argued that competition is harmed because the “exclusive” GPO contracts entrench further the contracted supplier, allowing it to gain a virtual monopoly and obtain all the rewards that a monopoly brings – i.e. higher prices and lower quality.

Since 1987 GPOs have operated under a statutory “Safe Harbor” created by Congress that allows them to carry on the health care purchasing mission without undue concern of federal prosecution. There have, however, been vocal critics of GPOs. In 1991, following challenges to the extent to which GPOs might not adequately be providing for an open and fair marketplace, the U.S. Department of Health and Human Services issued regulations that provided additional guidance for GPOs. Proactively, the Medical Device Manufacturers Association (MDMA) proffered a code of conduct for GPOs focusing on (1) antitrust issues, (2) the receipt of administrative fees from the contracted manufacturer and (3) alleged conflicts of interests between the GPOs and contracted suppliers. In 2002 the Senate Subcommittee on Anti-trust held hearings into competitive issues relating to GPO contracting.<sup>(76)</sup> The focus of the hearings was on the practices of sole-sourcing, commitment levels and multi-product discounts, the role of vendor payments to GPOs, and whether these practices may “reduce competition and innovation in health care and narrow the ability of physicians to choose the best treatment for their patients.”<sup>(77)</sup> Responding to this in 2002 the Health Industry Group

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(74) D. Balto Testimony, 2004.

(75) See The Honorable Herb Kohl, United States Senator, Statement Before the United States Senate Committee on the Judiciary (April 30, 2002) (hereinafter “Kohl Statement”).

(76) Kohl Statement, at 1. See also, The Honorable Orrin Hatch, United States Senator, Statement Before the United States Senate Committee on the Judiciary (April 30, 2002); The Honorable Strom Thurmond, United States Senator, Statement Before the United States Senate Committee on the Judiciary (April 30, 2002). See Senate Hearings.

(77) *Op. cit.*

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Purchasing Organization (HIGPA) [now the Healthcare Supply Chain Association] released its Code of Conduct. This code provided a foundation for the ethics for individual GPOs announcing that:

1. HIGPA will publish an annual report identifying those GPOs in compliance with its Code of Conduct.
2. HIGPA shall coordinate development and implementation of industry-wide educational programs on clinical innovations, patient safety, contracting processes, public policy, statutory and regulatory requirements, and best practices for compliance with the Code.
3. Compliance will be a requirement for membership in HIGPA.
4. HIGPA will support the creation and maintenance of a Web-based directory where vendors can post product information, including information about products considered new and innovative.

It is also noteworthy that one of the large GPOs, Purchasing Partners, acted independently by commissioning a report to analyze ethical issues faced by group purchasing organizations.(78)

Over the past decade questions have been raised regarding the extent to which GPOs provide access to contracts to a full range of companies, not just for large suppliers but also for those bringing new products into the market. Response from the GPO industry itself reveals a “rhetoric of openness” both to customers purchasing outside of their GPO (i.e., for products not on contracts) as well as the provision of channels for new product entry into GPO contracts. Research by The Lewin Group(79) addresses the issue of purchasing off contract and reports multiple examples of how GPOs have dealt with purchase of off contract products by their customers.

GPOs have also committed to the idea of PSR through their code of conduct, wherein they encourage and promote minority – and women-owned business enterprises (M/WBEs). GPOs increasingly focus on upstream sourcing issues since human rights issues, including selecting suppliers that pay a minimum living wage and that avoid the use of unacceptable working conditions in their factories, have gained prominence in the eyes of the customer. Emmelhainz and Adams(80) suggested that these issues have become relevant to supply managers as a result of greater awareness by consumers and increased regulatory scrutiny.

(78) K. HANSONS, *A Report to the Audit Committee of the Board of Directors of Premier, Inc.* October 23, 2002.

(79) The Lewin Group, *The Clinical Review Process Conducted by Group Purchasing Organizations and Health Systems*, A report prepared for The Health Industry Group Purchasing Association, April 2002, 15.

(80) M. A. EMMELHAINZ – R. J. ADAMS, *The Apparel Industry Response to ‘Sweatshop’ Concerns: A Review and Analysis of Codes of Conduct*, in *The Journal of Supply Chain Management*, 1999, 35:3, 51-57.

While an exhaustive international review of health sector codes of conduct is beyond this chapter, it is noteworthy that in the UK, where the healthcare procurement is largely a public sector activity, the government has sponsored major reports into the failure of the public sector to take up innovations, making explicit the role for Government for public procurement in innovation and procurement “as a lever for stimulating and enabling supplier innovation.”(81)

### **5. Challenges to GPO Sustainability & the Industry Response**

Over the last ten years there have been periodic challenges to group purchasing practices relating to their funding model of accepting administrative fees from suppliers, the extent to which they affect markets related to smaller enterprises and restrict access to contracts for a range of suppliers through their purchasing practices.(82) The principal criticisms of GPOs have been about their role in establishing and sustaining a fair marketplace through horizontal collaboration with provider competitors (i.e., customer hospitals) as well as through vertical collaboration with suppliers. Callman has written that while agreements between competitors should “be unlawful per se, when allowed by government agencies, such should be continually scrutinized and supervised.(83)

A 2002 GAO report states that “some manufacturers – especially small manufacturers of medical devices – allege that contracting practices of some large GPOs have blocked their access to hospitals’ purchasing decision makers. The manufacturers contend that these practices ultimately deny patients access to innovative or superior medical devices.”(84) These concerns instigated the need for reexamining antitrust guidelines in regards to the GPOs. The findings of the study concluded that price savings were not obtained consistently with GPO contract and savings varied by model and size of hospital. However, it should be noted that the study only looked at two products, one in the commodity category and the other a physician preference item across one geographical market in 18 hospitals.

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(81) N. CALDWELL – W. PHILLIPS – T. JOHNSEN – M. LEWIS, *Procurement Ethics and Telecare Innovation in UK Healthcare*, in Piga G and Thai, Kai (eds. by) *Advancing Public Procurement*, PR Academics Press, 139-155. Also see: N. D. CALDWALL – H. WALKER – C. HARLAND – L. KNIGHT – J. ZHANG – T. WAKELEY, *Promoting Competitive Markets: The Role of Public Procurement*, in *Journal of Purchasing and Supply*, 2005, 11(5-6) September-November, 242-251.

(82) C. WERNER. Facing Tough Questions on Ethics, GPOs Seek Ways to Respond. , *Healthcare Purchasing News*, December 2002, accessible at: [http://findarticles.com/p/articles/mi\\_m0BPC/is\\_12\\_26/ai\\_95612200/](http://findarticles.com/p/articles/mi_m0BPC/is_12_26/ai_95612200/), accessed May 8, 2011.

(83) R. CALLMAN, *cit.*, 1113-1114.

(84) GPOs Pilot Study Suggests Large Buying Groups Do Not Always Offer Hospitals Lower Prices. Statement for the Record by William J. Scanlon, GAO Testimony April 30, 2002 Director, Health Care Issues.

The goal of the Health Industry Group Purchasing Association Code of Conduct was: “to help ensure that providers have access to group purchasing organizations that offer necessary services at the lowest possible cost. The principles cover several areas, including legal compliance, disclosure of vendor payments, conflicts of interest, product innovation, and a diverse manufacturer base with access to the GPO contracting process.” (85)

In 2003 the GAO reported that selected GPOs had adopted or revised codes of conduct to respond to the questions in 2002 about their business practices, but that it was too soon to evaluate the impact of the codes of conduct. In 2005 HIGPA recognized the need “to assure ongoing adherence to ethical conduct and business practices, and to hold the confidence of the public and the Government in the integrity of the industry.” (86) To accomplish this goal they brought together GPOs to establish the Healthcare Group Purchasing Industry Initiative (HGPII); initially created, by nine of the US leading GPOs, to promote and monitor best ethical and business practices in purchasing for hospitals and other healthcare providers. The governing body of the Initiative was comprised of the nine founding GPO Chief Executive Officers, who served as a Steering Committee to set the Initiative’s policies and programs.

HGPII sought to assure ongoing adherence to ethical conduct and business practices, and to hold the confidence of the public and the Government in the integrity of the industry. For purposes of the antitrust laws, however, it is critical to distinguish between competitive bidding practices that result in certain vendors failing to win contracts and exclusionary practices that result in foreclosure of an entire market in which a particular product is sold, thereby reducing consumer welfare. In somewhat different terms, while GPO contracting practices may result in commercial disappointment for certain vendors, it is important that in most instances they do not injure competition.

Members of HGPII pledge to:

1. Establish a process for the industry to improve and monitor its ethical and business conduct practices through significant transparency and to sustain a high level of trust with the public.
2. Follow the six core ethical and business principles (87):
  - a) have and adhere to a written code of business conduct. The code establishes high ethical values and sound business practices for the signator’s group purchasing organization.

(85) Health Industry Group Purchasing Association. Health Industry Group Purchasing Association Code of Conduct. Washington, D.C. 2002, 1.

(86) *Health Industry Group Purchasing Initiative*, accessed May 8, 2012 at <http://www.healthcaregpoii.com/abouthgpii.html>, 1.

(87) *Health Industry Group Purchasing Initiative, cit.*, 1

- b) train all within the organization as to their personal responsibilities under the code.
  - c) work toward the twin goals of high quality healthcare and cost effectiveness.
  - d) commits itself to work toward an open and competitive purchasing process free of conflicts of interest and any undue influences.
  - e) have the responsibility to each other to share their best practices in implementing the Principles; each Signatory shall participate in an annual Best Practices Forum.
  - f) be accountable to the public.
3. Report annually on adherence to these principles using an Annual Public Accountability Questionnaire.
  4. Participate in the Annual Best Practices Forum to discuss best ethical and business conduct practices with other GPO representatives and interested parties. For instance the 2011 forum included sessions on expanding business opportunities for small, disadvantaged, and diverse vendors, trends in organizational ethics, current health care policy and legislative issues, and compliance programs. This forum also included a panel of representatives from six vendors who spoke about their experiences with GPOs.

The Initiative also formed an independent Advisory Council, with participants from outside the GPO industry, to provide a source of independent advice and counsel to a steering committee charged to build trust with the public and promote legal compliance and high ethical standards and achieve accountability. The principal mechanism for accountability is the annual accountability questionnaire that is available to the public and “used by the Initiative Coordinator to compile a summary report on the adherence of those signing to participate to the Principles and a report on evolving Best Practices in fulfillment of the Principles.” The questionnaire requests that each GPO:

1. describe the key components of the GPO’s written code of business ethics and conduct. (Please provide a copy and describe any changes since the last submission).
2. describe the GPO’s policies and procedures that address conflicts of interest for all employees and clinical advisory members in a position to influence contracting decisions and for all other employees and members of the Board of Directors and/or the GPO’s governing body.
3. describe the GPO’s policies and procedures that address activities, including other lines of business of the GPO and the GPO’s parent company or affiliates, that might constitute conflicts of interest to the independence of its purchasing activity.

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4. describe the GPO's policies with regard to disclosing to customers money or value received from vendors, whether in the form of administrative fees, marketing fees, partnership incentives, equity or any other form.
5. describe if it discloses to each customer all fees, in any form, paid to the customer organization?
6. describe the GPO's policy with regard to whether all responsible vendors are eligible to compete and receive a contract award under the criteria.
7. describe the GPO's publicly available policy and procedure that addresses vendor rights, including a procedure for vendor grievances.
8. describe the GPO's policy and process to evaluate and provide opportunities to contract for innovative clinical products and services.
9. describe the GPO's program or activities that encourage contracting with small, women-owned and minority businesses.
10. describe whether and in what manner the GPO distributes its written code of business ethics and conduct to all applicable employees, agents, contractors, clinical advisory committees, and others involved in group purchasing activity.
11. describe how new employees involved in group purchasing are provided an orientation to the written code of business ethics and conduct.
12. describe the nature and content of the GPO's annual employee refresher training on the written code of business ethics and conduct.
13. describe the mechanism (e.g., a corporate review board, ombudsman, corporate compliance or ethics officer) for employees to report possible violations of the written code of business ethics and conduct to someone other than one's direct supervisor, if necessary.
14. describe the mechanism the GPO utilizes to follow up on reports of suspected violations to determine what occurred and who was responsible, and to recommend corrective and other actions.
15. describe how the GPO employees' compliance with its written code of business ethics and conduct is measured in their job performance?
16. describe the processes the GPO utilizes to monitor, on a continuing basis, adherence to the written code of business ethics and conduct, and with applicable federal laws.
17. describe how the GPO fulfilled its obligation to participate in the most recent Best Practices Forum.

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18. describe how the GPO reports to the company's Board of Directors or its Audit or other appropriate committee on the GPO's ethics and compliance program and its commitment to the Initiative's Principles.
19. name the senior manager assigned responsibility to oversee the business ethics and conduct program.

Detailed responses to each GPO answer to the questions can be accessed publically through the individual GPO website links at: <http://www.healthcaregpoii.com/signatorycompanies.html>.

Swain points out that while the Senate committee members believe that the "initiative's transparency and accountability will "provide important support for technological innovation in American healthcare, which ultimately benefits patients," the Medical Device Manufacturers Association "says the initiative doesn't go far enough" by not having "independent oversight, or contain meaningful penalties for noncompliance" nor addressing issues of excess administrative fees." (88)

We suggest that what we have described is an instance where the US government has perceived the code of conduct as an effort designed to eliminate an alleged problem and thus decided not to impose new regulations. As suggested by Beach and colleagues, "Private rules that come into existence in this way do so through conscious acts of the government (albeit acts of omission). The resulting rules ...effectively control the relationship of all parties ... The government and all concerned agree that it is the intention that these rules control the relationships of the parties involved." (89)

The annual reporting mechanism established by HIGPII and attention to compliance through an annual questionnaire, available to the public, suggests that the code of conduct has established a footing for government and the GPO industry itself to assess GPOs. A 2010 GAO report considered the impact of the GPO codes of conduct. The six reporting GPOs indicated that their codes of conduct-which include conflicts of interest and other policies have had impacts on GPO contracting practices, innovative product selection, contract administrative fees, potential conflicts of interest, and the transparency and accountability of GPO business practices. However, the impact of the GPO initiatives reported by representatives of customers and vendors GAO interviewed varied. For example, while some customers and vendors reported that GPOs are operating with greater transparency regarding their contracting practices, most customers and vendors did not comment on an impact associated with GPOs' initiatives to add innovative products to contracts.

(88) GPO reform Plan Unveiled but Industry Unsatisfied, MDDI News, September 2005.

(89) J. BEACH, *Code of Ethics: Court Enforcement Through Public Policy*, in *Business and Professional Ethics Journal*, Volume 4, Issue 1, 1985, 53.

In summary, government continues to demand scrutiny of GPOs in response to the market criticisms to assure ongoing adherence to ethical conduct and fair business practices.

*Table 3: Concerns of GPO and evaluation/reporting by GAO to the Senate Finance Committee*

| Year   | Concerns and Questions   | GAO Report/Findings  |
|--|--|--|
| 2002-2003  | Anticompetitive business practices of GPOs   | Selected GPOs adopted or revised codes of conduct in response to questions about their business practices.   |
| <b>2005: Founding of Healthcare Group Purchasing Industry Initiative (HGPII)</b> |  |  |
| Year   | Concerns and Questions   | GAO Report/Findings  |
| 2009-2010  | Do GPOs save their customers money?  | GAO unable to report on any published peer-reviewed studies that indicate an empirical analysis of pricing data to show whether or not GPO customers obtain lower prices from vendors.   |
| 2009-2010  | What are the types of services provide by GPOs to their members and how GPOs fund these services                               | GAO reported on the services provided by GPOs and the funds used for these services including administrative fees as well as direct service fees.  |
| 2011-2012  | Evaluate oversight of GPOs including efforts to self regulate through HGPII and federal oversight provided by HHS, FTC and DOJ | GAO reported that HHS has not routinely/ directly investigated GPOs regarding contract administrative fees. HHS has also not imposed any administrative penalties on GPOs since 2004.<br><br>DOJ and FTC have investigated complaints relate to federal antitrust laws.<br><br>HGPII established an Ethics Advisory Council and also a Vendor Grievance Process. |

Independent Evaluation. HGPII has designed evaluation tools to promote the use of competitive contracting processes to maximize value and quality to GPO customers in a way that insures all vendors are treated in a fair and unbiased manner.

In order to provide vendors with a forum to voice complaints regarding award decisions, each GPO, as a condition of its membership in HGPII, has agreed to participate in a two step review process. The first step is a formal, published process established by each GPO to review vendor concerns. Although individual GPO Grievance processes vary, each is designed to provide

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vendors with an understanding of the bid process, foster respect for customer decision making, and provide an opportunity for vendors to raise discrepancies that might have occurred during the process. In the vast majority of instances, this process appears to be sufficient to address a vendor's concerns. Where a vendor continues to have concerns, a vendor may request an independent and unbiased third party evaluation through the HGPII Independent Evaluation.

In order to facilitate the HGPII evaluation and insure independency, HGPII utilizes the services of the American Arbitration Association (« AAA »), an organization that provides alternative dispute resolution services. Vendor complaints eligible for review include (1) pre-award complaints that occurs when a vendor has been informed prior to a contract award announcement that it will not receive an award relative to a competitively-bid RFP (e.g., the vendor failed to meet minimum bid requirements), (2) post-award complaints that occurs when a vendor is informed concurrently with or after the award announcement that it will not receive an award and (3) new technology complaints that occurs when a vendor is denied a contract award following submission of a request for a contract award for new technology.

### Discussion and Conclusion

Corporate political behavior is an attempt to use the power of a group of competing organizations as well as government to advance private ends.(90) The overall objective of political behavior is to produce public policy outcomes that are favorable to the firm's continued economic survival and success.(91) To the extent that individual firms are able to influence the nature and extent of public policy, corporate political behavior may be viewed as strategic.(92) Firms can use their influence in public policy for a number of strategic ends: to bolster their economic positions, to hinder both their domestic and foreign competitors' progress and ability to compete, and to exercise their right to a voice in government affairs.(93)

Government policies can impact businesses and hence businesses engage in public policy discussions and key decision making that can impact their organizations or their competitors. There are a number of ways in which organizations try to influence public policy decisions. The effects of government policy on the competitive position of businesses represent, in turn, important deter-

(90) B. M. MITNICK, *Choosing Agency and Competition*, in *Corporate Political agency*, 1993, 1-12.

(91) G. KEIM – B. BAYSINGER, *The efficacy of business political activity: Competitive considerations in a principal-agent context*, in *Journal of Management* 14.2 (1988): 163-180.

(92) E. SALORIO, *Strategic Use of Import Protection: Seeking Shelter for Competitive Advantage*, in *Research in Global Strategic Management*, 1993, Vol 4, 62-87.

(93) G. D. – C. P. ZEITHAML, *Corporate Political Strategies and Decision Making: A Review and Contingency Approach*, in *Academy of Management Review*, 1986, 828-843.

minants of firm performance.(94) The government and government policies are critical sources of uncertainty for firms(95) and from a resource dependency perspective, shape a firms competitive environments. There is substantial interdependence between a firm's economic or competitive environment and government policy.(96)

GPOs in the health sector and government have the ability to alter markets and shape procurement strategies. They can affect the success of innovative, substitute and complementary products and structure markets through entry and exit barriers. Government can further shape the market through antitrust legislation; to alter the cost structure of firms through various types of legislation pertaining to multiple factors.(97) In many industries the success of business in the public policy arena is no less important than business success in the marketplace; as a result, it is critical for firms to develop political strategies as a part of their overall strategy.(98) If the government is important to a firm's competitive future, political action must be a business priority.(99) In some countries, such as Sweden, Japan, and Germany, businesses formally participate in the public policy process. In many others, such as the United States, Canada, and Mexico, firms « compete » with a variety of other interest groups informally to affect public policy.

Clearly the described HIGPII effort to shape and promote its code of conduct is an illuminating example of the extent to which an industry can commit to help shape the environment. This chapter provides an assessment of how GPOs designed and implemented a horizontal combination strategy, engaged the political and regulatory environment, and designed, as part of its CPA efforts, a code of conduct to (1) respond to criticism from the marketplace and (2) to thwart-off future conflict with the market and, (3) put into place a set of "standards" by which the Senate Finance Committee could assess and monitor GPO policies and procedures. The code of conduct is a buffering mechanism in what has evolved as a governance mechanism in a controversial

(94) B. SHAFFER, *Firm Level responses to Government regulation: Theoretical and Research Approaches*, in *Journal of Management*, 1995, 495-514.

(95) J. J. BODDEWYN, *Political Aspects of MNE Theory*, in *Journal of Business Studies*, 1988, 341-363; C. K. JACOBSON – S. A. LENWAY – P. S. RING, *The political Embeddedness of Private Political Transactions*, in *Journal of Management Studies*, 2007, 453-478.

(96) D. P. BARON, *Integarted Strategy: Market and Non Market Components*, in *California Management Review*, 1995, 47-65; S. LENWAY – T. MURTHA, *The State as Strategic in International Business Research*, in *Journal of International business Studies*, 1994, 513-535; M. E. PORTER, *The competitive Advantage of Nations*, New York Free Press, 1990.

(97) J. GALE – R. BUCHHOLZ, *The Political pursuit of Competitive Advantage: What Business can gain from Government*, in *Business Strategy and Public Policy*, 1987, 231-252.

(98) W. D. OBERMAN, *Strategy and Tactic Choice in an Institutional resource Context*, in *Corporate Political Agency*, 1993, 321-324; D. B. YOFFIE – S. BERGENSTEIN, *Creating Political Advantage: The rise of the Corporate Political Entrepreneur*, in *California Management Review*, 1985, 124-139.

(99) D. B. YOFFIE, *How an Industry Builds Political Advantage*, in *HBR*, 1988, 80-89.

market. The scrutiny of the code also reveals how the code reflects on both corporate social responsibility issues as well as the idea of purchasing social responsibility – especially from the perspective of how competing organizations come together to answer criticisms and shape aspects of their behavior. The chapter identifies the variety of mechanisms by which the code responds to concerns regarding administrative fees, market maintenance, product positioning and the behavior of individuals working within GPOs.

It is noteworthy that while we have portrayed the evolution of the HIGPII code of conduct to inquiry by government, that inquiry was in many ways stirred by criticisms, not from GPO customers (i.e., hospitals and health care systems) but by suppliers seeking GPO reform, if not even harsher legislative action that might have significantly altered GPO structure and curtailed GPO purchasing activity or even served as a death stroke to the GPO industry. And while there is no guarantee that opponents of the GPO idea may well raise their heads in the future,<sup>(100)</sup> the trail of behavior documented by the code of conduct acts as a demonstration of citizenship via. of a code of conduct or purchasing social responsibility.

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(100) S. PRAKASH SETHI, *Group Purchasing Organizations: an undisclosed scandal in the U.S.*, Palgrave MacMillan, New York, 2009, 68.

## CHAPTER 4

### Brief notes on tenderer requirements in Italy

BY

Anna ROMEO

Associate Professor in Administrative Law, University of Messina

#### *1. The peremptory of causes of exclusion*

In the attempt to identify general requirements for participation in public tenders, the Italian legislation has been inspired by the idea of determining and limiting both positive and negative requirements of the contractor's reliability and professionalism, necessary for the prior definition of traders who are allowed to participate in the bidding process.(1)

Also (or, perhaps, especially) from the European viewpoint, a clear and precise fixing of these requirements permits the settlement of a system which guarantees equality and competition and gives real opportunity for any operator to participate without discrimination in the bidding process. Such a system is profitable for the administration as well, since it permits the latter to find the best deal.

In the definition of general requirements it is necessary to balance two conflicting interests: the wider participation in competitions,(2) with the consequent limitation of litigation related to failure in the observance of purely formal provisions, and the full observance of rules, averting the risk of positions which, in order to favour substantive issues, breaks away from the former.

In this context it is necessary to consider the timeliness of the validity of the principle which fixes peremptory causes of exclusion, introduced by the

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(1) Directive No. 2014/24/EU establishes (Art.58, (1)) that "Selection criteria may relate to: (a) suitability to pursue the professional activity; (b) economic and financial standing; (c) technical and professional ability. Contracting authorities may only impose criteria referred to in paragraphs 2, 3 and 4 of this Article on economic operators as requirements for participation. They shall limit any requirements to those that are appropriate to ensure that a candidate or tenderer has the legal and financial capacities and the technical and professional abilities to perform the contract to be awarded. All requirements shall be related and proportionate to the subject-matter of the contract". It also considers, Art. 58, (4), that "with regard to technical and professional ability, contracting authorities may impose requirements ensuring that economic operators possess the necessary human and technical resources and experience to perform the contract to an appropriate quality standard".

(2) G. L. ALBANO – R. CAVALLO PERIN – G. M. RACCA, *The Safeguard of Competition in the Execution Phase of Public Procurement: Framework Agreements as Flexible Competitive Tools*, in *Quaderni Consip*, in <http://www.consip.it>, 2010; R. CAVALLO PERIN – G. M. RACCA, *La concorrenza nell'esecuzione dei contratti pubblici*, in *Dir. Amm.*, 2010, 325-354.

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recent modifying law in the Code of Public Contracts guidelines (the so-called Development-decree, d.l. 13 May 2011, converted to L. 12 July 2011 n. 106) ordered to promote a wider participation and to prohibit to aggravate the proceedings.

The idea of limiting the applicability of the exclusion sanction to the non-observance of requirements imposed by law and to the existence of one of the causes for exclusion expressly provided for(3), may, on the one hand, limit the exclusion based on mere documentary deficiencies that are founded on unreasonable formalism and, on the other, ensure greater equality between competitors and thus reduce litigation.

However, we also must consider some extreme cases. If we consider the hypothesis of the temporary deposit provided by the participant to cover any failure to sign the contract in case of adjudication of the contract, we note that Art. 75 Code does not expressly establish exclusion for breach of its presentation. However, this penalty is provided by Art. 75, co. 8 with regard to the commitment of the guarantor to guarantee the execution of the contract if the bidder becomes the contractor (so-called final deposit).

It is, therefore, needed to establish whether the sanction of exclusion operates only insofar it is expressly provided by the Code or the Rules, or also when these rules impose obligations on competitors but without providing an express sanction of exclusion.

Regarding the above-mentioned hypothesis, we can consider a case in which an enterprise has a temporary caution of deficient amount. The contracting authority cannot legally proceed to exclusion because it is not expressly provided for by the legislation.

In fact, where the failure to fulfill required by law involves an absolute uncertainty about the content and the origin of the offer or represents an essential element the exclusion may be disposed. It is therefore preferable to opt for a strict application of the grounds for exclusion, as would be the case of submission of an insignificant caution.

## ***2. The « professional morality » and previous offences for crimes***

At this level, it seems appropriate to consider two aspects, in particular.

Firstly, the special requirement of the so-called « professional morality », (4) which is a cause for exclusion in the presence of previous offences for crimes apt

(3) R. GIANI, *Le cause di esclusione dalle gare tra tipizzazione legislativa, bandi standard e dequotazione del ruolo della singola stazione appaltante*, in *Urb App.*, 2012, 1, 95.

(4) E. CARLONI, *La moralità professionale negli appalti di servizi e di lavori pubblici*, in *Giorn. dir. amm.*, 2007, 8, 851 seq.; P. CORTESE, *Il requisito della moralità negli appalti pubblici*, in *Urb. App.*, 2003, 9, 1054 seq.

to harm the professionalism of the company because it is irreconcilable with carrying out works of public interest using public money.

This is not a matter of examining the hypothesis of the lack of this requirement, rather, it is the case of the total or partial failure to declare possession of it or its characterisation in false terms. This is likely to lead to punitive consequences to be considered in the light of European principles and, in particular, of the principle of proportionality.

In this perspective, it means evaluating the practical operation of a prescription which, according to a formalistic approach, prohibits whoever declares margins of appreciation regarding the possession of the requirements, resulting in the obligation to declare all the reported convictions.

Indeed, although agreeing on the idea of preventing the contracting authority to extend the cases of exclusions for subjective reasons, it seems preferable to assume that the feedback about the seriousness of criminal convictions and their impact on professional conduct should belong to the contracting authority and not to the competitor who is, rather, required to provide all the submitted sentences, without being able to independently make a selection on the basis of mere personal criteria.<sup>(5)</sup>

This means that we need to promote within contracting authorities an efficient practice of the power of control and to believe that the failure to provide sufficient evidence related to a conviction, in self-certification causes the untruthfulness of it and leads to the exclusion of the participant.<sup>(6)</sup>

In order to put the contracting authorities in a position to carry out the required evaluations, the competitors must make complete and accurate statements, under penalty of the exclusion from the tender, with no regard to the remoteness of convictions and offenses, since the mere passage of time cannot produce the effect of rehabilitating or extinguishing penal provisions in the absence of a formal judicial decision.

In this context, it is noteworthy the case of a firm that has made a false declaration because it has failed to declare to be incurred in fiscal accountability in the performance of accounting agent, such as service licensee to

<sup>(5)</sup> Tar Sardegna, Cagliari, 13 February 2013, No. 124.

<sup>(6)</sup> In this context, Directive No. 2014/24/EU considers (Art.57 (4) – Exclusion grounds) that “Contracting authorities may exclude or may be required by Member States to exclude from participation in a procurement procedure any economic operator in any of the following situations: (...) h) where the economic operator has been guilty of serious misrepresentation in supplying the information required for the verification of the absence of grounds for exclusion or the fulfilment of the selection criteria, has withheld such information or is not able to submit the supporting documents required pursuant to Article 59; i) where the economic operator has undertaken to unduly influence the decision-making process of the contracting authority, to obtain confidential information that may confer upon it undue advantages in the procurement procedure or to negligently provide misleading information that may have a material influence on decisions concerning exclusion, selection or award”.

recover tributes. In this case, the Court(7) has considered that the exclusion of the firm from tender is legal.

In fact, the untruthfulness of the statement about the existence of a conviction is an independent cause of exclusion from the tender, regardless of the assessment about the suitability of the conviction to affect the professional morality of the company.(8)

In this sense, in a public procurement procedures the declaration in which the competitor fails to indicate, in the statement concerning any criminal judgement received, a negotiated judgement by art. 444 Code of Criminal Procedure is an untrue statement and, therefore, a lawful clause of exclusion from the tender.(9)

It can be considered the case in which tender regulations require the participating companies to declare all offences committed, under penalty of exclusion, even if they don't consider these offences relevant or apt to affect the professional conduct. If the tender regulation requires that the declaration should encompass (among other things) the case of the possible extinction of the offences, the Court(10) has considered that a company that has failed to declare a conviction concerning the technical director should be excluded, even though it is a conviction for an offence already extinct. In fact, previous criminal offences related to an extinct offence can be an evaluative element of the professional conduct of a candidate. So the dissimilar statement, such as omission of a previous criminal offence, is to be considered itself unreliable because of the sufficient reason that it does not comply the requirement of the tender document.

In another case, the President of the principal company of the group disclosed a conviction for a crime against environment although the jury did not rule on the the crime's impact on professional morality.

The Court(11) has held that the existence of a criminal record does not automatically imply a negative judgement on the professional conduct of the

(7) Cons. St., 14 May 2013, No. 2610.

(8) TAR Piemonte, Torino, 22 October 2012, No. 3738. In the same view of Italian law, the Directive No. 2014/24/EU specifies (Art. 57, (6)) that "any economic operator that is in one of the situations referred to in paragraphs 1 and 4 may provide evidence to the effect that measures taken by the economic operator are sufficient to demonstrate its reliability despite the existence of a relevant ground for exclusion. If such evidence is considered as sufficient, the economic operator concerned shall not be excluded from the procurement procedure. For this purpose, the economic operator shall prove that it has paid or undertaken to pay compensation in respect of any damage caused by the criminal offence or misconduct, clarified the facts and circumstances in a comprehensive manner by actively collaborating with the investigating authorities and taken concrete technical, organisational and personnel measures that are appropriate to prevent further criminal offences or misconduct. The measures taken by the economic operators shall be evaluated taking into account the gravity and particular circumstances of the criminal offence or misconduct. Where the measures are considered to be insufficient, the economic operator shall receive a statement of the reasons for that decision".

(9) TAR Veneto, Venezia, 15 March 2006, No. 601.

(10) Cons. St., 10 December 2012, No. 6291.

(11) Tar Veneto, Venezia, 6 March 2013, No. 349; cfr. Cons. St., V, 30 June 2011, No. 3924; Cons. St., III, 11 March 2011 No. 1583; TAR Puglia, Lecce, III, 13 November 2012, No. 1871; TAR Lazio, Roma, III *ter*, 25 May 2012, No. 4740; TAR Piemonte, Torino, I, 26 January 2012, No. 124.

prospective competitor in a public contract because its relevance should be considered with regard to the object of the tender, the extent of the punishment, and the time elapsed since the commission of the offence.

If the Administration concludes that the criminal record declared by the competitor does not influence its professional morality, it is not obliged to explain in an analytical way the related reasons. The motivation about the lack of seriousness of the offence can be implicit in the admission of the company to the tender. On the contrary, the assessment of seriousness of the offence requires a particular motivational burden because it has an exclusionary effect.

However, in one case<sup>(12)</sup> a company was not excluded from the tender procedure for the award of the renovation of a hospital based solely on a false declaration with regard to the moral and professional reliability of the technical director of the firm. In fact, to exclude a tenderer, it is necessary to have the existence of a judgement of conviction or a plea bargain for offences incident on moral and professional reliability and, even in that case, the company may avoid exclusion if it has taken appropriate steps to dissociate itself from the criminal sanctioned behaviour.

### ***3. The absence of precedents of involvement of economic operators in organised crime***

From the above-mentioned perspective, it is important to carefully evaluate the moral requirement given the absence of precedents of involvement of economic operators in organised crime (Mafia), to be considered with reference to the effects of disqualification, suspension or a prohibition on conducting business with the public administration.<sup>(13)</sup>

(12) TAR Lombardia, Milano, 15 January 2007, No. 20.

(13) G. D'ANGELO, *La documentazione antimafia nel d.lgs. 6 settembre 2011, n. 159: profili critici*, in *Urb. App.* 2013, 3, 256. According to the importance of this cause of exclusion in Italian law, the Directive No. 2014/24/EU, provides (Art. 57 (1) – Exclusion grounds) that “Contracting authorities shall exclude an economic operator from participation in a procurement procedure where they have established, by verifying in accordance with Articles 59, 60 and 61, or are otherwise aware that that economic operator has been the subject of a conviction by final judgment for one of the following reasons: (a) participation in a criminal organisation, as defined in Article 2 of Council Framework Decision 2008/841/JHA; (b) corruption, as defined in Article 3 of the Convention on the fight against corruption involving officials of the European Communities or officials of Member States of the European Union ( 2 ) and Article 2(1) of Council Framework Decision 2003/568/JHA as well as corruption as defined in the national law of the contracting authority or the economic operator; (c) fraud within the meaning of Article 1 of the Convention on the protection of the European Communities’ financial interests; (d) terrorist offences or offences linked to terrorist activities, as defined in Articles 1 and 3 of Council Framework Decision 2002/475/JHA respectively, or inciting or aiding or abetting or attempting to commit an offence, as referred to in Article 4 of that Framework Decision; (e) money laundering or terrorist financing, as defined in Article 1 of Directive 2005/60/EC of the European Parliament and of the Council; (f) child labour and other forms of trafficking in human beings as defined in Article 2 of Directive 2011/36/EU of the European Parliament and of the Council. The obligation

In particular, a company involved in organized crime may have a greater ability to influence the actions of an administration where the officials of the administration involved in evaluating the tenderers have a higher level of discretion. The administration may be able to limit the ability of the company involved in organized crime from influencing the tendering process by limiting the discretion of the tendering officials, to promote the integrity of the process.

In this context, the Court(14) has established that the mere existence of a family relationship or affinity with the subject who is under investigation or convicted for mafia crimes is not a prerequisite, by itself, to automatically establish the existence of criminal infiltration in the company. In fact, it is necessary that the administration prove an actual and effective attempt to influence the practices and decisions of the company.

Consider for example, the case of a company where an employee is the brother of a leading member of an entity involved in organized crime. This situation may suggest that the Mafia is well positioned to infiltrate the company. However, the Court(15) has stated that this situation does not by itself, support a conclusion that the Mafia organization does in fact have the ability to influence the company.

However, even if the family relationship is not by itself sufficient evidence of an attempt of mafia infiltration, the Court(16) considers this relationship in conjunction with other factors such as the attendance, cohabitation or common interest with the suspect, as indicators that the company may be involved in criminal activity.

Similarly, close personal relationships between businessmen, one of whom affected by anti-Mafia information, is not, in itself, a factor which could be reasonably assumed the risk of Mafia infiltration in running the company owned by the second, because, absent any other objective evidence, these are not more than an interpersonal completely neutral relationship.(17)

In particular, the attempt to infiltrate for the purpose of affecting the decisions of the company has been considered sufficient, even if that purpose is not realized in practice. This finding is consistent with factual and sociological characteristics of the Mafia. The Mafia does not necessarily act in an overtly illegal manner, being able to stop at the threshold of intimidation, influence and latent conditioning of economic activities that are formally

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*to exclude an economic operator shall also apply where the person convicted by final judgment is a member of the administrative, management or supervisory body of that economic operator or has powers of representation, decision or control therein”.*

(14) TAR Campania, Napoli, sez. I, 6 May 2013, No. 2306.

(15) TAR Lazio, Roma, 7 March 2013, No. 541.

(16) TAR Campania, Napoli, 11 April 2013, No. 1922.

(17) TAR Calabria, Reggio Calabria, 9 April 2013, No. 209.

lawful. Consequently, even from a fully absolutory judgement can be drawn elements to support the disqualification.

In the case of an audit that examines activity occurring in the distant past, the Court has considered that this situation is not apt to support disqualification. In fact, the long time elapsed, the professional nature of the assignment and the lack of additional evidence demonstrating a different involvement with corporate officers considered close to organized crime, are non-sufficient and suitable to justify the suspicion of a present danger of mafia contamination in the activity of the company.

Therefore, this requirement for economic operators involves assessing the effectiveness of the preventive action, and here it appears important to establish Protocols of Legality as parallel means to those provided by the law in order to play an effective role in law enforcement against organized crime.

“Protocols of Legality” are the means by which administrations and traders enter into an agreement whereby each one within his own specific competence or professional attitude, commits to taking action against organized crime. Through the Protocols of Legality, administration and private parties agree to accept clauses or self-defence terms in order to further empower the participants and discourage the adoption of misconduct, through the use of penalties which is a consequence of a violation of the acceptance clauses.

Accompanied by precise requirements, they may become the means for planning prevention policy, that accompanies, through specific measures, decisions of the government to enable them to recognize and distinguish between good companies and bad.

In short, to promote the integrity of competition and the development of free markets and to combat the monopoly sought by the mafia’s economic culture which promotes its illegal interests, it is necessary to distinguish good companies from those that are subject to mafia intimidation.

#### ***4. The regularity of deductions***

Finally, in the context described above, similar considerations should be given to the requirement of regularity of deductions and the amount of power of the contracting authority in order to ascertain and estimate the severity of the violation.<sup>(18)</sup>

The importance of this aspect becomes clear when one considers that the failure to comply with tax obligations and contributions by some traders, at the same time, ends in a situation where “with higher costs and lower profits, with

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(18) L. PRIMICERIO, *Il requisito generale di regolarità fiscale nel codice dei contratti pubblici*, in *Urb App*, 2008, 6, 703 et seq.

the same price, honest entrepreneurs will eventually leave gradually from the market [precisely] because of competition of dishonest businessmen, making it the effect of adverse selection in the competition immediately obvious".(19)

In the Italian law there is a special requirement, the so-called DURC, consisting of a certificate attesting to the compliance of legislative and contractual obligations in respect of INPS, Inail Banks and construction company. This document is now automatically provided by contracting authorities, to traders who seek to participate in a public tender.

The assessment made by social security institutions shall be binding on contracting authorities and precludes them an independent assessment.(20) In fact, by introducing a legal threshold regarding the seriousness of the violation, the law deprives the contracting authority of any discretion regarding the evaluation of nature of the violation.(21)

Consider for example, the case of a company that has submitted its offer and has stated, in regard to the regularity of the payment of social security contribution, that it is unable to make use of a computerized DURC because the irregularity does not match the company's position but the individual position of its administrator as manager of other business.

The Court(22) has considered unlawful a DURC that stated contributory irregularities by the competitor, because the issue of the DURC took place on

(19) TAR Sicilia, Catania, sez. III, 10 October 2013, No. 2429. In this context, it is important the provision of Directive No. 2014/24/EU, Art. 57 (2) where it establishes that "*An economic operator shall be excluded from participation in a procurement procedure where the contracting authority is aware that the economic operator is in breach of its obligations relating to the payment of taxes or social security contributions and where this has been established by a judicial or administrative decision having final and binding effect in accordance with the legal provisions of the country in which it is established or with those of the Member State of the contracting authority. Furthermore, contracting authorities may exclude or may be required by Member States to exclude from participation in a procurement procedure an economic operator where the contracting authority can demonstrate by any appropriate means that the economic operator is in breach of its obligations relating to the payment of taxes or social security contributions. This paragraph shall no longer apply when the economic operator has fulfilled its obligations by paying or entering into a binding arrangement with a view to paying the due taxes or social security contributions, including, where applicable, any interest accrued or fines*".

(20) H. D'HERIN, *La Plenaria fa luce sull'efficacia del durc ai fini dell'esclusione dalle gare di appalto*, in *Urb App.* 2012, 8/9, 911 ss. The importance of this cause of exclusion, as well as the one concerning convictions, arise from the further provision according to which (Directive No. 2014/24/EU, Art. 57 (3)) "*Member States may provide for a derogation from the mandatory exclusion provided for in paragraphs 1 and 2, on an exceptional basis, for overriding reasons relating to the public interest such as public health or protection of the environment. Member States may also provide for a derogation from the mandatory exclusion provided in paragraph 2, where an exclusion would be clearly disproportionate, in particular where only minor amounts of taxes or social security contributions are unpaid or where the economic operator was informed of the exact amount due following its breach of its obligations relating to the payment of taxes or social security contributions at such time that it did not have the possibility to take measures as provided for in the third subparagraph of paragraph 2 before expiration of the deadline for requesting participation or, in open procedures, the deadline for submitting its tender*".

(21) TAR Puglia, Lecce, 21 November 2012, No. 8.

(22) Cons. St. Ad. Plen., 4 May 2012, No. 8.

a different subject that charged the company with an obligation concerning individual positions of its members. In fact, in that case the irregularity referred only to the position as holder of an autonomous business.

As the Court has held,(23) the regular contribution is a requirement for participation in the tender and must be held at the date of expiry for submission of tenders. Otherwise, the result is the exclusion of non-complying tenders.

### 5. Conclusions

The introduction of the Italian Public Contracts Code has not fully resolved certain critical issues. In particular, these include overly rigid procedural requirements, resulting in costs to individuals whether associated with traditional time-consuming procedures for the adjudication, and some institutions created to promote competition or for reasons of speed and efficiency, the use of which creates significant practical problems and frequent causes of opportunistic behaviour by private parties and corruption risks.(24)

It is certainly necessary to avoid the imposition of purely formal obligations for competitors who, despite achieving the dual goal of setting up tenders to present serious and well documented offers as well as an easy evaluation by the contracting authority, represent only an unnecessary procedural burden even more than for the entrepreneurs participating in the bid and for officials of the contracting authority and the members of the jury who struggle with difficult problems of interpretation.

Therefore, in keeping with the disposition of the European Union,(25) it seems preferable to bring the formal discipline of public tenders to the original simplicity of the auction governed by the laws of State Accounting: few, but mandatory,(26) formal requirements, ample opportunities to participate in the tender except in case of possession of limited participation requirements, with reference to all matters regarding the suitability of the offer and the bidder

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(23) G. M. RACCA, *La prevenzione e il contrasto della corruzione nei contratti pubblici (Art. 1, commi 14-25, 32 e 52-58)*, in B. G. Mattarella – M. Pelissero (eds. by) *La legge anticorruzione. Prevenzione e repressione della corruzione*, Torino, 2013, 125-151; F. DI CRISTINA, *La corruzione negli appalti pubblici*, in *Riv. trim. dir. pubbl.* 2012, 1, 177.

(24) M. TRYBUS – R. CARANTA – G. EDELSTAM, *EU Public Contracts law. Public Procurement and beyond*, Bruylant, Bruxelles, 2014.

(25) F. MANGANARO, *I contratti sotto soglia comunitaria*, in F. Saitta (ed. by) *Il nuovo codice dei contratti pubblici di lavori, servizi e forniture*, Padova, 2008, 939 et seq.

(26) G. M. RACCA, *The role of IT solutions in the award and execution of public procurement below threshold and list B services: overcoming e-barriers*, in D. DRAGOS – R. CARANTA (Eds.) *Outside the EU Procurement Directives – Inside the Treaty?*, Copenhagen, 2012, 373 et seq.; G. M. RACCA, *Public Contracts – Annual Report 2012*, in *Ius Publicum Network Review*, 2012, 1 et seq.; G. M. RACCA, *Report on Italian Public Contracts – Part. I*, in *Urb. e app.*, 2012, 859 seq.; G. M. RACCA, *Report on Italian Public Contracts – Part. II*, in *Urb. e app.*, 2013, 1, 5 seq.

after the adjudication, in the control of it, both in the verification of the regularity and in the execution of work.

In this perspective, the Italian legal system provides some preventive measures against corruption in public procurement, some certainly need to be strengthened, while others are not yet implemented.

Indeed, procurement decisions taken without considering market structures, bring the risk of consolidating or even aggravating anti-competitive structures.

In this sense, it might be useful to add to the current qualification system “objective reputational parameters” based on the behaviour of firms and standardized on evaluation schemes for use by all the contracting authorities.

In this way, a greater degree of knowledge about the contractors with whom the contracting authority most likely will enter into contractual relations would be provided. However, the relationship between consolidated reputation and full competitiveness of the market must be carefully balanced: the introduction of objective reputational parameters may form a real barrier for new entrants and an element of restrictiveness for notices. Furthermore, the provision of objective parameters should not be based only on the subject’s reputation: if we accept that reputation is a merely social evaluation, we must also accept that parameters of reputation can hardly be objective.

## CHAPTER 5

### Brief notes on the role of “protocols of legality” in Italy

BY

Loredana GIANI

Professor of Administrative Law, University of L'Aquila

#### ***1. Introduction***

The aim of this chapter is to give a general overview of the legal framework against corruption, focusing on some of the main aspects that have a greater impact on public contracts. The second part of the paper will focus on the application that some of the institutes and principles provided by the law have had on the sector of public contracts where instruments such as the “protocols of legality” were introduced to guarantee the “quality” of the contractors, and which have played and are still playing an important role in some regions, such as Campania and the Abruzzi, where in the latter they have a significant role in the management of part of the reconstruction of the area destroyed by the earthquake of 2009.

#### ***2. A new legal framework against corruption***

The legal framework against corruption in the public administration, and therefore in the area of public procurement, has changed noticeably in recent years.

A first important input came from Law No. 134/2012, with which Legislative Decree No. 83/2012 (the so-called Development Decree) was converted, which introduced a new article in the Criminal Code (236 bis) concerning “*False statements and reports*”. The article provides that:

*“the professional who reports false information or omits to report relevant information in the reports or certificates referred to in Articles 67, third paragraph, letter d), 161, third paragraph, 182 bis, 182 quinquies and 186 bis, can be punished with imprisonment from two to five years, and a fine of 50,000 to 100,000 euros.*

*If the act is committed in order to achieve an unfair profit for him/herself or for others, the punishment is increased. If the fact results in damage to creditors the punishment is increased up to a half.”*

It is clear that the legal right to be protected is identified with the trust that the abovementioned statements and reports must have in the light of the

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certain and prompt carrying out of the insolvency proceedings to which they refer, qualifying this as a crime against public trust.

Even if there is not a direct connection with the matter under examination the abovementioned law certainly expresses a new legislative trend that saw an important further step in Law no. 190 of 6 November 2012, which contains rules for the prevention and combating of corruption and illegality in the public administration, and was the source for the legislative decrees on “*Incompatibility and incompatibility with elected office*”(1) and on the “*prohibition to appoint and suspension of appointments for public administrations and private entities under their control.*”(2)

### ***3. The principal authorities involved in the anti-corruption framework***

The most significant elements of the law, for which the legislator, following a style that can undoubtedly be criticised for not presenting the necessary requirements in terms of clarity and ease of reading the text,(3) concern the subjective profile.

In accordance with the provisions contained in Article 6 of the United Nations Convention against Corruption, the tasks of the National Authority Against Corruption have been handed to the existing Commission for Control, Transparency and Integrity of Public Administrations.

Instituted by Art. 13 of Legislative Decree no. 150/2009, the five members who compose the Commission are appointed by the President of the Republic, on the proposal of the Minister for the Public Administration and Innovation, in agreement with the Minister for the Implementation of the Programme of Government, and after the opinion expressed by the competent Parliamentary Commissions.

The president of the Commission is elected by the five members from among themselves.

Even if there is a close evident link with the Government, which implies a strict connection with the political level, so as to potentially exclude the independence (from politics) of the Commission itself, there are some elements that could lead, as pointed out by some authors, to a different conclusion.

In fact, the members of the Commission are chosen from among experts possessing a high degree of professionalism, experienced in the sectors of

(1) Italian Legislative Decree 31 December 2012, No. 235.

(2) Italian Legislative Decree 8 April 2013, No. 39.

(3) The law contains just two articles, because of the special procedure chosen for its parliamentary approval. The first is articulated in 83 paragraphs, and the second provides only the prohibition to impose new or additional burdens on public finance.

public services, management and evaluation of performances, and in personnel management and evaluation.

In addition to this, the members of the Commission cannot be chosen from among those who hold elective public office or positions in political parties or trade unions, or who have had such duties in the three years prior to the appointment and shall not have any characteristics that are in conflict with the functions of the Commission. Moreover the members are appointed for a period of six years and may be reappointed once.

At the time of appointment, if civil servants or judges in active service, the members of the Commission are transferred from these roles and their positions can only be filled by a substitute for the duration of their mandate; if university professors, they are placed on unpaid leave.

In addition to its usual tasks aiming at directing, coordinating and supervising the independent exercise of the function of assessment, to ensure transparency of the evaluation systems, and the comparability and visibility indices of management, the Commission has some specific tasks, related to its function as National Authority Against Corruption. These tasks include the approval of the National Plan Against Corruption that the Department of Public Safety has to elaborate every year, in accordance with the policy defined by the Inter-Ministerial Committee.

The Authority analyses the causes and factors of corruption and identifies the interventions that can favour its prevention and contrast; voluntarily expresses opinions for the organs of the State and all other public administrations regarding the compliance of the acts and behaviour of public officials to the law, codes of conduct and collective and individual agreements governing the civil service; supervises and controls the concrete application and effectiveness of the measures taken by the Government in accordance with paragraphs 4 and 5 of Article 13, and the compliance with the rule on the transparency of administration.

It is interesting to point out that for the performance of the tasks mentioned above, the same decree gives the Commission the power to make inspections by means of requests for information, records and documents to public administrations and the power to impose the adoption of the acts required by the plans ruled by paragraphs 4 and 5 and the rules on transparency, or the overturning of the decisions or the prohibition of behaviour which are in contrast with the plan.

Alongside the Authority, the other institutional figures involved in this framework against corruption are: the Department of Public Safety, which operates, in accordance with the policy stated by the Inter-Ministerial Committee, for the definition of the general aspects such as the abovementioned plan or the

definition of standards for transparency, or for the alternation of management in those sectors which are particularly exposed to corruption; the Department of Public Function; the Prefects; the official in charge of the prevention of corruption, who is appointed by the political leadership of each administration, as a rule from among the upper echelons of the same administration, and in the local authorities it usually coincides with the General Secretary, unless decided differently and justifiably.

Among the main tasks of the official in charge of the prevention of corruption are the control on the effective implementation of the three-year plan for the prevention of corruption, the proposal of its amendment when significant violations are found or when significant changes in the organisation or the activity of the administration occur; the verification, in agreement with the competent management, of effective job rotation in the offices responsible for the performance of activities characterised by the presence of a higher risk of crimes of corruption being committed; the identification of staff to be included in training programmes.

The main objective of the official in charge is the prevention of corruption, so that if, within the administration, a crime of corruption is established in a final judgment, the “official in charge” is not only considered as having failed to achieve the objective (in terms of assessment of its activity), but is also responsible from a disciplinary point of view for the loss of revenue and for the damage to the image of the public administration, unless he/she cannot demonstrate the following circumstances:

- a) to have prepared, before the commission of the offence, the three-year plan and to have complied with all the requirements of the law;
- b) to have monitored the operation and compliance with the plan.

Disciplinary action for the failure to “prevent corruption” cannot be less than the suspension from duty without pay for a minimum of one month to a maximum of six months.

In case of repeated violations of the preventive measures contained in the plan, the “official in charge of the prevention of corruption” is also responsible, on a disciplinary basis, for the lack of control.

The breach by the employee of the administration of the preventive measures contained in the plan constitutes a disciplinary offence.

By December 15 of each year the official in charge of the prevention of corruption of each public administration publishes, on the website of the administration itself, the results of their activity and transmits the report to the political management of the administration which can directly hear from the “official in charge of the prevention of corruption”.

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#### ***4. The (three-year) plan for the prevention of corruption***

In order to prevent corruption, one of the key elements is the three-year plan for the prevention of corruption that shall be adopted by January 31 of each year and sent to the Department of Public Safety.

The plan is approved by the political management of the administration on the proposal of the official in charge of the prevention of corruption.

In order to prepare the plan for the prevention of corruption, technical and IT support can be requested of the Prefect also in order to ensure that the plan is formulated and adopted in accordance with the guidelines contained in the National Plan approved by the Commission.

Persons outside the administration cannot be entrusted with the preparation of the plan and the failure to draw up the plan and adopt procedures for the selection and training of employees are elements for the assessment of managerial responsibility.

The contents of the plan and its aims seem to be quite clear.

It must identify the activities characterised by a higher risk of corruption, including in the list the proposals of the managers of the public administration; it must provide, for these activities, mechanisms of training, implementation, and monitoring of the decisions suitable to prevent the risk of corruption; it must provide, for the same activities, an obligation of transparency for the person responsible for the supervision, functioning and compliance with the plan; monitor the compliance with the terms provided for by law or regulations, for the conclusion of proceedings; monitor the relations between the administration and those who enter into contract with it, or who are interested in authorisations, licences and delivering economic benefits, also verifying the existence of any kind of kinship or affinity between the proprietors, the directors, the shareholders, the employees and the management and the employees of the administration; identify specific transparency requirements, additional to those provided for by law.

#### ***5. The key role of transparency***

Another element that has a central role within the framework of the law is transparency. In fact, it has been referred to as an “essential level of benefits relating to social and civil rights” pursuant to Article 117, second paragraph, let. M), of the Constitution. It has to be ensured, according to the provisions contained in the law, by the publication on institutional websites of public administrations of information concerning the administrative procedures (including public contracts), according to criteria of easy accessibility,

completeness and ease of consultation, in accordance with the provisions of state and professional secrecy, and data protection.(4)

Among the data that have to be published on the institutional website we also find the budgets and final accounts, as well as the unit cost of construction of public works and production of services provided to citizens. The information on costs is published according to a framework drawn up by the Authority for the Supervision of Public Contracts for Works, Services and Supplies, which also deals with the collection and publication on its institutional website in order to allow an easy comparison.

In particular, the maximum transparency must be guaranteed with special reference to the procedures of authorisation and concession; the selection of a contractor for the award of works, supplies and services, including the means for selecting the contractor chosen among the categories provided in the Code for Public Procurement; granting and payment of contributions, grants, financial aids, as well as the attribution of economic benefits of any kind to individuals and public or private entities; competitions and selection for civil servants and career advancement.

By January 31 of each year, the information on the previous year is to be published in summary tables made freely available in digital format, which allow analysis and editing of the data, also for statistical purposes.

The same information must be submitted in digital format to the Authority for the Supervision of Public Contracts for Works, Services and Supplies which shall publish them on its institutional website in a section freely available to all citizens, categorised according to the type of the contracting authority and by region. And the same Authority, by April 30 of each year, has to transmit to the Court of Auditors the list of administrations that failed to transmit and publish, in whole or in part, the abovementioned information.

Again, a missing or incomplete publication of the information is considered a violation of quality and economic standards and is the source of responsibility for managers, and the heads of the services are responsible for any delays in updating the information.

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(4) In addition to the abovementioned duties related to the guarantee of transparency, the law has modified other provisions of the Law on Administrative Procedure. In particular the provision stating the terms for the conclusion of the proceedings has been modified, stating the duty to conclude a proceeding by issuing an act, also in the case of a negative response to the instance presented. The first paragraph of Article 2 has been amended as follows: *“if the procedure follows an instance, or if it must be initiated ex officio, the public authority has a duty to conclude it by adopting an explicit measure. When the administration recognises its manifest inadmissibility, or that it is unfounded, it must conclude the proceeding with an express measure, even written in a simplified form, outlining the reasons which may consist of a brief reference to the point of fact or law considered decisive”*. It is not a very significant change in terms of the recognition of the duty of the public administration to conclude a proceeding with the adoption of an express measure and the simplification of the duty to give reasons in the case of a negative result of the proceeding connected to the recognition of the inadmissibility (from a formal point of view) of the request or its being unfounded, but it undoubtedly represents in a certain way a reduction of the level of guarantee for the individual or for the private entity involved.

### **6. *The guarantee of impartiality of public officers***

The last aspect to be considered for a general outline is related to the changes that are due to have a significant impact on the organisation of the administration.

The first change regards the Administrative Procedure Act, to which has been added Article 6 *bis*, which provides that “the head of the procedure and those who are in charge of the relevant offices to adopt opinions, technical evaluations, acts having a specific relevance within another proceeding and the final order, shall refrain in the case of conflict of interest, indicating any conflict, even only potential.”

It is a provision which goes along with the amendment of Article 53 of Legislative Decree No. 165/2001, on the incompatibility and offices of civil servants and the regulation provided in the abovementioned Legislative Decree No. 39/2013.

According to the new rule, the government cannot give to employees tasks not included in the tasks and duties of the office, which are not expressly provided for or regulated by law or other sources of law, or that are not expressly authorised.

Public employees may not engage in paid positions that have not been delivered or authorised in advance by the administration in which they are employed. Failure to comply with this provision has various consequences: first the possibility to apply severe sanctions and disciplinary liability; second the compensation payable for the performance carried out shall be paid (or repaid) to the financial account of the administration for which the employee is working, and it is only to be destined to increase the productivity fund or its equivalent. The non-payment of the amount by the public servant integrates a public tax liability under the jurisdiction of the Court of Auditors.

Employees who, in the last three years of service, have had authoritative or negotiating powers on behalf of a public administration, cannot work, in the three years following, be employed by or have any professional activity for the private parties who are the recipients of the (authoritative) activity of the public administration. The sanction is clear because it has been provided that any contract or appointment made in violation of this provision shall be null and it is forbidden to those who have entered into these contracts to negotiate with any public administration for the following three years, with the obligation to repay the money earned for these contracts.

In this case the duty of transparency is extended to the private sector as well. In fact it is provided that within fifteen days of the remuneration for the (authorised) tasks the public or private entities must notify the relevant

administration of the amount of compensation paid to civil servants. And any assignment or authorisation, even if free of charge, to employees has to be communicated electronically by the relevant administration (which gave the assignment) to the Department of Public Function, with the indication of the object of the assignment and the gross compensation. The communication is accompanied by a report which sets out the rules under which the duties have been conferred or permitted, the reasons for granting authorisation, the criteria for the selection of the employees whose assignments have been given or authorised and the compliance of the same with the principles of good administration and the measures that will be taken to contain spending.

### ***7. Public contracts and agreements against corruption***

The abovementioned framework, in the area of public procurement, has been somehow preceded by the practice of entering into specific agreements between the prefects and companies or other administrations in order to guarantee legality within the procedures; and by Article 17 *quater* of Legislative Decree no. 195/2009 Urgent Provisions on Waste in Campania and the Post-Earthquake Emergency in the Abruzzi, converted into Law No. 16/2010.<sup>(5)</sup>

The Article entitled “Prevention of infiltration of organised crime (Mafia) in the interventions for the construction of prisons” gives prefects, in the geographical areas within their competence, the task of ensuring coordination and unity of direction in all the activities aimed at preventing the infiltration of crime in the awarding and execution of public contracts for work, services and supplies, for the construction of prisons.

But the effective extent of this provision is not limited to the specific area considered, because the following paragraphs of the Article refer to a wider system of controls which is extended essentially to all the areas of the so-called “grandi opere” (major works) for which has been outlined a complex system of controls headed by the Coordinating Committee for the General Supervision of “Grandi Opere”, instituted within the initiative against the Mafia, provided in Article 15, paragraph 5 of Legislative Decree No. 190/2002, now included in Article 180 of the Code of Public Contracts (Legislative Decree No. 163/2006).

According to the provision contained in the second paragraph of Article 17 *quater*, the Coordinating Committee gives immediate and direct support to the prefects, by means of a specialised section set up in the prefecture which is a form of operative connection between offices that already exist.

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<sup>(5)</sup> In line with the provisions contained in Article 35, Dir. 2014/23/UE and Article 24, Dir. 2014/24/UE.

In addition to this, the third paragraph, provides that “the anti-Mafia controls on public contracts and subsequent subcontracts relating to work, services and supplies, and on granting public providences, realised in implementing the programme of interventions referred to in Article 44 *bis*, Legislative Decree 30 December 2008, No. 207, converted, with amendments, by Law No. 14, 27 February 2009, are also made in compliance with the guidelines set by the Coordinating Committee for the General Supervision of the «Grandi Opere», as an exception to the provision of the Regulation of the Decree of the President of the Republic No. 252 of June 3, 1998”.

For the effectiveness of the anti-Mafia controls provided in paragraph 3, the traceability of related cash flows has been provided for, as well as the creation, at the territorial level of the prefecture, of lists of suppliers and service providers which are not at risk of Mafia infiltration.

### 7.1. The Coordinating Committee

The Coordinating Committee has been created, given the importance that the public procurement market plays, especially in the infrastructure sector included in the Strategic Infrastructure Programme provided by Law No. 443, 21 December, 2001, (the so-called *Legge obiettivo*), and it ensures the implementation of the provisions and measures contained in the Ministerial Decree of 14 March, 2003, for the carrying out of activities for the prevention of criminal infiltration.

The framework of the competences of the Coordinating Committee has been expanded following the entry into force of the emergency legislation for the earthquake in the Abruzzi and the Milan Expo of 2015 and the Prisons Plan.<sup>(6)</sup>

The abovementioned provision provides that the anti-Mafia controls on contracts, subcontracts for works, services and supplies related, respectively, to the realisation of reconstruction work in the Abruzzi, after the earthquake of 6 April, 2009, to the works and the interventions related to the implementation of the Milan Expo 2015 programme, and to the implementation of the programme of measures for the building of prisons, are made in compliance with the guidelines set by the Coordinating Committee.

The monitoring system, as outlined by the Ministerial Decree of 14 March, 2003, is structured as a network, due to the geography of the country, which contemplates at the central level the Coordinating Committee, in which is guaranteed the presence of those administrations that are more involved

(6) Law Decree 28 April 2009, No. 39, Art. 16, converted by Law No. 77/2009; Italian Law Decree 25 September 2009, No. 135, Art. 3-*quinquies*, converted by Law 20 November 2009, No. 166, and Italian Law Decree 30 December 2009, No. 195, Art. 17-*quater* converted by Law no. 26 February 2010, No. 26.

in the specific subject (the Ministry of the Interior, Office of the Minister; the Anti-Mafia Investigation Department of the Ministry of the Interior; the Department of Public Safety – Central Direction of Criminal Police, Criminal Analysis Service of the Ministry of the Interior; the Presidency of the Council of Ministers, Department for Planning and Coordination of Economic Policy – DIPE; the National Anti-Mafia – DIA – which coordinates investigations in proceedings for offences of organised crime; the Ministry of Infrastructure, which has some core competences in the field of public works; the Ministry of Economy and Finance, on issues related to the activities against money laundering; the Authority on Public Contracts for Works, Services and Supplies in which operates the National Observatory on Public Works; at the local level, the prefectures – now territorial offices of the Government – and the inter-force groups, which are coordinated by a vice-prefect, and are composed of the representatives of the territorial police forces, a representative of the Operative Centre of the DIA competent for that territory, representatives of the territorial administration for public works, labour and social security – the latter, in particular, to contrast the phenomenon of “moonlighting” and to ensure safety in the workplace, both of which reveal possible criminal interference in local contexts characterised by a weak sense of legality).

The provincial inter-force groups are connected to the Coordinating Committee and form a network, in the sense that they exchange information and data related to public infrastructures that are established within their areas of jurisdiction. They provide information and specific analysis to the prefect and ensure constant information to the Coordinating Committee for the general supervision of major works, and represent the operational interface of the Anti-Mafia Investigative Directorate.

The latter has a specific mandate for anti-Mafia activities related to public procurement and for this reason has developed over the years a strong know-how in the area – and has realised and manages at a central level the Central Observatory for Procurement (OCAP), an electronic system for collecting data and information acquired by the inter-force (interagency) groups when they access and inspect public construction sites.

In addition to this, Article 176 of the Code of Public Contracts provides that, on the basis of the proposals of the Coordinating Committee, guidelines for legality for the sector of “grandi opere” will be structured which shall also include the monitoring of financial flows throughout the entire supply chain of those who take part in the realisation of the interventions (from the contracting authority, to the general contractor, the contractor, the sub-contractors and suppliers).

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### *8. The experience of the Abruzzi*

In relation to the specific experience of the earthquake in the Abruzzi, the Coordinating Committee has issued various sets of guidelines, the first on 8 July 2009,<sup>(7)</sup> concerning the first phase of the operations following the earthquake in the Abruzzi, in particular the construction of residential complexes called CASE Project and set in advance specific forms of control over cash flows, provisions then contained in the DPCM provided in Art. 16, paragraph 5 of Law No. 77/2009. These guidelines have been amended.<sup>(8)</sup> The document aims to adapt the system of control to the increasing complexity of the system for reconstruction resulting from the increase of the subjects involved in the reconstruction (public procurement and execution of the works). The anti-Mafia report, issued by the prefect to the contracting authority, is the primary instrument for monitoring, but it has to be issued exclusively by the Prefect of L'Aquila even if they come from other prefectures in relation to the head office of the contractor.

A central role in the chain of control is also entrusted to the Specialised Section of the Coordinating Committee, chaired by the Prefect of L'Aquila, and to the Central Inter-Force (interagency) Group for the Reconstruction (Gicer) whose task is to analyse the flow of information.

The guidelines are divided into “Provisions which are exceptions to the jurisdiction over anti-Mafia reports”; “Provisions addressed to the contracting authorities and the Prefect of L'Aquila, with a view to harmonising monitoring procedures”; “Provisions relating to financial tracking, in line with the provisions contained in the special plan for the fight against the Mafia”.

Among the instruments provided by the guidelines we can find:

- a memorandum of understanding for the anti-Mafia controls that the Prefect of L'Aquila and the Commissioner for Reconstruction (the President of the Region) shall conclude on a proposal of the prefect providing for, among other things, the realisation by every contractor of an inspection plan of the construction site, a kind of database that would also trace the flow of local labour, which is easily subject to Mafia interference.
- the applicability of the anti-Mafia legislation on information also to foreign operators;
- the establishment, on an experimental basis, in L'Aquila, Pescara and Teramo Prefectures of lists of suppliers and service providers with registered offices in the territory of the three provinces that operate in areas considered to be particularly vulnerable to Mafia interference.

(7) Published in the Italian Official Gazette No. 156, July 8, 2009.

(8) The text was published in the Italian Official Gazette No. 186 August 12, 2010.

The guidelines were amended at the end of 2010(9) in order to extend the provision to those interventions for the reconstruction of private houses, so extending the regulation to private procurements as well, which are not awarded according to procedures provided in the Code of Public Contracts but are subject to some specific provisions such as the need for proprietors to request quotes from five construction companies, and to respect the provisions on the traceability of financial cash flows.(10)

In the third guidelines, the so-called anti-Mafia certificate for private procurement was not required, a requirement specifically provided for public procurement, also for a practical reason, in order to avoid further aggravating citizens, and because of the impossibility of screening a number of construction companies (some of them very small) that was higher than those employed in the reconstruction of the public part of the city. Merely by way of illustration, in 20 months, the construction companies involved in the “public reconstruction” amounted to more than 2,230 (all subject to anti-Mafia controls); while for the “private reconstruction” the number of construction companies could be more than 20,000. Therefore to apply the public system of control, in this context, would have been impossible, with evident consequences on the times needed to issue the required licences for reconstruction.

The system provided by the guidelines gives an important role to the municipalities (mainly the Municipality of L'Aquila) which are part of the network for the anti-Mafia monitoring outlined by the Ministerial Decree of 14 March 2003. It has been provided that the municipalities have to guarantee that contracts entered into by the proprietors with the construction companies must include clauses on the financial traceability of cash flows and on the exclusion of construction companies linked to the Mafia, granting to the proprietors the faculty to terminate the contract.

### ***9. Protocols of legality and anti-Mafia reports***

Another instrument that has been introduced in order to prevent Mafia interference in economic activities are the abovementioned Protocols of legality. They are agreements that any public administration can enter into, according to the provision contained in Art. 15 of Law No. 241/90 (Administrative Procedure Act), in order to establish a common commitment to ensure legality and transparency in the execution of a certain work, or in the provision of services, especially for the prevention, control and contrast of the attempt at Mafia infiltration, as well as for the control of security and safety in workplaces.

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(9) Published in the Official Gazette of December 31, 2010.

(10) Del. 26 April 2012.

In the protocols, the administration will take on, as a rule, the requirement to include in any invitation to tender, as a condition for participation, prior acceptance by the economic operators of certain clauses that reflect the purpose of prevention indicated in the protocol.

Typical is the case of the commitment to report any illegal request for money, attempt at extortion, intimidation or bias against the company, made to the company, before the tender or during the execution of the contract.

In this way the constraints provided by anti-Mafia regulation are strengthened by means of this forms of voluntary control not provided for in the regulation and which apply also to subcontracts.

The protocols have a contractual nature, and the consequences of the breach of the obligations provided in them are the immediate and automatic termination of the contract, if elements relating to attempts at Mafia infiltration emerge.

The effect is obviously decisive, legally, resulting in the termination of all its effects, and, more importantly, economically.

An interpretative problem can arise considering the content of Article 38 of the Code of Public Contracts which states the stringency of the grounds for exclusion. In fact it could lead to doubts as to the possibility of conditioning the participation in the tender to the acceptance of protocols (or obligations referred to therein), since the acceptance is not required by current legislation and because the rejection does not affect the further consequences provided by Art. 46, paragraph 1 *bis*.(11)

A different conclusion should, however, be reached as regards the execution phase of the contract.

As a general rule, Art. 1341 of the Civil Code provides that the general conditions of a contract prepared by one party with another are effective if at the time of the conclusion the parties knew or ought to have known, by using ordinary diligence, of a circumstance that in this case is contained therein.

It can be referred, more in general, to the principle of good faith in conducting contract negotiations and as in the execution phase as well, with reference to which the refusal to accept by the contractor has to be motivated.

In fact, contracting authorities may provide in the notices or letters of invitation that non-compliance with the provisions contained in the “protocols of

(11) “*The contracting authority excludes candidates or tenderers in the case of non-compliance with the requirements provided for in this code and regulations and other applicable laws, and in cases of absolute uncertainty on the content or source of supply, because of a failure to sign it, or other essential elements, or if the envelope containing the bid or the request for participation was not sealed or other irregularities related to the closure of the proposals, that foresee, according to the concrete circumstances, the possibility that the secrecy of the tender has been violated; calls and letters of invitation cannot contain more requirements than those provided by the law under penalty of exclusion. Any such requirements would be void*”.

legality” or in the “agreements of integrity” constitutes grounds for disqualification.

It is a significant extension of the grounds for disqualification that were listed in Article 38 of the Code.

With regard to procedures for the selection of contractors, the contracting authorities must immediately publish on the official website:

- a) the contracting authority;
- b) the subject of the notice;
- c) the list of subjects invited to tender;
- d) the contractor;
- e) the amount of the award;
- f) the time of completion of the work, service or supply;
- g) the amount of the sums paid.

Moreover, it is necessary to stress that the terminating effect of the anti-Mafia report is not only a consequence of a contractual provision, entered into because of the protocol. In fact, these clauses can frequently also be found outside the scope of the abovementioned protocols.

In addition to the protocols, the Italian system, in accordance with Article 10, paragraph 9, of Presidential Decree No. 252/1998, provides at least two different types of anti-Mafia report, typical and atypical: the first leads to the prohibition of the conclusion (i.e. the automatic termination) of the contracts with companies for which elements proving the interference of Mafia organisations emerge (through so-called typical or disqualifying information); the second consists in the offer to the administration of elements that – although not such as to lead to the conclusion of thinking that Mafia interference exists – allow the same administration to evaluate, within their discretion and in accordance with the law, the subjective requirements of the contracting entity (through so-called atypical information).

Following the abovementioned reconstruction, the Administrative Court<sup>(12)</sup> stated that the so-called Protocol of Legality:

*“in determining cases which bring to the duty of immediate and automatic termination of the contract, refers to elements which consist in an anti-Mafia report having an interdictive value. On one side, it emerges from the coordinated reading of let. C) and D) of Article 2, it not being reasonable to assume that the two provisions have the same consequences (that is, the immediate and automatic termination of the contract) on the one hand or a formal «anti-Mafia report having an interdictive value» and, on the other, on not better defined elements (atypical) related to an*

(12) TAR Lazio, Rome, I, 18 October 2010, No. 32839.

*attempt at interference. On the other side, it is quite clear that an immediate and automatic effect of revocation of a measure which widens the legal sphere of the individual (including a company), and, most importantly, the unilateral termination of a contract, cannot attain to that hypothesis punctually defined by the legislature, and that consent to consider (reasonably) as restricted the activity of the administration and that, imposing itself as factum principis, justify the termination of the contract.*

*This means that the revocation of the licence and the termination of the contract, automatically and immediately defined, can be achieved only in the presence of disqualification causes provided by the law, but cannot follow immediately and automatically on the mere detection of elements – which are not ex se an anti-Mafia report having a pre-emptive effect – that have to be evaluated by the administration and therefore to be motivated in relation to their relevance.”*

Ultimately, then, the atypical anti-Mafia report does not lead automatically to the termination of the contract and the contracting authority has to evaluate autonomously and exercising its discretion, deciding on the possibility of terminating the contract, acting on the information contained in the abovementioned report. It is interesting to note that, referring to the area of L'Aquila, the companies checked are 2,834 (1,982 according to the 1<sup>st</sup> ed. of the guidelines; and 852 on the basis of the provisions contained in the 2<sup>nd</sup> and 3<sup>rd</sup> guidelines).

The most relevant and difficult aspect of the regulation of these reports is the information, listed in Articles 84 and 91 of the anti-Mafia Code,(13) the anti-Mafia communication(14) and the anti-Mafia reports.(15) Highly uncertain are the criteria on the basis of which the Prefect competent for the geographical area where the company has its registered office evaluates the “attempt of Mafia infiltration”. In addition to some objective criteria such as judicial decisions that provide a precautionary measure or which provide even a non-definitive sentence for specific crimes, there are some other elements that noticeably widen the discretion of the Prefects without giving the necessary certainty to the evaluation contained in the inquires that they make in the exercise of the powers delegated by the Ministry of the Interior.

And according to the provision contained in paragraph 6 of Article 91, the Prefect can deduce/gather the attempt of Mafia infiltration also from non-definitive sentences for crimes instrumental to the activities of criminal

(13) Italian Legislative Decree 6 September 2011, No. 159, Anti-Mafia Code and precautionary measures, and new rules on anti-Mafia documentation, according to the provisions contained in Articles 1 and 2 of Law no. 136 of 13 August 2010.

(14) This is a certification stating the existence or non-existence of one of the hypotheses of withdrawal, suspension or prohibition provided in Article 67.

(15) In addition to the contents of the communication, it states the attempt of Mafia infiltration aiming to determine the choices of the companies taking part in a public tender.

organisations, jointly with concrete elements from which it emerges that the entrepreneurial activity could, even only in an indirect way, facilitate criminal activities or could simply be influenced by it, as well as from the assessment of the violation of the duties of tracing financial cash flows.

The fifth paragraph of the same Article provides that the competent prefect should also extend these assessments to individuals who could determine in any way the choices or the direction of the business and, for those enterprises that have been created abroad and that do not have an office in Italy, the assessments are made on those individuals who exercise managerial, representative or directorial powers.

The discipline provided on this subject expresses a very significant trend against corruption, even if some aspects, mainly related to the means according to which it is exercised by the Prefects, remain unclear.

The main problems are related to the balance between the need to combat the Mafia and the freedom of the individuals involved. A balance that becomes quite hard to maintain with reference to the concept of “attempt of Mafia infiltration”, an attempt that usually consists of various elements such as personal relationships with individuals who are connected with Mafia organisations.

Apart from the difficulty of defining the concept of “personal relationship”, it is absolutely evident that in some smaller localised settings it is almost impossible to avoid people who are directly or indirectly connected with Mafia organisations, but this does not necessarily mean that the entrepreneur and his/her company are connected with or form part of a Mafia organisation. While the assessment should be carried out not on the basis (or at least not only on this) of the personal elements, but on some more objective data, such as funding, selection of employees, distribution of revenues, selection of suppliers, so to guarantee that the anti-Mafia information – mainly in the lights of the consequences that derive from them, and of the length of their judicial review – would provide a snapshot of the exact situation mainly in the light of the consequences that it has on the fundamental (economic) rights of the company and the individuals involved.

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